



Statement of

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Senator Reed, Ranking Member Shelby and members of the committee, my name is Edgar Bright and I am President of Standard Mortgage Corporation in New Orleans. I also serve on the Residential Board of Governors of the Mortgage Bankers Association (MBA), the national trade association for the real estate finance industry, and am testifying on its behalf today.¹

It has been two years since Hurricanes Katrina and Rita made landfall. The events of August and September 2005 are still vividly etched into my mind, and the aftermath of those storms is still apparent everywhere you turn, especially in my home town of New Orleans, which suffered the most significant losses.

Immediately after Katrina hit, we began to assess our mortgage loan portfolio and instituted a policy of forbearance on all loans in the Katrina area. The entire real estate finance industry quickly followed suit. Many homeowners continue to receive forbearance on their loans more than two years after Katrina. Our forbearance policies have worked. Data collected and released by the MBA show that immediately after the storm, at the end of the fourth quarter of 2005, there were nearly 50,000 loans over 90 days past due in Louisiana. By June 2007, that number had fallen to fewer than 10,000, and foreclosures were initiated on fewer than 2,600 properties in the state up to that point in 2007, with most of these located outside the storm area.² For comparison purposes, in the first quarter of 2003, long before the storm, about 4,000 loans were over 90 days past due and there were about 2,000 new foreclosures. The comparable figures for Mississippi are: over 18,000 loans were 90 or more days past due in the fourth quarter of 2005. That number dropped to approximately 6,200 by June 2007. In the second quarter of 2007, foreclosure began on less than 1,700 properties in Mississippi. In the first quarter of 2003 about 2,000 loans were at least 90 days past due, and there were about 800 new foreclosures in Mississippi.

While the industry continues to offer forbearance from foreclosure to homeowners who are expecting Road Home³ funds, a serious issue is developing. It is our understanding that The Road Home program will be out of funds by the end of October. To date, less than 50 percent of eligible homeowners have received Road Home assistance, that translates to over 50 percent of families whose applications are pending or who have

¹ The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 500,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 3,000 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

² "Foreclosure begun" means the loans have started the process of foreclosure but have not been sold at foreclosure sale. Loans are classified "in foreclosure" according to investors' or local requirements. Investor standards define "in foreclosure" as meaning the loan has been referred to a foreclosure attorney or first legal action has occurred. Mortgage Bankers Association, *National Delinquency Survey*.

³ The Road Home program is the largest single housing recovery program in U.S. history. The program's objective is to help Louisiana residents get back into a home or apartment as quickly and fairly as possible. For more information, see <http://www.road2la.org/>.

obtained commitments from The Road Home will not receive funds unless additional federal assistance is provided. Clearly failing to get such a significant number of homeowners the funds necessary to rebuild their homes or sell their properties to the state will mean that communities will not recover. We therefore strongly support S. 1668, The Gulf Coast Housing Recovery Act of 2007, which, among other things, authorizes funds to cover the shortfall that exists in The Road Home program.

Suggested Improvements or Additions to S. 1668

Our experience with these storms and their aftermath has given us a template for action in the event of another catastrophe. While the homeownership segment of this tragedy was better addressed than many other parts in the response to the storm, there are significant lessons that can be learned. Congress and federal regulators should act now to resolve the following issues before another big storm hits the U.S.

A. Environmental Assessments

In Section 105, S. 1668 provides a beneficial provision that if a federal agency performs an environmental review, the review is considered sufficient for receipt and use of all federal funds. We believe this provision is well-intentioned and has great potential to avoid significant delays in responding to large natural catastrophes. However, it is unclear exactly how this will apply to the Community Development Block Grant (CDBG) program. Moreover, this provision fails to strengthen or clarify the application of existing exemptions to avoid environmental reviews altogether.

MBA found the environmental reviews or assessments required by the National Environmental Policy Act (NEPA) as one of the greatest challenges when working with the states in their development of plans to implement the disbursement of CDBG funds. NEPA effectively hamstrung the states as to how they could design their grant programs. NEPA requires “every federal agency evaluate the potential environmental impacts of major federal actions significantly affecting the quality of the human environment.”⁴ CDBG grants are subject to NEPA and other environmental laws contained therein, including historic preservation, floodplain management and wetland protection, coastal zone management, sole source aquifers, endangered species, wild and scenic rivers, air quality, farmland protection, HUD environmental criteria and standards and environmental justice.

According to HUD, HUD or its “designee” (the state) cannot specify the use of CDBG funds specifically for rebuilding, for example, without performing environmental assessments on each and every property indicating any impact of rebuilding (the “federal action”) on historic preservation, floodplain management and wetland protection, coastal zone management, sole source aquifers, endangered species, wild and scenic rivers, air quality, farmland protection, HUD environmental criteria and standards and environmental justice. NEPA, however, provides exemptions from this general policy in the event of a natural disaster. Such exemptions should have been

⁴ (42 U.S.C. § 4332(2)(C))

considered and adopted by HUD in its review of state plans, but were not. Instead of invoking the exemption, HUD determined that it could avoid NEPA if no controls or rebuilding requirements were placed on the funds.

