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Lessons Learned from the CARES Act Mortgage Forbearance Program and Its Aftermath

From the RADAR Group, Federal Reserve Bank of Philadelphia

Since the COVID-19 emergency will soon be over, this is our final report. So, it's time to sum up.

When we began our analysis on the CARES Act Mortgage Forbearance Program, the housing market was in crisis. After the shutdown of the economy in March 2020, unemployment peaked at 14.9 percent in April 2020. By May 2020, around 6.6 million mortgages in the U.S. were either past due or in some state of forbearance as the program was officially launched.

Since the CARES Act only applied to federally insured mortgages, there was no assurance of the extent to which private investors not subject to the program would participate. And since borrowers needed only to request a forbearance to be granted one, it was unclear how large the program would become. Finally, since forbearance only provides temporary relief, it was unclear whether servicers would be able to provide the longer-term relief for the millions of borrowers in forbearance to keep them in their homes.

At the Federal Reserve, we acquired Black Knight's **McDash Flash** database that allowed us to track mortgage loan performance on a weekly basis. And by merging our data with the Home Mortgage Disclosure Act (HMDA) application data, we could track the extent to which the program was addressing those most in need of assistance. When our first report came out on September 3, 2021, more than 3 million mortgages were still in some state of nonpayment.

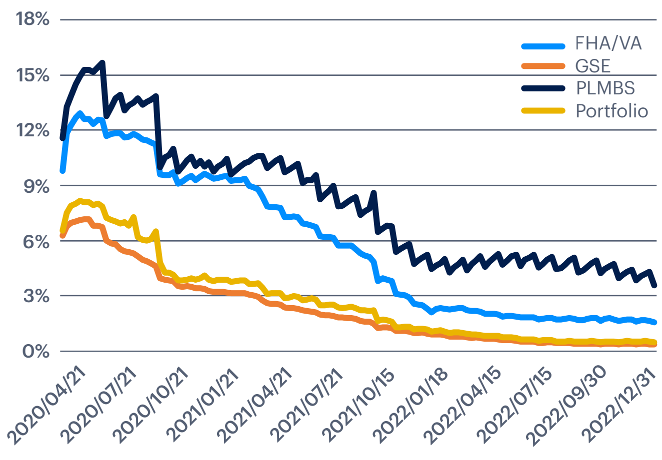
As the program winds down, more than 95 percent of the estimated 8.5 million borrowers who entered forbearance have exited. **Figure 1** depicts the progress made over time by the major investor groups. Forbearances have dwindled to levels consistent with prepandemic levels for portfolio lenders and the government-sponsored enterprises, Fannie Mae and Freddie Mac. The one remaining group of sizable forbearances are the FHA/VA borrowers, with now close to 200,000 mortgages still in forbearance.[1]

In a forthcoming paper, we examine the program in-depth.[2] Here we summarize its main findings and discuss one vestige of its aftermath: the FHA Payment Supplement Account (PSA) Program, specially designed for FHA borrowers, but which is unavailable to VA borrowers as of this writing. Our overall findings are that the program mitigated a default wave like that experienced during the Great Recession of 2008–09, as both government and private lenders participated on a broad scale to provide forbearance relief to all who requested it. And the program achieved its objectives of providing relief to those most in need of help.

Just as importantly, of the borrowers who entered forbearance and cured, almost three-quarters of their requests were worked out in some way by mortgage servicers to keep them in their homes. Thus, our findings show that the CARES Act Mortgage Forbearance Program with private-sector participation provided short-term debt relief to those most in need, with subsequent servicer workout programs providing longer-term help to keep millions of borrowers in their homes.

We also analyze a new FHA Payment Supplement Account (PSA) Program that will be able to reduce FHA borrowers' payments by up to 25 percent for those 90 or more days past due on their mortgages, specially designed for the current high mortgage rate environment.

