

CHAPTER 5. LOSS MITIGATION

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### 5.01 VA LOSS MITIGATION WATERFALL

a. When a borrower experiences repayment difficulty, the servicer must proceed through the numbered steps of the VA Loss Mitigation Waterfall (Waterfall). The servicer must review the loan and contact the borrower to ask a series of questions. Based on the borrower's responses, the servicer must offer the loss mitigation option specified by the Waterfall. A servicer may contact VA for further evaluation of a loan, on a case-by-case basis.

1. If the loan is less than three (3) full months past due, the servicer will only follow Steps 1 through 5 of the Waterfall. Steps 6 through 8 are not available.

2. If the loan is three (3) or more full months past due, the servicer must follow Steps 1-8 of the Waterfall. The options outlined in Steps 6 through 8 are only available for loans that are at least three (3) full months past due.

b. Each time the servicer reviews the loan under the Waterfall, the servicer must start at Step 1.

#### **1. STEP 1: ALTERNATIVES TO FORECLOSURE**

(a) The servicer asks the borrower if they wish to retain their home. If the borrower wishes to retain their home, the servicer proceeds to Step 2.

(b) If the borrower does not wish to retain their home, the servicer discusses alternatives to foreclosure to include a private sale, short sale, and deed-in-lieu of foreclosure (DIL).

#### **2. STEP 2: DETERMINE BORROWER'S READINESS FOR HOME RETENTION**

(a) The servicer asks if the borrower's reason for default has been resolved and if the borrower can resume making their current monthly mortgage payments within the next 90 days. If the borrower's reason for default has been resolved and the borrower can resume making payments, the servicer proceeds to Step 3.

(b) If the borrower's reason for default has not been resolved or the borrower cannot resume making monthly mortgage payments within the next 90 days, the servicer discusses alternatives to foreclosure to include a private sale, short sale, and DIL.

#### **3. STEP 3: REVIEW FOR SPECIAL FORBEARANCE**

(a) The servicer asks if the borrower can afford to repay the missed payments in a lump sum. If the borrower can afford to repay the missed payments in a lump sum, the servicer offers the borrower a Special Forbearance. If the borrower refuses the Special

Forbearance, the servicer discusses alternatives to foreclosure to include a private sale, short sale, and DIL.

(b) If the borrower cannot afford to repay the missed payments in a lump sum, the servicer proceeds to Step 4.

#### **4. STEP 4: REVIEW FOR REPAYMENT PLAN**

(a) The servicer asks if the borrower can afford the current monthly mortgage payment, plus additional amounts, until the loan is current. If the borrower can afford the current monthly mortgage payment, plus additional amounts until the loan is current, the servicer discusses a Repayment Plan with the borrower. VA encourages servicers to consider extended terms up to 24 months for a Repayment Plan, to allow a more affordable payment for the borrower. If the borrower can afford the servicer's terms, then the servicer offers the borrower a Repayment Plan. If the borrower can afford the terms but does not agree to the Repayment Plan, the servicer offers alternatives to foreclosure or proceeds to foreclosure, as appropriate.

(b) If the borrower cannot afford the terms of the Repayment Plan, the servicer proceeds to Step 5.

#### **5. STEP 5: REVIEW FOR TRADITIONAL VA MODIFICATION**

(a) The servicer reviews the loan to determine if the terms can be modified under a Traditional VA Modification and keep the current monthly principal and interest payment the same or lower. If so, the servicer offers a Traditional VA Modification, subject to the successful completion of a Trial Payment Plan (TPP). If the borrower does not agree to the Traditional VA Modification, the servicer offers alternatives to foreclosure or proceeds with foreclosure, as appropriate.

(b) If the Traditional VA Modification would result in an increase to the current monthly principal and interest payment and the borrower is less than three (3) full months past due, the servicer again discusses a Repayment Plan with the borrower. VA encourages servicers to consider extended terms up to 24 months for a Repayment Plan, to allow a more affordable payment for the borrower. If the borrower does not agree to the terms of the Repayment Plan, the servicer discusses alternatives to foreclosure because only Steps 1 through 5 are available on a loan that is less than three (3) full months past due.

(c) If the Traditional VA Modification would result in an increase to the current monthly principal and interest payment and the borrower is at least three (3) full months past due, the servicer proceeds to Step 6.

