Center for American Progress

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Is the FHA Distressed Asset Stabilization Program Meeting Its Goals?

By Sarah Edelman, Julia Gordon, and Aashna Desai September 2014

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Introduction and summary

In the summer of 2012, the Federal Housing Administration, or FHA, announced it was launching a new program to auction off pools of delinquent mortgages that had not yet gone through foreclosure but for which foreclosure was inevitable.[1]

According to FHA, selling these loans prior to foreclosure would save the agency money and provide a better financial outcome for taxpayers. Selling would also provide homeowners more options than were available under FHA rules due to statutory limitations, helping families and stabilizing neighborhoods.[2] In short, the Distressed Asset Stabilization Program, or DASP, "creates the opportunity for everyone—the homeowner, the new mortgage holder, FHA and the community—to walk away a winner."[3]

Since September 2012, FHA has made available for auction nearly 100,000 loans.[4] According to the Department of Housing and Urban Development's, or HUD's, new report on DASP outcomes, the program has helped reduce FHA's loss rates from 63.5 percent in the first quarter of 2010 to 52.9 percent in the second quarter of 2014, although the report does not disaggregate the impact of a variety of FHA policy changes, including improvement of its loss-mitigation options for servicers. Additionally, bids on these auctions have risen from approximately 40 percent of the loans' unpaid principal balances to an average closer to 60 percent.[5]

The report also suggests that homeowners have benefited from the program as well. Of the 50 percent of DASP loans that have reached resolution, 34 percent have avoided foreclosure, including the 11 percent of loans that are classified as "reperforming," which means that homeowners are again paying their mortgages regularly.[6] The outcome report contains no information on what enabled these mortgages to reperform, such as whether the homeowner obtained a permanent modification, a forbearance, or simply became reemployed. These numbers are significantly higher for the pools with specific neighborhood stabilization requirements, in which 58 percent have avoided foreclosure and 23.5 percent are reperforming.[7]

As DASP reaches its two-year anniversary, it is time to evaluate its performance and explore ways to strengthen it. FHA still insures more than half a million seriously delinquent loans, meaning there are still many loans potentially eligible for the program.[8] Moreover, the program serves as a critical model for the Federal Housing Finance Agency as Fannie Mae and Freddie Mac begin to sell nonperforming loans. Indeed, Freddie Mac auctioned its first pool of nonperforming loans this past August, so this possibility is now more than theoretical.[9] Between them, Fannie Mae and Freddie Mac still hold close to 700,000 seriously delinquent loans.[10]

This report provides an overview of DASP, including information on how it facilitates loan sales, who buys loans through it, and the information FHA has released concerning the outcomes of the purchased loans. The report then offers recommendations to enable DASP to better serve homeowners and neighborhoods while continuing to strengthen the FHA insurance fund.

Specifically, it recommends several programmatic changes that FHA could make to ensure that DASP buyers manage the loans they purchase in a way that most effectively stabilizes surrounding neighborhoods. For example, the pools with community stabilization requirements appear to be significantly more advantageous for homeowners and communities and sell at comparable prices to pools with fewer requirements.[11] Right now, however, the program only places such requirements on about 10 percent of the loans it sells.[12] With investor demand for nonperforming loans growing, FHA is well-positioned to ask more of buyers while continuing to protect taxpayers.

Background

The Federal Housing Administration does not directly make mortgage loans but rather provides insurance for lenders in the event that a homeowner defaults on a mortgage. For decades, FHA insurance has played a critical role in financing homes for millions of families, and today, most first-time homebuyers and homebuyers of color rely on FHA insurance to obtain a mortgage.[13]

During the housing crisis, when private capital froze and private mortgage insurers struggled, FHA significantly ramped up its activity to maintain a liquid housing market. Without FHA's intervention, it is likely that housing prices would have declined much further, perhaps almost twice as much as they did. The macroeconomic impact would have been devastating.[14]

However, stepping into this crucial countercyclical role while home prices were still declining took a toll on FHA's insurance fund.[15] Abuses of the FHA reverse mortgage product, along with losses associated with the seller-funded down-payment program, also damaged FHA finances. Consequently, over the past two years, FHA has taken numerous proactive steps to strengthen the insurance fund. These measures have included raising insurance premiums, eliminating overly risky products, adding underwriting protections, and creating the Distressed Asset Stabilization Program.