Figure 1: COVID-19 Forbearance Rates by Investor, April 2020 to December 2022



Sources: Black Knight Data & Analytics, LLC; and RADAR

Assessing the CARES Act Mortgage Forbearance Program

Table 1 summarizes how the 8.5 million borrowers who entered forbearance during the first year of the pandemic exited forbearance.[3]

We first note that around 22.5 percent of borrowers ever in forbearance were able to self-cure through a lump sum payment; 58 percent needed help of some kind to cure; and 19.5 percent have yet to exit forbearance, paid off out of delinquency or forbearance, or are delinquent or defaulted. While around 80 percent of borrowers were able to exit forbearance one way or another, of those who have cured, 58 percent/80.5 percent = 72 percent, or almost 5 million borrowers, received some sort of assistance from their mortgage servicers to stay in their homes.

Table 1: COVID-19 Forbearance by Category

Category 1: Self-Cure	**22.5%**
Category 2: Became Current with Help	**58.0%**
Repayment Plan	22.7%
Deferral	18.1%
Modification	16.4%
Trial Modification	0.9%
Category 3: Forbearance/Delinquent/Default	**19.5%**
Still in Forbearance	2.0%
In Loss Mitigation, But Not Paying	1.6%
Delinquent, Not in Loss Mitigation	4.2%
Paid Off from Forbearance or Delinquency	11.7%
Default	0.1%
Total	**100.0%**

Sources: Black Knight Data & Analytics, LLC; and RADAR

Table 1 also separates the three large categories into the kinds of help received to reperform and for those that did not reperform. We can see that among those who received help, borrowers were most likely to have gone through a repayment plan (23 percent). Deferrals of past due arrears where borrowers resume timely payment (18 percent) and formal modification (16 percent) are the next most likely options. Note that these rates of assistance occurred in the order from least to most costly for investors, suggesting that mortgage servicers performed workouts in the order preferred by investors based on cost.

The remaining borrowers are still in forbearance or out of forbearance and delinquent or defaulted. Note that 11.7 percent of borrowers paid off out of delinquency or forbearance. These are borrowers more likely to have defaulted had there not been robust house prices. While not shown here, many borrowers not receiving help were very deeply delinquent prepandemic, so they were not in a good position to be helped.

Also not shown here but detailed in our research, more minority and lower-income mortgage borrowers were able to avoid delinquency on their mortgages than their White and higher-income counterparts. Unconditionally, we find that, after accounting for forbearance, delinquency rates for Black borrowers fell from 6.9 percent in 2019 to 1.9 percent in 2020, while for White borrowers, the rates fell from 1.3 percent to 0.5 percent.

As a result, Black borrowers were able to shrink the delinquency rate gap between Black and White by 4.3 percentage points by taking up forbearances. Furthermore, we show that minority and lower-income borrowers took up forbearance at significantly higher rates, conditional on having entered nonpayment. Without forbearance, delinquency rates of minority and lower-income borrowers would have been twice as high as those of White and higher-income borrowers.

The FHA Payment Supplement Account Program

As shown in **Figure 1**, FHA/VA borrowers have the highest remaining forbearance rates. They also happen to be the most challenging to work out in the current high-interest rate environment. To modify an FHA loan, the servicer must purchase the loan out of the Ginnie Mae pool at par, or 100 percent of the unpaid principal balance (UPB). Then, to resecuritize the modified loan without incurring a loss, the servicer must set the rate on the modified loan to the prevailing market rate so that it can be sold at par. Most seriously delinquent loans have a note rate well below current market rates, so increasing the note rate as part of the modification offsets most or all the payment reduction provided by other modification steps (such as extending the loan term to 40 years or deferring principal).

The Payment Supplemental Account (PSA) Program is an alternative to a traditional modification, designed to lower a borrower's monthly payment by up to 25 percent without changing loan terms, thus allowing for an *in pool* modification. It does so by expanding the use of the *partial claim* (PC) allowed for FHA loans, which is a no-interest subordinated lien held outside the Ginnie Mae security that the borrower accumulates and then pays back at the time of payoff.

Specific details of the PSA Program are documented in **Appendix 1**. Here we use a representative loan in **Table 2** to illustrate how the program works. The loan has $300,000 in UPB with arrearages of $25,000, including principal interest, taxes, and insurance (PITI) advanced by servicers. The full PC capacity is 30 percent of UPB, or $90,000. A PC is a no-interest subordinated lien outside the security trust, so any additions to it do not affect existing loan terms.

