[June 23, 2009]

MEMORANDUM TO: Board of Directors

FROM: Sandra L. Thompson
Director

SUBJECT: Interagency Interim Rule on Capital Maintenance: Residential Mortgage Loans Modified Pursuant to the Making Home Affordable Program of the U.S. Department of Treasury

SUMMARY

Proposal: That the Board of Directors (Board) of the Federal Deposit Insurance Corporation (FDIC) approve the attached joint interagency Interim Rule (Rule) titled, *Capital Maintenance: Residential Mortgage Loans Modified Pursuant to the Making Home Affordable Program of the U.S. Department of Treasury* (Treasury). If approved, the Rule would be published in the *Federal Register* by the FDIC, the Board of Governors of the Federal Reserve System (FRB), the Office of Thrift Supervision (OTS), and the Office of the Comptroller of the Currency (OCC) (together, the Agencies) and would include a 30-day comment period.

Under the Agencies' general risk-based capital rules, a banking organization may assign a 50 percent risk weight to loans that are fully secured by first liens on one-to-four family residential properties (either owner occupied or rented) and that meet other prudential criteria. Mortgage loans that do not qualify for the 50 percent risk weight are assigned a 100 percent risk weight.

The Interim Rule provides that a mortgage loan modified under the Making Home Affordable Program (Program) will retain the risk weight assigned to the loan prior to the modification, so long as the loan continues to meet other applicable prudential criteria. The Rule would not change the existing regulatory capital treatment for state nonmember banks under 12 C.F.R Part 325, Appendix A. Accordingly, the revisions effected by the Rule are only clarifying in nature for the FDIC.

The Agencies have provided an opportunity for comment on all aspects of this Rule.

Recommendation: That the Board approve publication of this Interim Rule, which includes a public comment period of 30 days.

Concur:

____

Michael Bradfield
General Counsel

Discussion

Background

On March 4 and April 28, 2009, the Treasury announced guidelines under the Making Home Affordable Program (Program) to promote sustainable loan modifications for homeowners at risk of losing their homes due to foreclosure. The Program guidelines provide a detailed framework for modifying first- and second-lien mortgages on owner-occupied residential properties and offer incentives to lenders, servicers, and borrowers that participate in the Program. These incentives are designed to encourage participation in the Program and promote sustainable loan modifications for homeowners at risk of foreclosure, and balance the interests of borrowers, servicers, and lenders. As of April 28, 2009, twelve servicers, including the five largest, have signed contracts and begun modifications under the Program.[1]

Under the Agencies' general risk-based capital rules, a banking organization may assign a 50 percent risk weight to loans secured by a first-lien on one-to-four family residential property that is either owner-occupied or rented and meets certain prudential criteria.[2] If a banking organization holds both a first- and junior-lien mortgage on the same property and no other party holds an intervening lien, both loans are treated as a single loan secured by a first-lien mortgage and risk weighted at 50 percent if the two loans, when aggregated, satisfy the criteria for the 50 percent risk weight. Other junior-lien mortgage loans receive a 100 percent risk weight.

If a mortgage loan does not qualify for a 50 percent risk weight, a bank must assign it to the 100 percent risk weight category. However, staff notes that there are slight variations among the agencies risk-based capital rules in the criteria for determining whether a mortgage loan qualifies for a 50 percent risk weight. Specifically, the OCC and FRB capital rules provide that a mortgage loan that is restructured through a loan modification does not qualify for a 50 percent risk weight, whereas the FDIC and OTS capital rules permit a bank or savings association to assign a 50 percent risk weight to a modified mortgage loan. Furthermore, where a mortgage loan is placed on non-accrual and must be risk weighted at 100 percent, the FDIC permits a bank to restore the 50 percent risk weight once the borrower has demonstrated timely payment for 6 consecutive payment intervals.

Interim Rule

The Agencies' staffs believe that that the incentives provided by Treasury significantly reduce the credit risk associated with mortgage loans modified pursuant to Program guidelines. Accordingly, the Agencies' staffs have developed this Interim Rule to provide that a mortgage loan modified under the Program will retain the risk weight assigned to the loan prior to the modification, so long as the loan continues to meet other applicable prudential criteria.

---

[1] See U.S. Department of the Treasury Press Release, "Obama Administration Announces New Details on the Making Home Affordable Program" (April 28, 2009).
[2] See 12 CFR part 325, Appendix A (FDIC).

The Interim Rule would not change the existing regulatory capital treatment for state nonmember banks under 12 C.F.R Part 325, Appendix A. The Interim Rule simply clarifies the FDIC's current risk-based capital rules with respect to mortgage loans that are modified. FDIC staff recommends joining this Interim Rule to minimize any confusion about the risk-based capital treatment of mortgage loans modified under the Program.

RECOMMENDATION

Staff recommends that the Board of Directors of the Federal Deposit Insurance Corporation approve the publication of the attached Interagency Interim Rule on *Capital Maintenance: Residential Mortgage Loans Modified Pursuant to the Making Home Affordable Program of the U.S. Department of Treasury*, which includes a public comment period of 30 days.

DSC Contacts:	Nancy Hunt (ext. 86643) Ryan Sheller (ext. 86614)
Legal Division Contacts:	Mark Handzlik (ext. 83990) Michael Phillips (ext. 83581)