Given the significant ramifications of the HUD policy, the industry imposed certain private controls over the use of funds as a condition to subordinating its interest to The Road Home covenant. The process of establishing repair escrows ensured funds selected for home repair were used for that purpose. Unfortunately, those controls were eliminated when HUD failed to understand the private nature of these actions and demanded the state revise its plan. The state was left with no other choice but to provide funds directly to homeowners with no strings attached. We continue to think this is bad public policy and substantially increases the likelihood that funds dedicated to the State of Louisiana are not being used for their intended purpose or are not remaining in the state.

It is important to note the industry does not want to “police” the use of federal funds. That should be the role of the government. However, confusion over NEPA made any government-imposed controls nearly impossible. To correct this situation, we believe Congress should clarify existing NEPA exemptions and require HUD and other government agencies or their designees avail themselves of NEPA exemptions when such actions would protect the interests of the federal government. Alternatively, Congress could create a mechanism to allow the President of the United States or another appropriate government entity to “activate” the NEPA exemptions and exclusions or otherwise waive NEPA for the purpose of rebuilding pre-existing housing after a disaster.

B. Treatment of Federal Housing Administration (FHA) Non-Conveyable Properties

One of the biggest challenges the real estate finance industry faces is FHA’s current policy not to pay insurance claims on single-family properties when those properties are damaged. In general, FHA pays an insurance claim when it takes title (conveyance) to a property as a result of foreclosure. The amount of the claim is 100 percent of the outstanding principal balance plus reimbursable interest and expenses. However, if the property is damaged due to fire, flood, earthquake, tornado or hurricane (or the lender’s failure to preserve and protect), FHA will not pay a claim or take title to the property unless the property is repaired. This policy effectively renders the loan uninsured.

This policy is extremely damaging to the mortgage lending and servicing industry, especially those companies with a high concentration of loans in the hurricanes’ hardest hit areas and who have extended forbearance for over two years. Servicers should not have to take principal losses on FHA-insured loans when servicers are following federal flood insurance laws and FHA requirements. This policy has made FHA lending and servicing very unattractive in the Gulf States.

To exacerbate matters, in distributing the CDBG funds, HUD forced the State of Louisiana to terminate its original Road Home plan that recognized servicers' rights to establish repair escrows. Such repair escrows ensured grant funds would have been used to repair the collateral when the "repair/rebuild" grant option was selected by the borrower. The original plan would have reduced the number of damaged "conveyances" servicers now face.

Given the grave situation of uninsured losses on FHA loans, MBA supports S. 1668, which provides fairness to lenders in connection with Katrina- or Rita-damaged or destroyed homes financed with an FHA-insured loan. Specifically, the bill provides, in connection with Rita and Katrina, if there was no failure on the part of the mortgagee or servicer to provide hazard or flood insurance for the property in accordance with federal law and requirements, the Secretary of HUD:

- may not deny conveyance of title to the property to the Secretary and payment of the benefits of such insurance on the basis of the condition of the property or any failure to repair the property;
- may not reduce the amount of such insurance benefits to take into consideration any costs of repairing the property; and
- with respect to a property that is destroyed, condemned, demolished, or otherwise not available for conveyance of title, may pay the full benefits of such insurance to the mortgagee notwithstanding that such title is not conveyed.

Without a change in existing FHA policies, lenders and servicers are faced with significant uninsured losses. These losses are straining the already tight financial resources of mortgage lenders and restricting their ability to forebear and lend in these communities.

C. FHA Multifamily Insurance

In redeveloping affordable rental housing in the Gulf Coast states, FHA insurance has become an important component of financing both new construction and rehabilitation of properties. Particularly in the current environment of market uncertainty, the ability of FHA insurance and Ginnie Mae mortgage backed securities (MBS) to access the capital markets is critical to assuring affordable financing. Issues have arisen, however, with FHA's environmental standards which are significantly more restrictive than those of the Environmental Protection Agency (EPA) and the state agencies administering environmental policies. FHA's additional requirements are preventing much-needed housing from moving forward. We recommend that a provision be added to S. 1668 which would prohibit FHA from adding requirements that are above and beyond those determined acceptable by EPA and the appropriate state department of environmental quality. Certainly, the environmental professionals at EPA and state agencies administering environmental policies are well-qualified to determine what standards should be set to assure a property is safe for rental housing and that all environmental issues are appropriately mitigated. FHA should not be unnecessarily hindering the production of multifamily housing through the imposition of excessive requirements.

D. Duplication of Benefits

S. 1668 waives the current duplication of benefits problem with regard to Small Business Administration (SBA) loans and Federal Emergency Management Agency (FEMA) disaster assistance, provided there are no windfall profits. MBA fully supports this provision.