Table 2: Illustration of Payment Supplemental Account (PSA) Program

Unpaid Principal Balance (UPB)	$300,000
Existing Principal & Interest (P&I) payment	$1,200
Past due arrears	$25,000
Partial claim capacity = 30%*($300,000)	$90,000
Past due arrears covered = $25,000	$25,000
Funds available for PSA = $90,000 – $25,000	**$65,000**
New mortgage payment = (75%)*$1,200	**$900**
Funds needed to meet P&I reduction target for 5 years (25%*$1,200)*48 + (12.5%*$1,200)*12	**$16,200**
Enough funds for 5 years? ($65,000>$16,200)	**Yes**
Actual amount in PSA = Min ($65,000, $16,200)	$16,200
Partial claim amount used = $25,000 + $16,200	**$41,200**
Partial claim capacity used = $41,200/$90,000	**46%**

Sources: HUD, RADAR

First, the $25,000 of arrearages are placed into the PC account, making the funds available for the PSA, which is $65,000 in this case. Next, a calculation is made as to how much is needed to achieve the program's P&I reduction targets for five years and whether enough capacity exists for the PC to absorb the deferred payments. As detailed in Appendix 1, the goal of the PSA is to reduce the borrower's payment by 25 percent for the first 48 months and 12.5 percent for the last 12 months. In this case, to achieve the 25 percent payment reduction target, the payment needs to be reduced by $300 for the first 48 months (=$300/$1,200) and $150 for the last 12 months. This $16,200 payment shortfall can be easily absorbed in the $65,000 PC capacity, even after adding in the $25,000 in missed PITI payments. In total, the PC amount used is $41,200, which is 46 percent of the full PC capacity.

To assess how effective the PSA is in achieving its goals, we ran the PSA algorithm using our McDash Flash sample on all the FHA borrowers who were 90 or more days delinquent on their mortgages, which is a condition for inclusion in the PSA Program.[4] As shown in **Table 3**, more than 95 percent of the FHA seriously delinquent borrowers have enough PC capacity to achieve the payment-reduction goals.

Not all borrowers will qualify for the full payment assistance. These are borrowers who have missed so many payments that past due PITI payments absorb most or all their PC capacity. About 1.2 percent of borrowers can receive the full PSA for a period of between three and less than five years. These are borrowers who on average are behind by 20 payments. Another 1.2 percent can get a lesser payment reduction of around 11 percent; these borrowers on average are 25 payments behind. And around 2.5 percent of borrowers who have missed around 35 payments will have the past due PITI fully absorb all PC capacity, so they will be unable to receive any payment reduction.

In sum, based on our large sample of FHA borrowers, our assessment is that the proposed PSA Program can help more than 95 percent of borrowers achieve the full benefit of the five-year PSA Program.

Table 3: Assessing the Proposed FHA Payment Supplement Account Program

PC=30% Supplemental Payment Period 3-5 years	Sample Counts	Share	Number of Missed Payments	PC Usage	P&I Reduction
No supplement payments available	924	**2.5%**	35	100%	0%
Provides less than target P&I reduction for 3 years	455	**1.2%**	25	100%	11%
Meets P&I Reduction Target for 3-5 years*	432	**1.2%**	20	100%	25%
Meets P&I Reduction Target for 5 years*	35,734	**95.2%**	7	41%	25%
	37,545	100%			

Notes: PC = Partial Claim; P&I = Principal and Interest.
* The P&I reduction target is 12.5 percent for the last 12 months of the supplemental payment period.
Source: RADAR estimates using data from Black Knight Data & Analytics, LLC.

A final point is that the PSA will generally be optimal for these special cases in which market rates are substantially above borrowers' fixed mortgage rates. More traditional modifications may be preferred when market rates are below existing note rates, which was the case before recent Federal Reserve rate increases.

An observant reader will notice that no mention has been made about Veterans Administration (VA) loans. The reason is because the VA does not have the tool of PCs. The VA provided them during the COVID-19 pandemic until last October but let their authority lapse. Getting them reauthorized will require legislation, which could potentially be a big help for VA borrowers if they became eligible for a PSA.

