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What's Working and What Needs to Change For Mortgage Process -Urban Institute

Two Urban Institute (UI) researchers pose a pertinent question in a recent paper. Laurie Goodman and Aaron Klein ask, "What is the purpose of the Fed lowering short term rates to zero and buying hundreds of billions of mortgages to lower mortgage interest rates if people cannot functionally access a mortgage?"

They point out that the mortgage process, whether to purchase a home or refinance it, has a long to-do list including title searches, appraisals, applicant employment and income verification, notarization, closings, and recording of the transaction in county offices. If any of those items cannot be checked off, the ability to get a mortgage is jeopardized. With much of the world shut down in order to mitigate the COVID-19 pandemic, the entire process could be broken.

Given the massive losses of income and with the incentives of low interest rates and the large amounts of home equity built since the great recession, it is reasonable to assume the demand for cash-out refinances will rise. Any breakdown in the refinance process will limit households' ability to tap what may be their best source of funds to weather the crisis.

UI says the epidemic's impact will vary geographically; some areas and lenders have systems that can perform under the crisis conditions while others do not. "Even if many refinancings sail through the process, others will be stuck in an "inability to process" pile that grows ever larger the longer the pandemic lasts."

The paper lists fivepotential points of disruption in the refinancing process and suggests policy solutions for each:

Title Searches

A title search is necessary for any real estate transaction. Lenders require up to date information on ownership, and property encumbrances but, with many county assessor's offices shut down, information cannot be updated. In approximately 2,000 of the 3,600 municipal jurisdictions that record titles, information through the date of the shutdown can be searched online. There is exposure to risk from the date of the search to the point the new mortgage can be recorded but the authors point out that this is always true and gap insurance is normally included in the title insurance policy. Most title insurance carriers have extended the gap from 60 to 90 days, taking on the

National Average Mortgage Rates

	Rate	Change	Points
Mortgage News Daily			
30 Yr. Fixed	7.08%	-0.05	0.00
15 Yr. Fixed	6.45%	-0.02	0.00
30 Yr. FHA	6.55%	-0.05	0.00
30 Yr. Jumbo	7.25%	-0.04	0.00
5/1 ARM	7.07%	-0.03	0.00
Freddie Mac			
30 Yr. Fixed	6.86%	-0.01	0.00
15 Yr. Fixed	6.16%	+0.03	0.00
Mortgage Bankers Assoc.			
30 Yr. Fixed	7.03%	+0.09	0.62
15 Yr. Fixed	6.56%	+0.09	0.54
30 Yr. FHA	6.90%	+0.11	0.95
30 Yr. Jumbo	7.11%	-0.01	0.50
5/1 ARM	6.38%	+0.11	0.54

Rates as of: 7/3

Recent Housing Data

		Value	Change
Mortgage Apps	Jun 12	208.5	+15.58%
Building Permits	Mar	1.46M	-3.95%
Housing Starts	Mar	1.32M	-13.15%
New Home Sales	Mar	693K	+4.68%
Pending Home Sales	Feb	75.6	+1.75%
Existing Home Sales	Feb	3.97M	-0.75%

additional risk but even 90 days may be insufficient.

		Value	Change
Builder Confidence	Mar	51	+6.25%

Where electronic search capability is absent the problem is more significant. Those 1,500 jurisdictions are likely to be more rural and sparsely populated but still comprise close to 10 percent of potential refinancing. Where physical offices are closed, title searches cannot be completed nor can a borrower refinance.

UI suggests that one solution is to simply allow the prior title insurance policy to remain "en force" for both rate/term and cash out refinances closed during the "coronavirus period." The title company would bear a small amount of additional risk on their lender insurance for cash-out refinancing, but the logic is straightforward. The property is not changing hands and if the borrower attests there are no new liens there is little additional risk involved. The authors suggest that such a rule for refinancing outside the crisis also makes sense.