In considering DASP, it is important to understand that FHA generally pays out on a claim after the owner of the loan has already foreclosed on it and evicted the former homeowner. Under DASP, however, FHA can pay a claim on a delinquent loan before the loan goes through foreclosure. Once a claim is made, FHA has satisfied its insurance obligation to the lender. It then bundles loans into pools to auction in a competitive bid process to private investors.

According to FHA, DASP serves several important goals. First, the program can potentially provide seriously delinquent homeowners with a final opportunity to avoid foreclosure. Due to statutory constraints, mortgage servicers—the companies responsible for collecting mortgage payments and avoiding losses for the mortgage owner—have very limited discretion with regard to the kinds of loan modifications they can offer homeowners for FHA loans. For instance, they are not allowed to reduce the principal amount of the loan, which is often the most sustainable type of loan modification.[16]

Additionally, due to those same constraints, FHA cannot easily transfer servicing to a specialized default servicer still under FHA oversight when the original servicer is not doing a good job.[17] Other investors, including Fannie Mae and Freddie Mac, regularly transfer servicing in an effort to improve servicing outcomes. DASP operates as something of a backdoor method to get to transfer these loans into the hands of new servicers that might do a better job with default servicing. Moreover, since DASP buyers acquire the loans at discounted rates, they may be able to afford to make a deeper loan modification than the previous owner or to permit a more realistic short sale price. DASP does not, however, require any particular loan modification, or even that servicers make loan modifications, nor does it impose any kind of loss-mitigation waterfall, or preferred sequence of options that prioritizes keeping homeowners in their houses.

Finally, DASP enables FHA to pay a claim without requiring the servicer to evict the homeowner first. An eviction can be costly, and DASP eliminates the costs of foreclosure and subsequent maintenance costs associated with taking these loans into FHA's real estate-owned, or REO, portfolio.[18]

How loans are bought and sold through DASP

Mortgage servicers choose which loans to sell through DASP. According to FHA, to be eligible for DASP, the loan must be at least six months delinquent and the servicer must certify that it has exhausted all FHA loss-mitigation requirements.[19] To date, FHA has largely relied on mortgage servicers to certify that a loan meets DASP eligibility requirements, though the agency is in the process of adding additional oversight to this process to prevent fraud.[20] When the sale is complete, borrowers are notified that their loan has been sold.

Before a loan is sold through DASP, FHA pays the insurance claim—the remaining unpaid principal balance of the loan—along with some fees and expenses to the entity that owns the loan.

FHA auctions pool these acquired loans on a quarterly basis and sell them to the highest qualified bidder.[21] The entity that buys the loan through DASP either services the loan or hires a new mortgage servicer to service the loan. After the investor buys the loan, it must fulfill any requirements that FHA has specified. These requirements are described in detail in the next section.

Auctions through the Distressed Asset Stabilization Program

Currently, the Federal Housing Administration holds two different kinds of quarterly DASP auctions. The majority of loans are sold through auctions called national offerings in which loans are pooled together from across the country. Winning bidders may not foreclose on the loans they buy for at least six months after the loan settlement date.[22] Additionally, investors must fulfill simple, quarterly reporting requirements concerning the disposition or status of the loans they have purchased.

FHA also operates quarterly neighborhood stabilization outcome, or NSO, auctions. To date, about 20 percent of the loans bid on through DASP have been made available through NSO auctions. Loans bid on through NSO auctions are generally located in geographically concentrated metropolitan areas that have been hit hard by the foreclosure crisis, including Atlanta, Georgia; Phoenix, Arizona; Chicago, Illinois; Prince George's County, Maryland; Tampa, Florida; and Newark, New Jersey.[24]

NSO buyers also are not permitted to foreclose during the first six months after settlement, but they have to fulfill the significant additional requirement of resolving at least half of the NSO loans they buy in a way that FHA has determined stabilizes the surrounding neighborhood. Specifically, within 48 months, the buyer of an NSO pool must achieve one of the qualifying neighborhood stabilization outcomes referenced in the chart above for at least half of the loans it has purchased.[25]

Qualifying neighborhood stabilization outcomes[23]

- Six-month mortgage reperformance
- Short sale
- Sale to rental tenant
- Held for rental
- Gift to local government
- Sale to neighborhood stabilization program grantee or subgrantee
- Borrower pays outstanding mortgage debt

FIGURE 1

Loans auctioned through DASP: National vs. NSO

Source: Single Family Loan Sale Initiative," available at http://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/comp/asset/sfam/sfls (last accessed August 2014). See endnote 4.

