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Fannie Mae and Freddie Mac Agree to Terms on Resolving Mortgage Disputes

Joe Light

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Fannie Mae and Freddie Mac said Tuesday they have come to terms with lenders on how to resolve mortgage disputes, capping an effort that regulators hope will make loans cheaper and easier to get for some risky borrowers.

The announcement marks the end of a four-year push by Fannie, Freddie and their regulator, the Federal Housing Finance Agency, to ease mortgage companies' fears of being slapped with penalties for faulty loans, in a bid to encourage them to pick up lending to more risky borrowers.

FHFA Director Mel Watt said in a statement that the changes "will increase clarity for lenders and will ultimately increase access to mortgages for creditworthy borrowers."

Under the new rules announced Tuesday, lenders will have the ability to appeal a mortgage-related penalty to an independent arbiter, a step meant to speed up the resolution of disagreements between regulators and lenders.

Fannie and Freddie don't make mortgages. They buy them from lenders, wrap the loans into securities and provide guarantees to make investors whole if the loans default.

When Fannie and Freddie determine that a lender has made mistakes on a mortgage or that it doesn't meet their requirements, the companies have sometimes forced lenders to buy the loans back.

As billions in loans defaulted during the financial crisis, Fannie and Freddie said many of the mortgages didn't meet their requirements. That, combined with major lawsuits and federal settlements, prompted some lenders to pull back from making some mortgages to categories of borrowers eligible for federal backing but more prone to default.

Even with the changes to the dispute process, however, some mortgage experts doubt that borrowers will see greatly expanded mortgage access.

Fannie and Freddie will back loans to borrowers with a credit score of as low as 620, on a scale of 300 to 850. Before the changes were implemented, some large banks hit with the hardest penalties set higher credit score cutoffs or imposed other requirements that excluded riskier borrowers.

Rather than limit mortgage access, that instead shifted more business to smaller nonbank lenders that didn't experience severe penalties after the mortgage crisis, said Mark Calabria, director of financial regulation studies for the Cato Institute, a libertarian think tank.

Although it remains difficult for less-creditworthy borrowers to get a mortgage, without the FHFA's effort, lenders might have pulled back from the mortgage market even further, said Michael Calhoun, president of the Center for Responsible Lending, which advocates for broader loan access.

Fannie and Freddie "need to do a lot more, but it does remove what was a huge impediment and stops further contraction," Mr. Calhoun said.

Some lenders have said that Fannie's and Freddie's changes have led them to feel more comfortable lending to riskier borrowers.

Bill Emerson, CEO of Quicken Loans Inc., said the nonbank lender now will make any loan that Fannie and Freddie will accept. Mr. Emerson said Quicken never had severe restrictions on mortgages backed by the companies but that could have changed without the FHFA's moves of the last couple of years.

Franklin Codel, head of home lending for Wells Fargo & Co., said in an email that the change "brings greater certainty and strengthens the home lending system."

The process of allaying lenders' concerns on penalties and broadening mortgage access began in 2012 but has ramped up since Mr. Watt took the helm of the FHFA in 2014.

In 2013, the agency said lenders wouldn't face buybacks as long as the borrower didn't miss a payment for three years except in cases of fraud, and later said that borrowers could miss up to two, nonconsecutive payments.

In 2014, the agency reached an agreement with lenders on what would constitute fraud. Last year, the FHFA defined the severity and associated costs for various mistakes, opening the possibility for lenders to receive a less onerous penalty for smaller problems.

Now, under Tuesday's agreement, Fannie, Freddie and lenders will go to an independent arbiter in cases where they still disagree on whether a mortgage had a mistake. That takes some power away from Fannie and Freddie, which previously were the final deciders unless a lender tried to take the companies to court.