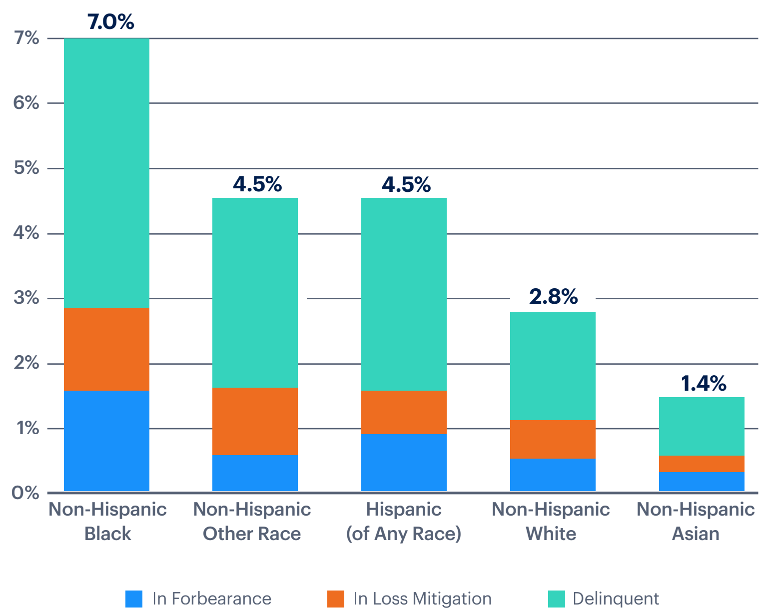
Demographic Characteristics of Past Due Mortgages

For completeness, we close out by showing that, despite the successes of the CARES Act Mortgage Forbearance Program, past due rates remain much higher for minority and lower-income borrowers, making applications like the FHA's PSA Program and other workout programs of ongoing importance, especially as house prices started to decline in the second half of last year. To examine past due rates by race and income, we merged a sample of our servicing data from Black Knight Data & Analytics with confidential HMDA data, where borrower race and household income are collected at application. As shown in **Figure 2**, 7.0 percent of Black borrowers are in some past due state, the highest of any group. Hispanic borrowers have the next highest rate, above those of White or Asian borrowers.

Past due states include borrowers in forbearance, borrowers not in forbearance but in some stage of loss mitigation,[5] and borrowers who are delinquent but neither in forbearance nor in loss mitigation.

For further details on Figure 2, see **Appendix 2**, which includes these past-due percentage breakouts, as well as past due rates by income quartile and for our four major investor groups.

Figure 2: Past Due Rates by Race and Ethnicity as of January 9, 2023



Sources: Black Knight Data & Analytics, LLC; Home Mortgage Disclosure Act (HMDA); and RADAR

Appendix 1
Payment Supplemental Account (PSA) Program Details

- Place PSA at the bottom of the COVID-19 waterfall.
    - Offer if borrower:
        - Has a greater remaining partial claim (PC) capacity than arrearages,
        - Cannot resume payments with a standalone PC, and
        - Cannot obtain 25 percent P&I reduction through standard Recovery Mod (RM).
    - Target 25 percent P&I reduction for four years and 12.5 percent reduction for the fifth year to reduce payment shock.
    - After catching up borrowers, servicer places PC funds in a no-interest restricted account to supplement borrowers' monthly principal payments over time.
- Details
    - Catch up borrower arrearages using PC funds.
    - If possible, provide a 25 percent P&I reduction for two to four years and a 12.5 percent reduction for each subsequent year, for a minimum three-year total period.
        - (The test for sufficient PC capacity is to provide a 25 percent reduction for >= 2.5 years and <= 4.5 years.)
    - If this level of reduction cannot be provided for the minimum three-year period, offer whatever reduction is possible for three years, with no graduated payment, if:
        - The reduction is >= a de minimus amount, such as 5 percent, and
        - PSA reduction is > can be provided by the standard relief modification.
    - Borrower who redefaults:
        - Can cure default during the PSA Program using any undrawn PC funds and reenter the existing PSA Program but cannot receive a second PSA Program during the existing plan.
        - Alternatively, can reenter the FHA waterfall and receive a standalone PC or modification using undrawn PC funds in addition to any funds remaining in the restricted account.

