

Summary of H.R. 5579, The Emergency Loan Modification Act of 2008

A

complex mix of circumstances has made it difficult for struggling borrowers to restructure or refinance their mortgages. One of the reasons given for the slow pace of loan modifications is that some mortgage servicers are fearful of incurring legal liability to investors in pools of mortgage-backed securities. While servicers have been trying to work with borrowers under a variety of initiatives to avoid foreclosures, many of these efforts have been in the form of temporary repayment plans that may not provide the long-term stability needed by borrowers, investors or the markets.

To address this problem, Reps.

Paul E. Kanjorski (D-PA) and Michael N. Castle (R-DE) have sponsored H.R. 5579, the Emergency Loan Modification Act of 2008. H.R. 5579 clarifies certain responsibilities of and provides a safe harbor from legal liability for mortgage servicers who engage in specified loan modifications and workouts. More specifically, H.R. 5579 establishes that servicers must maximize recovery of proceeds from pooled loans for the benefit of the investors as a whole. It clarifies that a servicer is acting in the best interest of all investors if it engages in loss mitigation efforts, including accepting a short payment or short sale, or enters into a loan modification or workout plan for a loan that is in default or for which default is imminent or reasonably foreseeable, and the value to be realized would be greater than the value to be realized through foreclosure. Lastly, H.R. 5579 provides a safe harbor for servicers that meet this duty if the modifications remain in place for at least five years, do not establish repayment schedules that result in negative amortization, and do not require the borrower to pay additional points and fees.

Advocates of this bipartisan legislation believe that it will clear the way for servicers to initiate the kind of long-term sustainable loan modifications that will help to avoid costly foreclosures, thereby benefiting homeowners, lenders, investors, and entire communities. They note that the bill's provisions are consistent with and do not abrogate existing contractual obligations, and that it will remove disincentives to working out loans before they go into default.

It is expected that the Castle-Kanjorski bill will be rolled into a larger legislative package scheduled to come to the House floor on Wednesday, May 7th. Other elements of that package could include GSE and FHA reform proposals similar to those that passed the House last year, the Frank bill (H.R. 5830), and a tax measure passed by the House Ways and Means Committee.