**6. STEP 6: REVIEW FOR 30-YEAR MODIFICATION**

(a) The servicer reviews the loan to determine if the modified terms under a 30-Year Modification would result in no more than a 15% increase to the monthly principal and interest payment. (A reduction or no change to the monthly principal and interest payment is also allowed.) If so, the servicer offers the borrower the 30-Year Modification, subject to the successful completion of a TPP. If the borrower does not agree to the 30-Year Modification, the servicer offers alternatives to foreclosure or proceeds to foreclosure, as appropriate.

(b) If the 30-Year Modification would result in an increase of more than 15% to the monthly principal and interest payment, the servicer proceeds to step 7.

**7. STEP 7: REVIEW FOR VA PARTIAL CLAIM**

(a) The servicer reviews the loan to determine if the loan and borrower meet the qualifying criteria for a VA Partial Claim. If so, the servicer offers the borrower a VA Partial Claim, subject to the successful completion of the TPP. If the borrower does not agree to the VA Partial Claim, the servicer offers alternatives to foreclosure or proceeds to foreclosure, as appropriate.

(b) If the qualifying criteria for a VA Partial Claim are not met, the servicer proceeds to Step 8.

**8. STEP 8: REVIEW FOR 40-YEAR MODIFICATION**

(a) The servicer reviews the loan to determine the terms under a 40-Year Modification. The servicer discusses the 40-Year Modification with the borrower. If the borrower can afford the servicer's terms, then the servicer offers the borrower the 40-Year Modification, subject to the successful completion of a TPP.

(b) If the borrower cannot afford the terms of the 40-Year Modification or if the borrower can but chooses not to agree to the terms, the servicer offers alternatives to foreclosure or proceeds with foreclosure, as appropriate.

(c) This is the final step in the Waterfall.

c. RE-ENTERING THE WATERFALL: Borrowers who failed to successfully complete a loss mitigation option or TPP, or who failed to take the necessary actions to finalize a home retention option may be reviewed for loss mitigation options again.

1. Subject to section 5.01 c.2., servicers must use the Waterfall to review borrowers again when all the following conditions are present:

(a) the servicer establishes contact with the borrower,

(b) the borrower wants to be reviewed for loss mitigation options, and

(c) the borrower indicates their financial circumstances have changed since the most recent review under the Waterfall.

2. If during the current default episode, the servicer reviewed the borrower under the Waterfall and the borrower was offered three (3) or more loss mitigation options that were unsuccessful (including alternatives to foreclosure), the servicer must request documentation from the borrower prior to offering any additional options within the Waterfall. The supporting documentation must confirm the household income supports the household expenses (e.g. servicer verifies all sources of income contributing to the household and considers the overall expenses impacting the household budget) and confirm the reason for default has been resolved.

For example, the borrower has been behind on payments since January 1, 2024. In June 2024, the borrower was offered a Special Forbearance, but the borrower was not able to reinstate the loan. In July 2024, the servicer offered the borrower a 30-Year Loan Modification, but the borrower did not accept the offer. In December 2024, the borrower was offered a Repayment Plan, but the borrower did not accept the servicer's terms of the Repayment Plan. In March 2025, the servicer reviewed the borrower under the Waterfall, and the review directed the servicer to the VA Partial Claim. Before offering the Partial Claim TPP, the servicer must obtain the documentation mentioned above.

(a) If the borrower is unable or unwilling to provide documentation, the servicer offers alternatives to foreclosure or proceeds with foreclosure, as appropriate.

(b) If the documentation does not confirm the household income supports the household expenses or does not confirm the reason for default has been resolved, the servicer offers alternatives to foreclosure or proceeds with foreclosure, as appropriate.

(c) If the documentation confirms the household income supports the household expenses and the reason for default has been resolved, but the servicer believes that offering an additional home retention option will not bring the loan current, the servicer can request PreApproval to proceed with alternatives to foreclosure or foreclosure, as appropriate. For more information on PreApprovals, refer to Chapter 6 of this Manual.

(d) If the servicer offers a loss mitigation option during the Waterfall review and the borrower does not agree to the terms or accept the option, this counts toward the total options offered.

(e) Failing a TPP, Special Forbearance, or Repayment Plan is considered an offered loss mitigation option and counts toward the total options offered. Failing to take the necessary actions to finalize a home retention, such as executing a loan modification agreement, is also considered an offered loss mitigation option and counts toward the total options offered.