Appendix 2
Mortgage Shares in Different States of Nonpayment by Demographic/Investor Groups as of January 9, 2023

Demographic/Investor Classifications	In Forbearance	Delinquent, No Forbearance			Total
		In Loss Mitigation	Not in Loss Mitigation		
			30-60DPD	90+DPD	
Race and Ethnicity					
White, Non-Hispanic	0.6%	0.5%	1.2%	0.5%	2.8%
Black, Non-Hispanic	1.6%	1.3%	2.9%	1.2%	7.0%
Asian, Non-Hispanic	0.3%	0.3%	0.6%	0.2%	1.4%
Other Race, Non-Hispanic	0.7%	1.0%	1.9%	1.0%	4.5%
Hispanic (of Any Race)	0.9%	0.7%	2.3%	0.6%	4.5%
Income at Origination					
1st Quartile (Lowest)	1.0%	0.9%	2.0%	0.8%	4.6%
2nd Quartile	0.8%	0.7%	1.6%	0.6%	3.7%
3rd Quartile	0.6%	0.5%	1.1%	0.4%	2.5%
4th Quartile (Highest)	0.3%	0.3%	0.5%	0.2%	1.3%
Investor Type					
GSE	0.4%	0.3%	0.5%	0.2%	1.4%
FHA/VA	1.2%	1.3%	3.1%	1.2%	6.8%
PLMBS	2.7%	1.5%	5.4%	2.2%	11.8%
Portfolio	0.4%	0.3%	0.9%	0.5%	2.1%
Servicer Type					
Bank	0.5%	0.4%	1.2%	0.4%	2.5%
Non-Bank	1.3%	1.7%	2.5%	0.9%	6.4%

Notes: Figures are from a 20 percent random sample of data from Black Knight Data & Analytics originated in 2019 and prior matched with confidential Home Mortgage Disclosure Act (HMDA) data.

Sources: Black Knight Data & Analytics, LLC; HMDA; and RADAR

In this table, we further break out past due loans between those 30- and 60-days past due (DPD) and those 90 or more DPD, which includes loans in foreclosure.

For borrowers' household income data, we divide them by metropolitan statistical areas (MSA) median income (also in HMDA), then categorize into quartiles. We categorize borrowers relative to median income in their MSAs in the application year to make household purchasing power at application comparable across MSAs and time.

For our four major investor groups described in Figure 1, consistent with these demographic trends, FHA/VA loans have significantly higher shares in nonpayment because their business is targeted to low- to moderate-income borrowers, who also have higher shares of minorities. PLMBS loans have the highest nonpayment rates; they primarily hold nonagency nonconforming mortgages.

Endnotes

[1] Mortgages in private-label mortgage-backed securities (PLMBS) are higher by percentage, but PLMBS are a small share of the market, and 99 percent of the loans in forbearance are pre-2009, many of which have been previously modified.

[2] See An, Cordell, and Lee (2023) forthcoming. The views expressed in this report are solely those of the authors and do not necessarily reflect the views of the Federal Reserve Bank of Philadelphia or the Federal Reserve System.

[3] We focus on mortgage borrowers who entered forbearance in 2020 since they are the bulk of forbearances; we also include many cases whose forbearances expired of this writing.

[4] To reduce the moral hazard of borrowers requesting PSA assistance, HUD requires borrowers to be 90 or more days delinquent on their mortgage or be able to document *imminent default*. Being seriously delinquent on a mortgage imposes large costs to borrowers in degraded credit scores that restrict access to credit or raise its costs substantially if they do need to obtain credit.

[5] Borrowers in loss mitigation and not in forbearance include borrowers in a *trial* loan modification in which borrowers are offered lower payments and the servicer requires several consecutive payments to be made before these more favorable loan terms are made permanent and borrowers are brought current on their mortgages.