Comments

of the

National Consumer Law Center (on behalf of its low-income clients)

on

Loan Guaranty: COVID-19 Veterans Assistance Partial Claim Payment Program

85 FR 79142

RIN 2900-AR05

Document Number: 2020-26964

Submitted January 8, 2021

On behalf of our low-income clients, the National Consumer Law Center[1] writes to express serious concerns with the Department of Veterans Affairs' proposed COVID-19 Veterans Assistance Partial Claim Payment program (COVID-VAPCP).[2] VA-guaranteed borrowers who have recovered from COVID-19 hardships and can resume their pre-hardship payment need access to affordable plans that will bring their loans current and also support the VA's loan fund. We appreciate the agency's efforts to design relief. The VA's proposed COVID-VAPCP option, however, will not meet the agency's goals because the program will result in significant monthly payment increases for VA-guaranteed borrowers. We know from the previous financial crisis that such increases will cause substantial and unnecessary mortgage re-defaults and foreclosures.

Instead of finalizing the proposal, the VA should revise it to create a partial claim program similar to FHA's COVID-19 Standalone Partial Claim, as outlined in FHA Mortgagee Letter 2020-22. FHA's partial claim program allows borrowers with the ability to afford their pre-hardship mortgage payments to resume them instead of facing increased payments. In addition, under FHA's system, borrowers can access the partial claim in a streamlined fashioned and avoid significant barriers to assistance that plagued borrowers in the previous crisis.

Given the devastating economic consequences from the pandemic, a streamlined, affordable foreclosure alternative is necessary to avoid further economic harm. It is particularly important for borrowers of color who have faced the worst of the pandemic and who rely significantly on the VA-guaranteed loan program.

1. The VA's proposed COVID-VAPCP imposes significant payment shock on borrowers and requires submission of burdensome documentation.

If finalized, the VA's proposed COVID-VAPCP loan will cause substantial increases in borrowers' monthly payments after five years due to the structure of the agency's proposal. Based on previous experience with loss mitigation programs, relief options that provide for payment increases lead to significant redefault and foreclosures.

a. The VA's proposal will lead to increased monthly payments and, as a result, unnecessary foreclosures.

Under the proposed COVID-VAPCP, the VA would lend money to borrowers to bring their loans current after borrowers recover from COVID hardships.[3] Borrowers would access the partial claim loans through their mortgage servicers who evaluate financial information that borrowers submit. These partial claim loans would be capped at 15% of the primary mortgage

[1] Since 1969, the nonprofit National Consumer Law Center® (NCLC®) has used its expertise in consumer law and energy policy to work for consumer justice and economic security for low-income and other disadvantaged people in the United States. NCLC's expertise includes policy analysis and advocacy; consumer law and energy publications; litigation; expert witness services, and training and advice for advocates. NCLC works with nonprofit and legal services organizations, private attorneys, policymakers, and federal and state government and courts across the nation to stop exploitative practices, help financially stressed families build and retain wealth, and advance economic fairness. These comments were written by NCLC Staff Attorneys Steve Sharpe and Alys Cohen. For further discussion, please contact Steve Sharpe at ssharpe@nclc.org.

[2] We also have submitted a joint brief comment letter with a broad range of other consumer and industry groups.

[3] *See* proposed 38 C.F.R. 36.4806.

balance, would accrue interest at 1% per annum, and would be secured by mortgages on the borrowers' property. Borrowers would be required to repay the COVID-VAPCP loan within ten years; however, payments would not be required for the first five years of the loan. As a result, borrowers would have to pay off the loan in the second five-year period, including the interest that accrued from the first five years.

It is the condensed, five-year repayment term that will cause the significant payment increases for borrowers. The example the VA uses in the Federal Register shows how significant the payment increase could be in a very routine case:

> Take, for example, a veteran who enters a CARES Act forbearance with 300 monthly payments remaining and an unpaid principal balance of $239,450. Given a total monthly payment of $1,587.83, at the end of a 12-month forbearance period, the veteran would owe $19,054 in missed guaranteed loan payments. A loan modification at the same interest rate and a new 30-year term would result in a $26 decrease in monthly loan payments but $39,518 in additional interest over the life of the guaranteed loan. **Conversely, a VA partial claim payment would result in a $341.58 per month payment to VA in years 6 through 10** but only $1,441 in additional interest over the life of the guaranteed loan.[4]

The VA's example reflects a monthly mortgage payment increase of over 20% during the five-year repayment period, and the data on mortgage forbearance indicate that such increases will be common as a result of the large past due balances prevalent with borrowers facing COVID hardships. According to December data from the Mortgage Bankers Association, approximately 78% of all mortgage borrowers exiting their first six-month forbearance plans shifted into extended forbearance periods.[5] The trend toward extended forbearance periods will result in larger past due amounts that the borrower must address. By requiring borrowers to pay these over a relatively short period of time, borrowers' payment obligations will increase substantially.