FHA asks NSO buyers to report quarterly on the disposition and status of the loans they have purchased and submit relevant documentation in cases where the buyer believes an NSO is underway.

Who is buying loans through DASP, and why is demand for them growing?

Since the third quarter of 2012, 27 entities have won bids on loans through DASP. Private investors—including private equity firms, hedge funds, specialty servicers, and single-family rental companies—have won bids on close to 98 percent of all loans auctioned through DASP,[26] and the remaining loans have been won by nonprofit organizations with neighborhood stabilization missions. For many DASP buyers, the most profitable outcome strategy is to modify the loan and sell it at a higher price when the homeowner is once again making regular payments. However, it is important to note that this is true for loans prior to DASP as well, and in many cases servicers do not produce the outcome most profitable to the investor.[27] Buyers who have effective borrower outreach strategies in place are better positioned to improve mortgage loan performance.

TABLE 1

Top 5 DASP buyers

Buyer	Total loans won	Percent of total DASP loans
Lone Star Funds	22,447	22.70%
Bayview Asset Management	19,803	20.00%
Selene Investment Partners	6,813	6.80%
RBS Securities	6,573	6.65%
DC Residential Loan Acquisition, L.P.	6,491	6.56%

Notes: Includes winning bids from the third quarter of 2012 through the second quarter of 2014. Lone Star Funds is a private equity fund and bids on pools primarily through LSF9 Mortgage Holdings, LLC; Bayview Asset Management is funded by private equity firm Blackstone Group L.P. and bids on pools through Bayview Acquisitions, LLC; Selene Investment Partners is a division of the firm Ranieri Partners and bid through SRMOF II 2012-Trust; RBS Securities is the investment banking arm of the Royal Bank of Scotland and bid through RBS Financial Products, Inc.; and DC Residential Loan Acquisition, L.P. is a fund backed by Oaktree Capital Management and the total number of loans represented in the table include winning bids made by DC Residential Loan Acquisition Venture L.P. II, III, and IV.

Source: Derived from HUD data at U.S. Department of Housing and Urban Development, "Single Family Loan Sale Initiative," available at http://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/comp/asset/sfam/sfls (last accessed August 2014). See endnote 4.

Since the first DASP auction in 2012, the bidding prices on the assets have risen significantly. While in the third quarter of 2012, HUD received approximately 40 percent of the unpaid principal balance, or UPB, the bids were closer to 60 percent of the UPB in the second quarter of 2014.[28] To use another measure, since 2012, the bids have risen from an average of 56 percent of the broker price opinion—the estimated value of the underlying assets—to about 75 percent in the second quarter of 2014, an increase of about 34 percent.[29]

DASP auctions are not the only asset sales that benefit from an increased demand for nonperforming loans. Earlier this summer, Freddie Mac received 76 percent of the UPB on a pool of distressed loans worth $659 million.[30] In fact, during this summer alone, more than $9 billion in nonperforming and reperforming loans have been sold to investors.[31] Analysts estimate that investors will trade roughly $60 billion in distressed mortgage assets by the end of 2014, compared with the total of $25 billion in 2013.[32]

One key reason the bid prices are increasing is that home prices are rising in many parts of the nation, which renders the underlying collateral more valuable. However, there are a number of other factors at work as well.

One of these factors is the decline in the number of nonperforming loans. The nonperforming loan inventory from all sources—not just FHA—has dwindled by about 65 percent since 2012, meaning that investors may face greater competition for remaining nonperforming loans.[33]

Also, some investors that buy loans from HUD may benefit from a growing source of financing that makes it easier for them to bid more money for the loans: bonds backed by delinquent loans. This market, which barely existed earlier in the foreclosure crisis, grew to about $8.96 billion by 2013,[34] and about $5 billion worth of these delinquent loan bonds have been sold during the first two quarters of 2014.[35] In short, companies buying distressed assets may now have the option to securitize the loans they buy, particularly if they can show they have the ability to get mortgages to reperform.

