July 8, 2022

The Honorable Tina Smith
United States Senate
720 Hart Senate Office Building
Washington, D.C. 20510

The Honorable Mike Rounds
United States Senate
716 Hart Senate Office Building
Washington, DC 20510

Dear Senator Smith and Senator Rounds:

On behalf of our low-income clients, we provide four recommendations for improving the United States Department of Agriculture's (USDA) programs aimed at providing and sustaining affordable homeownership in rural areas. We appreciate the opportunity to make these proposals, and we look forward to further discussion.

The United States Department of Agriculture (USDA) operates two significant programs for financing the purchase or construction of single-family homes in rural areas in the United States through its Rural Development (RD) mission area. The agency serves as a lender under its Section 502 direct loan program and also acts as a guarantor of loans made by private lenders under its Section 502 guaranteed loan program. Almost one million households have USDA-guaranteed loans and over 200,000 households currently have direct loans.

USDA can help borrowers avoid unnecessary foreclosure, and thus stabilize rural housing, by adopting basic programs that are in place in other segments of the government-backed mortgage market. USDA direct loan borrowers should have meaningful access to moratorium (forbearance) relief and simple loan modifications, and they should not immediately lose access to these proven alternatives to foreclosure once a loan has been accelerated.[1] These changes would simply bring USDA in line with FHA's and VA's rules for loan servicers. With respect to the USDA-guaranteed program, we urge Congress to require the agency to provide reports and data regarding loan performance in line with what HUD provides for the FHA-insured loan program.

1. **USDA must make alternatives to foreclosure available for direct borrowers throughout the foreclosure process.**

RD offers a number of foreclosure avoidance options, generally referred to as "loss mitigation options," for borrowers in both the direct and guaranteed loan programs run into trouble making their mortgage payments. For borrowers in the guaranteed loan program, these options are available throughout the foreclosure process. However, RD has adopted a policy barring

[1] When a mortgage loan is accelerated the lender terminates the borrower's right to pay off the loan in monthly installments. Instead, the full loan balance becomes due immediately. Absent immediate payment of the entire loan balance, the lender can proceed to sell the home at a foreclosure sale.

borrowers in the direct loan program from accessing foreclosure avoidance options, which the agency labels as "special servicing," once it accelerates a loan.[2] This policy shortens the time for resolving delinquencies and leads to unnecessary losses – to the agency, the homeowner, and the homeowner's community.

Loan acceleration is an early step in a home foreclosure process that can take months or even years. After a loan is accelerated but before the foreclosure sale, a borrower may experience a positive change in financial circumstances or qualify for a plan to bring the loan current. Current RD policy bars homeowners in the direct loan program from accessing these options even when significant time remains before a foreclosure judgment or sale.

RD's policy barring homeowners in foreclosure from accessing options to prevent foreclosure is out of step with the rest of the mortgage market. FHA-insured borrowers, for example, may access loss mitigation until shortly before a foreclosure sale. The same is true for borrowers whose loans are held by Fannie Mae and Freddie Mac. RD guaranteed loan borrowers also have access to loss mitigation after acceleration.[3]

The Consumer Financial Protection Bureau's Real Estate Settlement Procedures Act (RESPA) regulations governing the loss mitigation process for all "federally related mortgage loans,"[4] including RD direct loans, require servicers to evaluate borrowers for all available loss mitigation options until a specified time prior to the foreclosure sale of the property.[5] These RESPA rules recognize that defaulting homeowners frequently do not seek help from housing counselors and other experienced advocates until after a loan has been accelerated and they learn that foreclosure proceedings have begun. RD's refusal to allow direct loan borrowers to access its major loss mitigation options after acceleration frustrates the goal of the RESPA rules, to prevent avoidable foreclosures. Meaningful loss mitigation options must remain available to homeowners throughout the foreclosure process.

RD's policy also clearly violates the statute that created moratorium relief for borrowers who have defaulted on their loans for reasons beyond their control. That statute applies "[d]uring any time such loan is outstanding. . . " and not only prior to acceleration.[6] In fact, in *United States v. Shields*,[7] a federal district court held that the agency's bar on post-acceleration moratorium relief violated the law because it is contrary to the moratorium statute. The agency nonetheless has continued a policy that is harmful to homeowners, costly to the government, contrary to the federal moratorium statute, and out of step with the rest of the mortgage market. This policy must be updated to make loss mitigation available to direct loan borrowers after acceleration.

[2] 7 C.F.R. 3550.211(h).
[3] USDA, Loss Mitigation Guide: Single Family Housing Guaranteed Loan Program 4, 11, 18 (April 2020), available at https://www.rd.usda.gov/files/3555-1chapter18.pdf.
[4] 12 U.S.C. § 2602(1)(B)(ii).
[5] 12 C.F.R. § 1024.41.
[6] 42 U.S.C. § 1475.
[7] 733 F. Supp. 776 (D. Vt. 1989).

2. **Direct loan borrowers who complete a moratorium should automatically receive affordable loan modification offers that address their post-moratorium income and financial situation.**

RD is statutorily authorized to grant moratoriums of up to two years on mortgage payments to borrowers who suffer financial hardships for reasons outside of their control.[8] By postponing the borrower's monthly mortgage payments, a moratorium provides significant relief to a borrower who is working through hardship. A moratorium does not, however, relieve a borrower of the obligation to repay the amounts that are deferred during the moratorium period.

