

Selling Guide Announcement SEL-2016-01

February 2, 2016

Lender Selling Representations and Warranties Framework – Independent Dispute Resolution

Fannie Mae, jointly with Freddie Mac, and at the direction of the Federal Housing Finance Agency, is announcing the Independent Dispute Resolution (IDR) process, which completes the planned scope for the origination defects and remedies framework (the “remedies framework”). This also represents completion of the development phase of the overall representations and warranties framework. Incremental refinements to these frameworks may arise as the GSEs continue to work with lenders on implementation. The following announcements describe the framework (and have been incorporated into the *Selling Guide* accordingly):

- SEL-2012-08, *New Lender Selling Representations and Warranties Framework*;
- SEL-2014-05, *Lender Selling Representations and Warranties Framework Updates*;
- SEL-2014-14, *Lender Selling Representations and Warranties Framework Updates*; and
- SEL-2015-11, *Selling Representations and Warranties Framework – Origination Defects and Remedies*.

The IDR process is specifically designed to address alleged loan-level breaches of selling representations or warranties that remain unresolved after completion of the appeals process. The IDR process will not replace the Government Sponsored Enterprises’ (GSEs) current quality control and related appeal processes, but will offer a neutral third party to resolve demands that remain unresolved after the appeal and escalation processes have been exhausted.

Early this year, Fannie Mae will update the appeal and escalation processes to more clearly describe the opportunities for a lender to appeal a repurchase demand as well as an opportunity for escalation to management in order to resolve as many disputes as possible before any IDR process begins.

Lenders remain responsible for underwriting and delivering investment quality mortgage loans in accordance with the terms of the Lender Contract. Additionally, the refined appeal and IDR process described in this Announcement applies only to selling-related disputes and does not affect any servicing duties, responsibilities, obligations, or change the servicing appeal process at this time. However, it is anticipated that an IDR process will become available for servicing-related disputes in the future.

Effective Date

The IDR process will be available for whole loans purchased, and mortgage loans delivered into MBS with pool issue dates, on and after January 1, 2016.

Background

Over the last several years, the GSEs introduced and refined the representations and warranties framework and recently introduced the remedies framework. As part of this effort, Fannie Mae listened closely to lender concerns about the impact that loan repurchases have had on mortgage lending, and understand the need to address these concerns in ways that are mutually satisfactory.

The IDR process announced today provides lenders an opportunity to elect a final, binding resolution to disputes regarding loan-level origination defects through a process that is more streamlined and cost-efficient than litigation. While almost all disputes will likely be resolved through the existing appeals and escalation processes, and the IDR process is not expected to be used with any frequency, there is value for both lenders and Fannie Mae in having an established process with clear expectations and costs for the parties involved. These changes will enable lenders to manage risk more effectively.

Overview of the Process

The first step in the process begins when Fannie Mae identifies a significant defect and issues a demand for repurchase or other remedy to a lender. Fannie Mae has an obligation to support the claim of a significant defect in accordance with the revised requirements recently published in the *Selling Guide*.

The lender then has an opportunity, within certain time limits and in the manner outlined in the Guide, to correct the defect or appeal the demand. The lender has the obligation to support its appeal or correction with documentation that meets the requirements of the Guide.

If the dispute is not resolved through the initial appeal from the lender and corresponding response from Fannie Mae, the process continues through a second opportunity for the lender to appeal, rebut, or provide further evidence that the defect does not exist or has been corrected. For a much smaller group of mortgage loans not resolved by the end of the second appeal, an escalation process provides another opportunity for resolution.

If the dispute is not resolved after all those steps are completed, then if elected by the lender or Fannie Mae, the IDR process will be the final step in the resolution process.

Overview of the IDR Process

The IDR process will be available to all active lenders unless they

- have been suspended, disqualified, terminated, or formally notified as being in default of the terms of their contract;
- have failed to timely comply with a demand after the time for challenging a demand has expired; or
- are in default of a prior IDR award or have any outstanding amount past due to the IDR administrator.

The IDR process will include the following components:

- prescribed timelines for initiating the process, selecting a neutral arbitrator, and conducting administrative and planning conference calls;
- standards for case packages that must be prepared;
- an option for each party to use legal counsel and subject matter experts;
- a hearing with a neutral arbitrator and representatives from the lender and Fannie Mae conducted by telephone or video conference;
- a process for creating a collective proceeding for a group of mortgage loans that involve similar disputes (“expanded proceedings”) with the agreement of Fannie Mae and the lender;
- written award and brief opinion provided by the arbitrator; and
- reimbursement for certain costs and expenses by the non-prevailing party to the prevailing party.

The arbitrator rather than Fannie Mae will be making the final determination about whether a defect existed at the time IDR begins. The written award from the arbitrator will be final and binding upon and enforceable against the non-prevailing parties.



In addition to resolution of the demand, the party that does not prevail at the hearing will be responsible for paying the prevailing party a “Cost and Fee Award” in the amount of 10% of the unpaid principal balance of the related mortgage loan at the time the loan was acquired. If the parties mutually agree to expanded proceedings to cover multiple mortgage loans, then the parties will negotiate an appropriate Cost and Fees Award before the IDR process begins.

Selling Guide Updates

Specific changes related to the incorporation of the IDR process, including support for the arbitrator’s authority to make conclusive and binding decisions and changes to the broader appeals process, will be made to the *Selling Guide* in the coming months.

Lenders who have questions about this Announcement should contact their Account Team.

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