Another factor that may increase demand for these nonperforming loans is the entry of large investors into the single-family rental industry. Since 2011, large investors have purchased 368,000 single-family homes,[36] many of them real estate-owned properties, and converted them into rental units. As the REO inventory declines and as home prices rise, some single-family rental companies are pursuing nonperforming loans as an alternative acquisition channel for inexpensive properties.[37] For example, one of these single-family rental companies, Altisource Residential—an affiliate of specialty servicer Ocwen—has bought about 2,500 loans through DASP;[38] Pretium Partners, a company that owns single-family rental company Progress Residential, recently bought 746 loans at an NSO auction in June.[39]

Nonprofit participation in DASP

A number of mission-based nonprofits have an interest in participating in DASP, particularly the NSO portion. Some that have bid successfully are already demonstrating DASP's potential to help stabilize neighborhoods. Nonprofit buyers include New Jersey Community Capital, a community development financial institution, and the Mortgage Resolution Fund, a national nonprofit partnership created by the Housing Partnership Network, Mercy Portfolio Services, Enterprise Community Partners, and the National Community Stabilization Trust. These buyers have leveraged foreclosure relief dollars from the Department of the Treasury's Hardest Hit Fund, which provides Troubled Asset Relief Program, or TARP, dollars to state housing finance agencies, and private sources of capital to rework hundreds of distressed loans bought through DASP.[40]

Despite the potential for nonprofits to make a difference, however, they have only won approximately 12 percent of the loans sold through NSO auctions—a mere 2 percent of all DASP loans.[41] While it is not entirely clear why nonprofit participation is so low, some nonprofits have found it difficult to compete with for-profit companies in the bidding process, even those nonprofits with the demonstrated ability to buy and manage a portfolio of distressed assets. Currently, FHA gives no preference or leg up to nonprofits in DASP auctions, even for the NSO pools, sticking instead to straight competitive bidding. For instance, Hogar Hispano, a foreclosure prevention program operated by the nonprofit National Council of La Raza, offered to pay 61 percent of the value of an NSO pool in 2012 but lost to a for-profit company that bid slightly higher at 66 percent on the dollar.[42]

DASP buyer at a glance: Bayview Asset Management[43]

Headquarters: Coral Gables, Florida

Synopsis: Founded in 1995, Bayview Asset Management is a mortgage investment firm that manages distressed and performing mortgages. It is the second-largest buyer of distressed loans from FHA.

Main stakeholder: Blackstone Group LP, the world's largest private equity firm, acquired a minority stake in Bayview in the aftermath of the Great Recession. Blackstone also owns Invitation Homes, the country's largest single-family rental company.

Status: Bayview, which buys primarily under the name Bayview Acquisitions LLC, has won about 20 percent of all DASP loans auctioned since the third quarter of 2012. It has concentrated acquisition activity on national pools, but the company also won 28 percent of NSO loans auctioned through DASP overall, the second-largest share won by any single buyer.

Geographical footprint: Bayview has won bids on more than one-third of DASP loans—national and NSO combined—from Illinois and about one-quarter of DASP loans from New Jersey. Bayview has also won about two-thirds of NSO loans auctioned from Atlanta and large NSO pools of Florida, Philadelphia, and Chicago mortgages.

Has the Distressed Asset Stabilization Program been effective?

This week, the Federal Housing Administration released its first report on outcomes for loans sold through DASP.[44] The report claims that in two years, the program has helped reduce FHA losses and has prevented a number of foreclosures. The data, as well as additional information available from participating buyers and from intermediaries working directly with homeowners, suggest how to improve the program going forward. The following section looks at both positive and negative outcomes of the program.