Once a moratorium ends, it is almost always impossible for a borrower who is recovering from a financial hardship to pay all the deferred payments in a lump sum. This is particularly true for the low- and very low-income borrowers that the direct loan program serves. RD deals with this issue by offering only two options for non-emergency defaults, both of which are inadequate.[9] The first is forgiveness of the interest that has accrued during the moratorium, and the second is reamortization of the loan balance over the remaining term of the loan. The primary inadequacy of both of these options is that if either or even both are applied, the borrower's monthly post-moratorium mortgage payments will still always be greater than the pre-moratorium mortgage payments, creating a payment shock that financially vulnerable borrowers coming off a hardship can ill afford.[10]

To prevent borrowers from failing after a moratorium, RD must finally permit loan term extensions and interest rate reductions after a moratorium.[11] Fannie Mae, Freddie Mac, FHA, and even the RD-guaranteed programs use loan term extensions and interest rate reductions as part of the loan modification process. As a result, the borrower's payment often decreases rather than increases. Because homeowners who have faced a hardship generally continue to experience pronounced decreases in income, extending the loan term so that the homeowner's monthly payment can be reduced after a moratorium improves loan performance and home retention (and for homeowners who can resume previous payments the extension allows the payments to revert to pre-forbearance levels). RD must adopt a loan term extension and interest rate reduction policy for direct loan borrowers. Such a change will help borrowers retain their homes and will improve the financial stability of the RD direct loan program.

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[8] 42 U.S.C. § 1475.

[9] Borrowers with COVID hardships may also have access to streamlined refinancing; however, the availability of this option is tied to the national emergency and is not part of the agency's permanent loss mitigation protocols.

[10] The forgiveness of interest accrued during a moratorium has also been ineffective because borrowers have not been informed of this option. RD has recently made what we believe to be its first statement of the standard for when to forgive interest in its February 7, 2022 final rule regarding direct loans. USDA, Direct Single Family Housing Loans and Grants Programs, 87 Fed. Reg. 6761 (Feb. 7, 2022). We appreciate that the agency will provide forgiveness of interest based on an analysis of affordability, and we hope the rule is followed; however, as explained above forgiveness of interest in the past does not provide a substitute for a full modification that can address the affordability of future monthly payments.

[11] 7 C.F.R. 3550.208.

3. **USDA must provide direct loan borrowers meaningful access to moratorium relief consistent with the moratorium.**

Changes need to be made to the moratorium program regulations because they include arbitrary rules that exclude many direct loan borrowers who face financial hardships and qualify for this relief under the statute. The moratorium statute requires the agency to make moratorium decisions based on an individual borrowers' showing that he or she is unable to continue to make mortgage payments for reasons outside the borrower's control without unduly impairing the borrower's standard of living.[12] Under the current moratorium regulation, however, RD denies moratorium relief to direct loan borrowers unless they can demonstrate either a reduction of at least 20% in the borrower's own income in the past 12 months or that the borrower has incurred certain specified unexpected and unreimbursed expenses.[13] These regulatory rules bar relief if a borrower's income loss is less than 20% or occurred more than 12 months ago or when a household member other than the borrower, such as a non-borrowing spouse, experiences a reduction in income.

These limits on eligibility for a moratorium are arbitrary and inconsistent with the moratorium statute. For the low- and very low-income borrowers the direct loan program serves, budgetary margins are often so slim that a loss of income of even 5 or 10% can render a borrower unable to continue to make mortgage payments without unduly impairing the borrower's standard of living. Financial hardships that started more than a year ago can also continue to impair a borrower's ability to afford the mortgage, particularly if she has attempted to keep up with payments by using savings or borrowing elsewhere. Denying moratorium relief when a non-borrower household member loses income or incurs unexpected expenses also undermines the goals of the program. The failure to consider *household* income, as opposed to that of the borrower, may have made sense, at least for some families, in 1949 when the moratorium statute was enacted, but it does not hold up today when household composition is more fluid. If a borrower, after having secured the RD loan, marries, or forms a new household, adjustments are often made in each individual's household obligations, including who is the primary earner. Failing to incorporate the range of financial arrangements in a family and requiring the borrower to continue to make unaffordable payments because a spouse's or partner's loss of income will not qualify the household for a moratorium is unreasonable.

RD must update the moratorium regulation to ensure that direct loan borrowers who qualify for moratorium relief under the statute are not denied assistance.

4. **USDA should provide performance data and reporting in line with the information FHA provides for its insured loans.**

Stakeholders need basic performance data in order to better understand and comment on agency proposals. FHA currently provides a monthly Single-Family Loan Performance Trends Report that provides information on delinquency rates, borrowers who are seriously delinquent, and

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[12] 42 U.S.C. § 1475(a).
[13] 7 C.F.R. 3550.207(a).

borrowers in foreclosure, among other important data points.[14] FHA also provides an annual report to Congress, which provides significant detail on the health of the program.[15] Finally, HUD provides access to its Neighborhood Watch system, which gives raw data sortable by servicer and by region regarding loan performance.[16]

We are unaware of similar data reporting by the USDA regarding its guaranteed loan program. While we believe HUD could further improve its data reporting, USDA stakeholders would benefit from the agency implementing the steps HUD has already taken. Further, while we greatly appreciate the current administration's willingness to share this data when we have asked, it is no substitute for having a system in place that ensures everyone can access basic information about the program.

We believe these three proposals will improve USDA's efforts to provide and sustain homeownership in rural areas. We would appreciate any opportunity to further discuss these or other ideas. For any further discussion, please contact Steve Sharpe, National Consumer Law Center, ssharpe@nclc.org.

Sincerely,

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

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[14] FHA Single-Family Loan Performance Trends Report, available at https://www.hud.gov/program_offices/housing/hsgrroom/loanperformance.

[15] FHA, Annual Report to Congress Regarding the Financial Status of the FHA Mutual Mortgage Insurance Fund, https://www.hud.gov/fhammifrpt.

[16] FHA, Neighborhood Watch System, https://entp.hud.gov/sfnw/public/