National Consumer Reporting Association

Problems in Credit Documentation for Short Sales

(Revised Position June 12, 2013)

Problem: There are no unique codes documenting short sales, or pre-foreclosure sales in the Metro2 coding system used by the credit reporting industry. Utilized for recording the details of consumers' credit history, these codes were developed by the Consumer Data Industry Association (CDIA) with the cooperation of the three national credit reporting agencies. The codes currently in use to designate a short sale were previously used to denote a foreclosure. As a result, automated underwriting systems misinterpret a short sale transaction as a foreclosure, thereby shortchanging consumers who would be eligible for a new mortgage under the shorter timeframes associated with a short sale rather than the longer timeframe associated with a foreclosure. The prolonged waiting period is most evident with a conventional loan, where an eligible past short seller with 20 percent down can get another mortgage after only a **two** year wait, rather than the **seven** year wait after a foreclosure.

The Metro2 system is periodically updated with new codes to document new credit reporting circumstances. Although the lack of a Metro2 short sale code has been acknowledged as early as May of 2009[1], it continues to stall the growth of the economy; an estimated 2.2 million past short sellers are ready to reenter the housing market but are blocked from doing so because they are being forced to wait the longer timeframe associated with a foreclosure. Most complex transactions have had multiple Metro2 codes; there are more than 30 specific codes related to bankruptcy variations, but only three borrowed foreclosure codes to report a short sale. Considering the magnitude of the financial crisis and the millions of short sales that are a by-product of it, it is past time for this problem to be addressed by adding a new specific code to properly document short sales and improve credit reporting accuracy. The gap in codes to designate short sales is delaying millions of potential homebuyers from re-entering the housing market and impedes the recovery of our broader economy.

Solution: This is a complex problem that requires a dual solution: both a short term fix and a longer term fix, with the long term fix having two options.

[1]Chapter IV: HAFA MHA Handbook, v4 1 p.165, Section 11.2: Credit Bureau Reporting: "Because CDIA's Metro 2 format does not provide an Account Status code allowable value for a short sale, a short sale should be identified with the reporting of Special Comment Code "AU.""

A short term solution would be for the Federal Housing Finance Agency (FHFA) to issue guidance to the banking industry participants that they regulate and to whom they recently provided new short sale guidelines, to allow Fannie Mae and Freddie Mac loan holders to proceed with a short sale while being current with an acceptable hardship, per the August 21, 2012 "New Standard Short Sale Guidelines for Fannie Mae and Freddie Mac" guidelines that became effective Nov. 1, 2012. This guidance would require lenders to provide a letter to the consumer at the time of the short sale closing saying that this was in fact a short sale and not a foreclosure. This letter can be used by mortgage credit reporting agencies to correct the improper recording for the consumer when the consumer has restored their credit worthiness and is seeking to re-enter the housing market. This is a cumbersome process, but can be implemented fairly quickly by FHFA. The guidance also needs to instruct lenders to issue that same clarification letter, when requested by the consumer, be issued for all short sale loans that have previously closed.

The original longer term solution would be to require that a short sale specific code be created so the consumers who have gone through this process have their loans clearly documented as a short sale and not as a foreclosure. This needs to be a new, unique code and not a similar and previously used code which led to the current confusion. The creators of the coding system, CDIA, are in control of this system and have been reluctant to create these codes despite the problems being caused by the lack of the code.

(Revised solution) Since this appears to be a Fannie Mae issue more than Freddie Mac or other automated underwriting (AU) systems. A quicker option for a long term solution is for Fannie Mae to change their AU to properly recognize the codes in use for short sales. While this solution also has some issues, it appears to offer less problems and quicker systemic resolution to the situation to allow a quicker recovery to the housing marked. If Fannie Mae is unable to make the adjustment, or if other AU's are found with similar problems, the need for a new code is still possible.

How we would like you to help: Join a colleague letter to the FHFA requesting that they issue a directive to follow their guidance in the August 21, 2012 "New Standard Short Sale Guidelines for Fannie Mae and Freddie Mac" effective Nov. 1, 2012. This letter would be copied to the FTC and/or the CFPB as regulators of the credit reporting industry to urge them to express the need for the development of these codes as quickly as possible and for FHFA to issue this guidance.

As the regulator for Fannie Mae, FHFA has the ability to get the problem resolved at the Fannie Mae AU level much faster than via the new code.