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Plan to Encourage Banks to Allow Short Sales

U.S. to Give Lenders Incentives for Avoiding Foreclosures

By Renae Merle

Washington Post Staff Writer

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Banks could get government incentive payments for allowing borrowers to sell their home at a loss rather than go through foreclosure, under new guidelines issued yesterday for the Obama administration's \$75 billion housing plan.

The program, known as Making Home Affordable, focuses on paying lenders to modify distressed borrowers' loans to affordable levels. But under this expansion of the program, lenders can also receive incentive payments even if the homeowner's loan is not modified.

In those cases, the lender could get up to \$1,000 for allowing a short sale. In such deals, the lender accepts less than the value of the mortgage in what has usually been a time-consuming and cumbersome process. Under the plan, the government will also share the cost of extinguishing second liens on the property, such as those for second mortgages.

If the short sale fails, the borrower can turn over their house keys in a process known as "deed in lieu of foreclosure," transferring ownership to the lender without a foreclosure. At the end of the process, the homeowner could be eligible for \$1,500 for relocation expenses.

"If a modification is not possible, we are also announcing steps to encourage the quick private sale or voluntary transfer of property, which will save homeowners money and protect their financial future," Treasury Secretary Timothy F. Geithner said. "These are critical steps in stemming the foreclosure crisis and stabilizing the housing market."

The additions to the program are an acknowledgement by government officials that not all distressed borrowers will be able to save their homes. Despite government efforts, lenders are starting the foreclosure process on an increasing number of homes. And the country's growing unemployment rate is putting more people at risk, government officials have said.

"We're not going to solve all problems, and this won't benefit all homeowners," Geithner said.

The program's expansion also includes a \$10 billion feature that protects lenders from losses associated with falling home prices. If a lender modifies a loan and the homeowner redefaults, the lender faces more severe losses if home prices have fallen in the interim.

The new incentive will encourage loan modifications in places where home values have dropped severely, according to a summary of the program. It reduces "the risk of loss to lenders from modifications compared to alternatives that could result in the loss of homeownership," the summary said.

The Obama administration launched its foreclosure prevention plan in March, and more than 50,000 homeowners have been offered lower-cost mortgages. Lenders representing 75 percent of U.S. mortgages have agreed to participate, according to administration officials.

But the program has been implemented unevenly throughout the financial services industry, with some lenders lagging. And demand from distressed homeowners has overwhelmed many lenders and nonprofit organizations.

"The enhancements today will help more borrowers avoid some of the financial damage caused by foreclosure," said John Taylor, president of the National Community Reinvestment Coalition. "We're encouraged by the early numbers, but more work remains to be done to compel lenders to fully participate in the program and to modify loans before they go into default and face imminent foreclosure."

Speaking alongside Geithner and Housing and Urban Development Secretary Shaun Donovan at a news conference touting the program's progress, Warren Rohn, 70, of California, said it had "saved my bacon."

Rohn had closed his trucking business late year after work dried up. In April, his lender sent him an application for the government program and lowered his interest rate to 2 percent. "Losing my trucking business was tough enough, but I'm not sure what I would have done if I lost my home," he said.