DASP may be helping strengthen the FHA insurance fund

By September 2013, FHA had reduced its in-foreclosure inventory—or defaulted assets that are not yet in the real estate-owned portfolio—by 20 percent since DASP's start, and it had limited losses on defaulted assets by almost 11 percent.[45] It is not clear, however, whether the change in loss levels is entirely due to DASP or even due to DASP at all, since FHA has taken many other contemporaneous steps to limit losses. The Department of Housing and Urban Development projects that DASP and some other strategies to prevent the department from incurring more losses will add $5 billion to FHA's insurance fund in the coming years.[46]

DASP may be helping avoid foreclosures

DASP appears to have helped a small percentage of participating homeowners keep their homes while helping many others avoid foreclosure through short sales and deeds-in-lieu of foreclosure.

According to FHA, the homeowner received a foreclosure prevention alternative in about one-third of all resolved DASP loans.[47] Approximately 11 percent are reperforming on their mortgages, which could mean that they have received a loan modification, but could also mean that they received a forbearance, a temporary payment plan, or simply once again had the income to pay their mortgage. There is no information in the report about whether any homeowners received principal reduction, which had been one of the original selling points for the DASP program.[48] Thirteen percent received permission for a short sale, and about 9 percent relinquished their homes in exchange for forgiveness of any remaining mortgage payments, which is also known as a deed-in-lieu-of-foreclosure.[49] About one-third of the loans went into foreclosure, and the remaining one-third were sold to other investors.[50] For loans sold to investors, FHA requirements do not travel with the loan, and FHA does not collect information about whether the subsequent purchaser pursued foreclosure or foreclosure alternatives.

The FHA report notes that only about half of the loans sold through DASP have reached final resolution, and the report provides no data on what has happened so far to the other half. As would be expected, earlier sales have very high resolution percentages, but for more recent auctions, quite a number of the mortgages have yet to be resolved.

TABLE 2

Status of combined national and NSO loans sold

Category	Count	Percentage of loans sold	Percentage of resolved loans
Resolved			
Foreclosures avoided			
Reperforming	2,049	5.4%	10.9%
Forbearance	82	0.2%	0.4%
Paid in full/short payoff	167	0.4%	0.9%
Third-party sale	2,445	6.4%	13.0%
Deed-in-lieu	1,684	4.4%	8.9%
Total foreclosures avoided	**6,427**	**16.9%**	**34.1%**
Foreclosure	5,850	15.4%	31.0%
Total outcomes	**12,277**	**32.3%**	**65.1%**
Other resolutions			
Whole loan sale	6,592	17.4%	34.9%
Subtotal resolved	**18,869**	**49.7%**	**100.0%**
Not yet resolved			
Delinquent servicing	19,121	50.3%	
Total loans sold	**37,990**	**100.0%**	

Source: Department of Housing and Urban Development, "Quarterly Report on FHA Single Family Loan Sales: Data as of May 30, 2014" (2014), available at http://portal.hud.gov/hudportal/documents/huddoc?id=report082814.pdf. (Data includes loans sold from 2010 through the second quarter of 2013).

NSO pools yield better outcomes for homeowners

What is more striking about the data is the success of loans in the neighborhood stabilization outcome pools. A full 23.5 percent of resolved loans in these pools are reperforming—more than twice the percentage of those in the overall program. Close to 21 percent avoided foreclosure through a short sale, and almost 11 percent did so through a deed-in-lieu. Moreover, less than 1 percent of the NSO loans were resold, so almost all of the loan outcomes will be captured by the required DASP reporting.[51]

TABLE 3

Status of NSO loans sold

Category	Count	Percentage of loans sold	Percentage of resolved loans
Resolved			
Foreclosures avoided			
Reperforming	656	7.1%	23.5%
Forbearance	1	0.0%	0.0%
Paid in full/short payoff	58	0.6%	2.1%
Third-party sale	576	6.3%	20.7%
Deed-in-lieu	325	3.5%	11.7%
Total foreclosures avoided	**1,616**	**17.6%**	**58.0%**
Foreclosure	1,152	12.5%	41.3%
Total outcomes	**2,768**	**30.1%**	**99.4%**
Other resolutions			
Whole loan sale	18	0.2%	0.6%
Subtotal resolved	**2,786**	**30.3%**	**100.0%**
Not yet resolved			
Delinquent servicing	6,401	69.7%	
Total loans sold	**9,187**	**100.0%**	

Source: Derived from HUD data at U.S. Department of Housing and Urban Development, "Quarterly Report on FHA Single Family Loan Sales: Data as of May 30, 2014" (2014), available at http://portal.hud.gov/hudportal/documents/huddoc?id=report082814.pdf. (Data includes loans sold from 2010 through the second quarter of 2013).

