Fannie Mae, Freddie Mac Unveil New IDR Process

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Federal National Mortgage Association (Fannie Mae) (OTCBB:FNMA) and Federal Home Loan Mortgage Corp. (Freddie Mac) (OTCBB: FMCC) have announced the formation of independent dispute resolution (IDR) process to make repurchase dispute resolutions efficient.

IDR marks the last step taken by Freddie Mac and Fannie Mae under the Representation and Warranty Framework. Lenders will now be able to accelerate unresolved disputes to an arbiter — a neutral third party. It will relieve pressure on mortgage lenders who often have to pay huge penalties for bad loans. More importantly, lenders will be empowered to choose risky borrowers, and in turn, creditworthy borrowers will have better access to mortgages. A neutral arbiter would resolve disagreements between lenders and regulators now.

Mortgage Bankers Association President and CEO David Stevens welcomed the ruling as a final step to provide transparency and confidence to “lenders of all sizes.” It will provide clarity on government sponsored entity (GSE) procedures to handle repurchase requests.

At present, lending is still tighter than pre-housing crisis since banks are fearful of “buying back mortgages,” as highlighted by the Housing Finance Policy Center at the Urban Institute, Washington. The number of loans that defaulted during the financial crisis and litigation suits caused lenders to stop making mortgages to eligible borrowers. Some analysts are doubtful if the new ruling could promote and help increase access to mortgage, as expressed by The Wall Street Journal.

The Representation and Warranty Framework was developed in 2012. The framework was implemented after the financial crisis to provide support to lenders. Since 2012, two different rulings in 2013 and 2014 impacted the framework. In 2013, an agreement was reached that lenders will not be forced to repurchase the loan if the borrowers do not miss any payment for three years. While in 2014, the GSE along with lenders agreed to define the term fraud and outline the costs associated with fraud.

Prior to these rulings, risky borrowers were not able to qualify for loans as large banks increased the cutoff for eligibility of borrowers. It happened after stringent regulations were imposed. It diverted ineligible borrowers to “smaller nonbank lenders,” who were less prone to strict penalties, as expressed by Mark Calabria, director at Cato Institute. This time, Freddie Mac and Fannie Mae will keep the cutoff lower, between 300 to 850, at 620.

Freddie Mac stock closed up 2.03% at $1.25 on Wednesday, while Fannie Mae also closed up 2.02% at $1.26.