Analyses of previous loss mitigation programs show that meaningful payment decreases are essential to avoiding redefault. The Department of Treasury's retrospective discussion of loss mitigation programs during the last financial crisis focused on the need to ensure payment reduction. According to *Guiding Principles for the Future of Loss Mitigation: How the Lessons Learned From the Financial Crisis Can Influence the Path Forward*, "[t]he data show that greater payment reduction can reduce the chance of re-default and ensure that homeowners have sustainable outcomes."[6] The Office of Comptroller of Currency made a similar conclusion in its metrics reports. "Among modifications that reduce borrowers' monthly payments, modifications that reduce payments by at least 10 percent consistently re-default at lower rates than modifications that reduce payments by less than 10 percent—the larger the reduction in monthly

---

[4] *See* 85 Fed. Reg. at 79148 (emphasis added).
[5] *See* Paul Centopani, *Forbearance rate resumes decline after upward movement*, National Mortgage News (Dec. 14, 2020).
[6] U.S. Dept. Treasury, *Guiding Principles for the Future of Loss Mitigation: How the Lessons Learned From the Financial Crisis Can Influence the Path Forward* at 13 (July 25, 2016), https://www.treasury.gov/press-center/press-releases/Documents/guiding-principles-future-of-loss-mitigation.pdf.

payment, the lower the subsequent re-default rate."[7] Accordingly, a program that increases payments for borrowers who have faced a hardship moves in the wrong direction.

FHA's experience shows how payment increases are harmful. FHA analysis of its modification program at the beginning of the previous financial crisis confirmed that payment increases did not lead to a successful program. In 2009, FHA determined that a revamp of its modification system was necessary because the former loss mitigation system provided borrowers with higher payments. According to HUD, "[r]ecent industry studies of these loan modifications revealed that borrowers who experienced an increased mortgage payment on a modified loan had a significantly higher re-default rate than borrowers whose loan modification provided a lower payment."[8] In order to improve outcomes, HUD changed the terms of its modifications to ensure long-term payment reductions.

In addition to significantly higher payments, the VA's proposal will also lead to payment shock due to the fact that borrowers will not make additional payments for the first five years of the loan only to face a steep increase starting in year six. The steep increase will push many borrowers over the edge financially and lead to default.

b. VA's proposal also suffers from unnecessary documentation requirements.

Imposing burdensome financial documentation requirements, as the VA includes in its proposal, will also create impediments to affordable loss mitigation options.[9] While having in-depth financial analysis on individual borrowers could help determine who could make increased payments, having such a process imposes significant barriers to access. The VA's proposed regulation imposes such burdens without also providing specific guidance to ensure that the servicer properly assesses affordability. The VA has essentially established extensive documentation requirements in response to its proposed payment shock approach and then has failed to explain to servicers how they can ensure that a borrower will be able to afford such payments five years in the future.

Instead the VA should offer a streamlined option in line with the other federal agencies. We are in the midst of a financial crisis with significant levels of default. Imposing substantial documentation requirements, let alone requirements sufficient to determine whether a borrower can afford a payment increase five years from now, runs contrary to what is needed.

2. Rather than finalize its proposal, the VA should adopt a partial claim program modeled on FHA's Standalone Partial Claim.

The VA has a model available on how to develop a partial claim option for VA borrowers who can afford to resume their former monthly payments– the FHA's COVID-19 Standalone Partial Claim. The FHA's partial claim program does not involve increases to borrowers' monthly

[7] OCC, Mortgage Metrics Report 3rd Quarter 37 (Dec. 2015), https://www.occ.gov/publications-and-resources/publications/mortgage-metrics-reports/files/pub-mortgage-metrics-q3-2015.pdf. .

[8] U.S. Dept. Housing and Urban Dev., Mortgagee Letter 2009-35 (Sept. 23, 2009), https://www.hud.gov/program_offices/administration/hudclips/sfhsuperseded/mltrs_full.

[9] *See* proposed 38 C.F.R. 36.4803(e).

payments, and it can be offered up front on a streamlined basis without the need for servicers to collect detailed financial documentation. The VA should adopt these features of the FHA partial claim program and avoid the payment shock its program involves.

Like the VA's proposal, FHA's COVID Standalone Partial Claim program allows borrowers to bring their loans current through a subordinate mortgage loan from HUD.[10] Unlike the VA's system, FHA's partial claim does not accrue interest and does not require payment within 120 months of the loan. Instead, FHA generally requires full payment of the loan by the earlier of the end of the primary mortgage's term or when the primary mortgage is paid off. In addition, the FHA's partial claim program can be offered without detailed financial information, which is required under the VA's proposal.

The VA should align itself with FHA's partial claim program in order to improve loan performance, which will benefit borrowers, servicers, and the VA. The repayment terms of FHA's partial claim avoid substantial payment increases and payment shock. Borrowers are allowed to resume payments and have time to plan for repayment of the 0% interest loan from HUD. Because it can be offered on a streamlined basis, the FHA partial claim program avoids the significant impediments to relief that can come from the need to collect detailed financial documentation (even though such documentation may be warranted for certain other loss mitigation products).