Information from individual nonprofits confirms the FHA report's findings. For example, New Jersey Community Capital, or NJCC—a nonprofit buyer of NSO loans—has been able to modify about 35 percent to 40 percent of the homeowner occupied loans it purchased in New Jersey and Florida through DASP.[52] The way NJCC achieves these striking results is by reducing the principal balance on these loans whenever possible to keep homeowners in their homes, as well as by providing homeowners with housing counseling so they are better prepared to maintain their modified loans.[53] When NJCC is not able to modify the loan, it makes every effort to avoid leaving neighborhoods with a blighted property. It may convert the home into a rental unit operated by its single-family rental business, or, if a home is already vacant when NJCC acquires the loan, NJCC may distribute it to community developers to be rehabilitated and converted into affordable housing.[54]

TABLE 4

Status of national loans sold

Category	Count	Percentage of loans sold	Percentage of resolved loans
Resolved			
Foreclosures avoided			
Reperforming	1,393	4.8%	8.7%
Forbearance	81	0.3%	0.5%
Paid in full/short payoff	109	0.4%	0.7%
Third-party sale	1,869	6.5%	11.6%
Deed-in-lieu	1,359	4.7%	8.4%
Total foreclosures avoided	**4,811**	**16.7%**	**29.9%**
Foreclosure	4,698	16.3%	29.2%
Total outcomes	**9,509**	**33.0%**	**59.1%**
Other resolutions			
Whole loan sale	6,574	22.8%	40.9%
Subtotal resolved	**16,083**	**55.8%**	**100.0%**
Not yet resolved			
Delinquent servicing	12,720	44.2%	
Total loans sold	**28,803**	**100.0%**	

Source: Derived from HUD data at U.S. Department of Housing and Urban Development, "Quarterly Report on FHA Single Family Loan Sales: Data as of May 30, 2014" (2014), available at http://portal.hud.gov/hudportal/documents/huddoc?id=report082814.pdf. (Data includes loans sold from 2010 through the second quarter of 2013).

Some servicers are referring loans to DASP that do not meet DASP's eligibility criteria

FHA requires servicers to complete all FHA loss-mitigation protocols and to certify that the loan is otherwise headed to foreclosure before referring a loan to DASP. However, homeowner advocates have notified HUD of several DASP loans that clearly do not meet the program's eligibility standards, such as loans to homeowners who received notices that their loans were auctioned through DASP even as they were in the middle of working out loan modifications with their original mortgage servicers.[55] Roughly 76 percent of the 88,665 loans auctioned through DASP during the 2013 and 2014 auctions came from Bank of America, JP Morgan Chase, and Wells Fargo, all companies whose problems with properly servicing troubled loans are well documented.[56]

If servicers are referring loans to DASP without completing the assessment of homeowner options required by FHA, it can hurt FHA's bottom line, since a successful modification can reduce losses more for FHA than a DASP sale. It is also likely to hurt the homeowner by preventing them from receiving the type of permanent, affordable loan modification available under FHA's guidelines. Additionally, more than 60 percent of loans referred to DASP came from judicial foreclosure states, which suggests that servicers may be using DASP to sidestep the judicial process.[57]

Some DASP pools contain significant numbers of vacant homes

Some buyers have found that a significant number of loans secure vacant or abandoned properties in the pools that they have purchased through DASP. For example, nearly half of a pool purchased by one nonprofit buyer was made up of vacant homes.[58] This high number of vacancies makes it difficult for buyers to accomplish the type of foreclosure prevention work for which they raise capital.

Moving forward: Strengthening the Distressed Asset Stabilization Program

While DASP appears to have helped a number of homeowners, evidence indicates that with some adjustments, the program could assist even more homeowners and support neighborhoods more effectively while still continuing to strengthen the insurance fund of the Federal Housing Administration. Below are some recommendations for such adjustments.