One of the continuing obstacles homeowners face is receiving the proper amount of funding to make the necessary property repairs. Under the Stafford Disaster Relief and Emergency Assistance Act,⁵ federal agencies are not permitted to give recipients of federal assistance duplicate benefits. While in theory this statutory requirement makes sense, in practice, with this particular disaster, it is causing some deficiencies in funding.

In the case of residential homeowners, duplicate benefits are those federal benefits obtained by homeowners for the same purpose as those provided by another source, i.e., private insurance, FEMA, or SBA benefits to repair the home. As an example, a “duplication of benefit” will occur when CDBG funds, combined with a SBA loan for structural repair (and other sources of funds for repair), exceed the SBA’s estimate of damage. Unfortunately comparing the SBA loan and a CDBG grant is like comparing apples to oranges because they use different valuations of damage and often cover different damaged items. This situation results in the state paying on the SBA loan with CDBG grant funds, but it leaves the homeowner with insufficient funds to repair the property. In many situations, homeowners were awarded CDBG grants or a Road Home grant, but received no funds or had significant deductions because the money went to pay down another government loan or pay back grants. While paying down SBA loans with grant funds can be advantageous if all property repairs are completed, it is problematic when CDBG money is still needed to complete the rebuilding. Likewise, repayment of FEMA grants should not be triggered upon mere receipt of CDBG funds. Moreover, given the SBA loan is a liability, rather than an asset, eliminating SBA loans from the duplication of benefits calculation makes good sense.

E. Coordinate Valuations Among All Government Entities

As was the case after Katrina, valuations and appraisals of damaged properties after natural disasters are often conducted numerous times by numerous agencies. There should be some mechanism to share this information among agencies. Coordination among all government agencies, and with the private sector, would significantly reduce the number of valuations being performed, thus saving taxpayers money and speeding up delivery of disaster assistance. One component that is critical to achieving this objective is a common electronic language that ensures data is entered and stored

⁵ 42 USC 5155

consistently, and with the same definitions by all, so that computers “can talk to each other” and data can be sorted and manipulated as desired.

F. VA No-bids

Unlike FHA, the Department of Veterans Affairs’ (VA) Loan Guaranty Program does not provide 100 percent insurance against default losses. The VA is unique in passing risk of declining market prices to servicers because it provides only a limited guaranty. The guaranty varies, but generally covers 25 percent of the original loan balance. In the event of a liquidation sale (i.e., foreclosure), the VA uses a statutory formula to determine if it will pay only the guaranty or pay the servicer the outstanding debt (called “total indebtedness”) and take title to the property. When the latter occurs, the VA sells the real estate owned to recoup the amount paid to the servicer.

When the former occurs and the VA determines not to take title to the property, it will issue a “no-bid” advice letter. A no-bid occurs, by statute, when the net value (fair market value minus a statutory VA “holding cost” factor) is less than the un-guaranteed portion of the total indebtedness (unpaid principal balance, allowable interest and advances less any credits). When this occurs, VA will pay the amount of the guaranty, but will not take title to the property. The servicer thus takes any loss after the resale of the property. These losses can be substantial, and in the wake of Hurricane Katrina, could be catastrophic.

Most VA loans are in Ginnie Mae MBS and, thus, servicers do not get the benefit of the principal and interest payments. The principal and interest is passed through to security holders, who are protected 100 percent against principal loss by Ginnie Mae’s guaranty. The servicer takes the principal, interest and even out-of-pocket loss exposure to a large degree, despite the fact that they receive only a small administration fee per loan as income. Servicers are not equipped nor are they compensated to absorb catastrophic principal, interest and other losses.

In an effort to provide the VA with flexibility in this area and to assist mortgage companies in containing total losses, we ask Congress to consider providing the VA authority to waive the statutory requirement to declare no-bids. We ask that VA be permitted to take conveyance to a property and pay the total indebtedness and out-of-pocket expenses in cases of federally declared disaster areas without having to abide by the no-bid calculation. We also suggest allowing the VA to pay a claim even when conveyance does not occur due to unique circumstances, such as a declaration of hazardous waste contamination on the property.

We believe, by making the necessary statutory changes to these programs, the VA will have more comprehensive authority to manage the issue of damaged properties and claims after a catastrophic disaster. The changes will demonstrate the federal government’s commitment to the VA program. Without these changes, many lenders are likely to abandon these products as foreclosure losses begin to mount, thus

affecting the future viability of programs specifically designed to assist low- to moderate-income veterans and their families.

Conclusion

We applaud Senators Dodd and Landrieu for their introduction of S. 1668. Enactment of this bill, with the modifications discussed in this statement, would be an important step to provide the tools to ensure recovery in Louisiana and other local economies affected by Hurricanes Rita and Katrina. Housing is the cornerstone to rebuilding neighborhoods and communities. I commend this Committee's attention to it.

MBA appreciates the opportunity to testify today and offer our thoughts and considerations as you monitor the recovery and deliberate S. 1668. We look forward to working with you on this important legislation.