Verification of Employment

Verbal verification of employment, required for refinancing, can be difficult to obtain when so many employers are closed or hard to reach on the phone. Fannie Mae and Freddie Mac (the GSEs) are temporarily allowing email verification by the employer as well as use of a current pay stub or bank statement and for verification to be provided up to the time of loan delivery. UI says these are important steps and ones that probably should not be temporary.

However, lenders are also expected to verify continuity of income for their GSE loans and Goodman and Klein say this is a burden on lenders and one that may not be possible to achieve. This could result in the self-employed having difficulty getting refinancing.

One solution could be to cap the risk to lenders through representation and warranty relief. A better one would be to eliminate the requirement for a same GSE refinance as it would present no increase in risk to the company. The authors also suggest eliminating the requirement for cross GSE refinancing (Freddie to Fannie/Fannie to Freddie) as both companies are in the same conservatorship.

Appraisals

Getting a traditional appraisal is difficult right now. Borrowers are leery about allowing appraisers in their homes and appraisers feel the same about being there. The GSEs traditionally offer appraisal waivers for low LTV refinances under their automated underwriting systems and both appear to have expanded the LTV range for these waivers. They are also permitting exterior only appraisals for same company refinancings but still require traditional appraisals for cash-out or cross company refinances. This all but guarantees they cannot be completed.

This becomes crucial in the COVID situation where many families are facing substantial income losses and need to tap into their home equity. Congress recognized reality when writing the recent CARE act, temporarily eliminating the early withdrawal penalty from 401(k) and other retirement accounts. UI says similar temporary modifications to allow tapping into equity would be wise.

UI recommends extending waivers to all same and cross GSE refinancings including cash-out transactions. This would mean only a marginal increase in risk as the maximum LTV on cash-out loans is 80 percent. Enabling more such loans will allow households to tap into the $19.7 trillion of existing home equity, potentially allowing more people to keep current on their mortgages and reducing forbearances. It is important to act quickly as right now any borrower can get forbearance by stating they have a hardship, however, once they enter into forbearance, they are no longer eligible to refinance.

Closing

Closings are being affected as many buyers and sellers are unwilling to let a notary into their home to sign the necessary papers and many states do not allow e-notarizations. This is changing; last month New York State began allowing virtual notarization, bringing the total to 23 states.

UI recommends that more states should follow New York's lead or Congress could solve the problem simply by passing the SECURE Notarization Act. Moreover, using teleconferencing video systems (Zoom, Skype, BlueJeans) that record the proceedings can capture the closing and allow for the borrower and seller to be "present" if they choose.

Post-Closing

A final set of problems exist in jurisdictions, where mortgages cannot be recorded electronically. State and local governments may need to adapt more quickly to electronic filings, suspend the requirement until offices open, and ultimately consider whether this is a critical aspect of local government, and if so, how to provide it in a manner consistent with social distancing and medical safety.

Goodman and Klein urge the Federal Housing Finance Agency (FHFA) and the GSEs to "prioritize their social purpose over profitability." They say there is a strong case for a widespread streamlined refinancing program such as the post-2008 Home Affordable Refinance Program (HARP). It reduced payments for 3.4 million homeowners but, while other parts of the loss mitigation toolkit have grown stronger, streamlined refinances have all but disappeared. Fannie Mae's High LTV Refinance Option and Freddie Mac's Enhanced Relief Refinance Mortgage are extremely limited and most of today's refinancers are ineligible for them. Eliminating the minimum LTV on this program would be an excellent first step, as would restoring and expanding the streamlined refinance program to allow both cross and same GSE refinancings with no documentation.

The authors conclude that, addressing the new COVID challenges to refinancing and tapping home equity is critical to helping homeowners survive this recession. "Policy makers have to be careful not to assume business as normal when pushing macro-levers, such as interest rates, and focus critical attention on the micro-levers to ensure people are able to access a working housing refinancing market."