Prevent mortgage-servicing companies from abusing DASP

FHA should take additional steps to ensure that mortgage servicers are not using DASP as an alternative to fulfilling their loss-mitigation requirements under FHA's rules. Especially since FHA has recently improved the loan-modification options it offers to borrowers with FHA-insured loans,[59] homeowners should receive the full suite of available loss mitigation. When mortgage servicers push loans into the program prematurely, not only may homeowners suffer unnecessarily, but FHA also may lose money if it has to pay unwarranted insurance claims.

Until now, FHA has relied on servicers to self-certify that loans meet eligibility requirements. Agency staff have indicated, however, that they plan to start auditing a sample of servicer self-certifications, which should help ameliorate this problem.[60] The agency should also consider notifying homeowners that their loans are entering DASP prior to the auctions, leaving time for a homeowner in the midst of the loss-mitigation process to contact FHA with that information.

Additionally, FHA should be able to remove loans that are erroneously sold into the program more easily. Currently, if a servicer abuses the program, it is difficult for FHA to address the problem and revoke the paid claim. CAP supports efforts to strengthen DASP's clawback provisions so that FHA can hold servicers accountable. Needless to say, FHA should carefully monitor not just whether loans are incorrectly referred, but also whether buyers adhere to the sale requirements in both national and NSO pools.

CAP also recommends that FHA develop a separate set of requirements for vacant properties. Allowing mortgage servicers to feed vacant properties into a program with requirements focused mainly on keeping homeowners in their homes undermines the core thrust of the program and makes it hard for entities interested in modifying delinquent loans to trust the quality of the pools they are buying. Yet because vacant properties pose a significant threat to communities and neighborhoods, and because their disposition could also save FHA money, we recommend FHA explore whether to include vacant homes in a separate but related initiative that includes appropriate requirements on how those homes are treated. For example, instead of a six-month prohibition on foreclosure, FHA could impose a requirement that such properties be offered for sale to potential owner-occupants or investors who live or operate in the immediate neighborhood prior to repurposing them as single-family rentals owned by investors outside the community.

Strengthen DASP post-sale requirements to improve outcomes for homeowners and neighborhoods

Especially given the increasing demand for DASP loans, FHA is well-positioned to ask buyers to do more to improve outcomes for both homeowners and neighborhoods. The recommendations below suggest several options, including instituting additional requirements for the national pools, expanding the portion of loans sold through NSO auctions, and helping more nonprofits acquire DASP loans.

Add homeowner- and neighborhood-friendly requirements to national offerings

FHA should require all DASP buyers to pursue an explicit loss-mitigation waterfall, through which they attempt to work out a loan modification with the homeowner and try to resolve the loan through a short sale or deed-in-lieu of foreclosure before foreclosing or selling the property to another investor.

Such a requirement should not reduce DASP's ability to save money for FHA for three reasons. First, demand for these pools is growing and the bids are highly competitive, with high prices for both national and NSO pools. Second, since many buyers already have interests aligned with homeowners because loan modifications are the most profitable outcome for them, they may already be using such a waterfall, meaning that this requirement will only affect the value for those bidders whose priorities do not already align with those of homeowners. Third, since FHA properties tend to cluster in neighborhoods, helping preserve the value of neighboring homes and communities should reduce overall FHA delinquencies and foreclosures, saving the agency money.

Once the investor has a DASP vacant home in its portfolio—either because the home arrived vacant or because of a deed-in-lieu or foreclosure—it should implement a "first-look" period where owner-occupants and/or community stabilization nonprofit organizations have an opportunity to buy the home before the company rents out the home or sells it to another investor. Such a requirement would help ownership of the home remain in the community and help potential buyers compete with cash investors.

Consistent with its support for housing counseling in its Homeowners Armed with Knowledge, or HAWK, program,[61] FHA should encourage all buyers to incorporate nonprofit, HUD-certified housing counselors into their outreach models. FHA should also require all DASP buyers to secure and maintain REO properties in a way that prevents any loss to a home's value.