VA has identified no statutory impediments to aligning its proposed partial claim with FHA's.[11] Its statutory analysis concluded that it could operate a partial claim program through its loan refund authority and the broad powers it is granted under 38 U.S.C. § 3720. According to its proposal, "[i]n applying the authorities as a consistent, coherent framework, VA would, by way of a loan to the veteran, purchase from the servicer the veteran's CARES Act indebtedness and establish repayment terms favorable to the veteran, while leaving intact the veteran's guaranteed loan."[12]

Given that the VA can establish repayment terms of the partial claim and given that the statutes it identified do not mandate particular payment terms, the VA can modify the repayment terms that it proposed and align them with the FHA's program. By doing so, it can avoid the payment shock while meeting its statutory obligations.

3. In creating an affordable partial claim program that the VA implements, the VA should eliminate rules that unnecessarily limit the partial claim's effectiveness.

a. VA should eliminate the September 9, 2021 cutoff for partial claim payments.

In implementing an affordable partial claim program, the VA should eliminate its September 9, 2021 deadline for servicers to submit partial claim packages to the agency and should instead allow an affordable program to continue as long as the country continues to struggle with the

[10] U.S. Dept. of Housing and Urban Dev., Mortgagee Letter 2020-22 (July 8, 2020), https://www.hud.gov/sites/dfiles/OCHCO/documents/20-22hsgml.pdf.
[11] 85 Fed. Reg. at 79146.
[12] *Id.*

pandemic. The VA's proposal simply stated that the agency will stop taking claim payments by the September deadline. While the agency claimed its position was in some way tied to the anniversary of the COVID emergency declaration, it provided no meaningful explanation of how the emergency declaration date was tied to the cutoff for receiving claims.[13]

In fact, the VA's deadline for receiving claims will arbitrarily eliminate a post-forbearance option for borrowers who will still be in forbearance as of September 2021. Consistent with other agencies, VA Circular 26-20-12 allows for borrowers to be in forbearance as of that date. Given the persistence of the pandemic and the continued economic destruction it is causing, the need for forbearance into 2021 is high. As of December 29, 2020, there were 1.1 million government-insured borrowers in forbearance.[14]

Given that VA borrowers will still be in forbearance as of September 2021, the agency should remove its arbitrary cutoff.

b. The VA should not implement a partial claim that serves as a "last resort" for borrowers.

Instead of creating a "last resort" partial claim, the VA should create an affordable partial claim system that borrowers can access as part of the loss mitigation waterfall.[15] Because the VA sees the proposed partial claim as a last resort, it will only be offered once a full evaluation of all options is completed. This requirement makes accessing the partial claim difficult and dependent upon a financial analysis. Instead, VA should follow FHA's lead and offer borrowers facing a COVID the option of a partial claim (one without a payment increase) on a streamlined basis, which FHA offers borrowers as the first step in its waterfall of foreclosure alternatives. This will allow borrowers in a pandemic to access relief efficiently.

4. In any partial claim program that the VA implements, the agency should require servicers to include escrow portions of unpaid payments in the claim.

As discussed above, the VA's partial claim program should allow borrowers who can afford to resume their pre-hardship mortgage payments the option of resuming them. This will not happen, however, if the partial claim does not include the full amount of the tax and insurance portions of unpaid payments and instead only includes amounts actually paid by the servicer at the time of the claim. A partial claim that only includes amounts actually paid out of the account will cause an escrow shortage, and as a result, an increased mortgage payment.

Such an increased mortgage payment can be avoided if the VA requires servicers to include unpaid monthly escrow payments along with unpaid principal and interest payments in the partial claim regardless of what the servicer has actually disbursed. This prevents an avoidable escrow shortage because it includes the money needed to address future disbursements. This policy is consistent with FHA's policy for the COVID Standalone Partial Claim, which states

---

[13] 85 Fed. Reg. at 79152-79153.
[14] *See* Paul Centopani, *Forbearances Climb for Third Week in a Rrow*, National Mortgage News (Jan. 4, 2021).
[15] *See* proposed 38 C.F.R. § 36.4804.

that “the COVID-19 Standalone Partial Claim amount includes only arrearages, which consists of Principal, Interest, Taxes, and Insurance (PITI).”[16]

5. Conclusion

The VA should not finalize its COVID-VAPCP because it will result in payment shock to borrowers that will lead to unnecessary redefaults and foreclosures. Moreover, the VA’s proposal makes relief too difficult to access for borrowers facing pandemic hardships. Instead, the VA has the statutory authority to adopt a partial claim program like FHA’s, which will allow borrowers to resume their pre-hardship payments on a streamlined basis. The VA should adopt a model like FHA’s in order to best serve its borrowers.

[16] U.S. Dept. of Housing and Urban Dev., Mortgagee Letter 2020-22 (July 8, 2020), https://www.hud.gov/sites/dfiles/OCHCO/documents/20-22hsgml.pdf.