Strengthen and expand NSO auctions

FHA can help stabilize neighborhoods by expanding the NSO portion of DASP. To date, FHA has required NSOs for about 10 percent of loans, or about 10,288 of the 98,000 homes DASP has offered for sale.[62] Shifting more loans to neighborhood stabilization pools should not make DASP any less profitable for FHA. Even with the more stringent post-sale requirements, companies have recently bid similar amounts—and, sometimes, even higher amounts—on NSO pools as they have on the pools sold through national offerings.[63]

Strong NSO bids could be occurring because the geographic concentration of the loans in these pools makes it easier for buyers to find productive outcomes for the loans. If geographic concentration is important, FHA should explore the viability of selling more geographically concentrated pools with NSO requirements.

Currently, buyers can fulfill the NSO requirements in a variety of ways. As suggested above for the national pools, FHA should structure the various NSO requirements as a waterfall of options that includes the first-look provision if the NSO buyer decides to rent the home or sell it to another investor. Additionally, after pursuing the waterfall, a buyer should be able to fulfill NSO requirements by selling the home to an owner-occupant, just as it currently can by renting the home.

Encourage more nonprofit participation

Despite FHA's hope for greater nonprofit participation, such organizations have bought only a small fraction of DASP loans. We recommend that FHA make it easier for nonprofits to participate. One way would be to create separate nonprofit NSO pools where competitive bidding is limited to nonprofits only. Alternatively, where private investors and nonprofits both bid for the same pools, FHA could give nonprofits a last chance to rebid after the initial bidding is completed to see if they can match or exceed the highest bid.

FHA also should encourage partnerships between for-profit bidders and mission-driven nonprofits. These partnerships can marry the ability of community organizations to reach struggling borrowers with the private market's access to capital. FHA could consider whether to make a partnership a requirement for companies to bid on NSO pools.

Additionally, FHA should make improvements to its 203(k) program—financing that covers properties' acquisition and rehabilitation costs—to help build nonprofits' capacity to buy loans and rehabilitate properties.

Finally, FHA and the Department of the Treasury should work together to make it easier for nonprofits to use Hardest Hit Funds to buy and modify DASP loans. Both of these programs share the same goal, but they each have very specific requirements that nonprofits working with them have found difficult to coordinate.

Collect and regularly share data on program outcomes

As DASP goes forward, FHA should significantly expand and improve its data collection and publish program outcomes on a regularly scheduled basis so that the public can better understand the strengths and challenges of the program. Public information should include not just the outcome data already collected but also the terms of any loan modifications, demographic information about the homeowners, and whether the home is being used as a long-term rental, among other things. This information could be provided in an aggregate format that protects personally identifiable information and investor proprietary interests. Sharing this information will inspire confidence among stakeholders that the program is helping homeowners and that all homeowners are being treated fairly. FHA also should provide more public information about their efforts to enforce the DASP sale restrictions.

Conclusion

Almost six years after the financial crisis and after more than 5 million foreclosures,[64] it would be nice to think the housing market was out of the woods. However, nearly 2 million homeowners remain at risk of foreclosure because of reduced income, underwater loans, or the failure of mortgage servicers to assist them properly.[65]

Fortunately, the Federal Housing Administration, which has played an outsize role in keeping the mortgage market afloat through the Great Recession, continues to engage in innovative efforts to avoid foreclosures. Through its Distressed Asset Stabilization Program, FHA is attempting to protect taxpayers by reducing losses on defaulted loans and provide thousands of borrowers headed to foreclosure with a second chance to stay in their homes or to leave them in a way that is less devastating both financially and emotionally.

Yet as FHA's outcome data make clear, some parts of DASP are more beneficial for homeowners than others. The neighborhood stabilization outcome pools have a much better track record for loan reperformance and other foreclosure alternatives, and they do not pass on many loans to investors that operate without any DASP restrictions.[66]

Going forward, FHA should make programmatic changes that encourage better outcomes across all pools. It should also consider how to expand the number of NSO pools, increase nonprofit participation in the program, ensure that mortgage servicers do not abuse the program, and expand data collection and publication. By engaging in a continual improvement process of this nature, FHA can establish DASP as a best-practice model for other investors, including Fannie Mae, Freddie Mac, and all other investors committed to protecting both taxpayers and homeowners.

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Endnotes

1 Prior to 2012, FHA had run a pilot program known as the Single Family Loan Sale Program, and DASP represented an expansion and enhancement of that program.

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