3. Servicers must use the Waterfall to review borrowers who were offered an alternative to foreclosure but who later indicate an intention to retain home ownership, if the borrower’s financial circumstances have changed and the borrower is able to resume making regular mortgage payments.

d. DISASTER MODIFICATIONS. Servicers may offer the VA Disaster Modification or the Disaster Extend Modification options to borrowers who have been affected by a Presidentially declared disaster. VA does not require the servicer to review the Waterfall before offering these options.

e. Reference for VA Loss Mitigation.

<u>Loss Mitigation</u>	<u>Loss Mitigation Details</u>	<u>Home Retention</u>	<u>Requires 3 Month Delinquency</u>	<u>Requires Successful TPP</u>	<u>Limited/ One Time Use</u>
Special Forbearance	Chapter 5.04	x			
Repayment Plan	Chapter 5.05	x			
VA Traditional VA Modification	Chapter 5.06(b)	x		x	
30-Year Modification	Chapter 5.06(c)	x	x	x	
VA Partial Claim	Chapter 22	x	x	x	x
40-Year Modification	Chapter 5.06(d)	x	x	x	
VA Disaster Modification	Chapter 5.06(e)	x		x	
Disaster Extend Modification	Chapter 5.06(f)	x			
Short Sale	Chapter 5.08				x
Deed-in-Lieu of Foreclosure	Chapter 5.09				x

5.02 LOSS MITIGATION

a. The loss mitigation process includes a review of both home retention options and alternatives to foreclosure. Home retention options include Repayment Plans, Special Forbearances, all loan modification types, and VA Partial Claims. Additional Information on VA Partial Claims can be found in Chapter 22 of this Manual. Alternatives to foreclosure include short sales, and DIL of foreclosure.

b. VA technicians may become involved in the loss mitigation process when:

1. Borrowers contact VA directly to request assistance; or

2. The VA-assigned technician determines that a loss mitigation option should be pursued after reviewing the Adequacy of Servicing (AOS) or Pre-Foreclosure process on the loan.

c. When a borrower wants to remain in the home, servicers must review and offer home retention options as outlined in the Waterfall. This Waterfall can be found in section 5.01 of this chapter and requires minimal documentation from the borrower. Servicers must

not collect financials and/or additional documents that are not outlined by VA. Home retention options include:

1. Special Forbearance.
2. Repayment Plan.
3. All loan modification types.
4. VA Partial Claim.

d. If servicers encounter a situation where they believe it is in the best interest of the borrower and VA to deviate from the Waterfall, they must request pre-approval through the VA Loan Electronic Reporting Interface (VALERI) application. For more information on pre-approvals, review chapter 6 of this manual.

e. If the servicer and the borrower cannot resolve the delinquency through a home retention option or the borrower no longer wishes to retain the home, the servicer must consider the viability of alternatives to foreclosure before taking action to foreclose the loan. Alternatives to foreclosure include:

1. Short sale.
2. DIL.

f. When servicers report to VALERI a home retention event through their nightly file and the loan reinstates, VALERI generates a Default Cured/Loan Reinstated (DCLR) event.

If servicers report a home retention event manually through the VALERI Events Bulk Upload Templates, the servicer must also report the Default Cured/Loan Reinstated event after the home retention event has cured the loan.

VA will determine whether a servicer qualifies for an incentive payment after the default is cured through the Default Cured/Loan Reinstated event. Regarding incentives paid for alternatives to foreclosure, VA will determine whether the servicer qualifies for an incentive payment after the servicer reports an alternative to foreclosure event.

g. When loss mitigation options are not feasible, the servicer must immediately refer the loan to foreclosure to reduce potential losses to the Government and to ensure the borrower's indebtedness is not unduly increased. VA encourages servicers to continue to pursue loss mitigation options even after initiating the foreclosure process. Any new loss mitigation reviews start at Step 1 of the Waterfall.

h. Upon completion of any loan modification or alternative to foreclosure on a loan that is less than 61 days delinquent, the servicer must report the Electronic Default Notice

(EDN) event by choosing imminent default or property problems as the reason for default. The EDN must be submitted prior to reporting the Loan Modification Complete event or alternatives to foreclosure. VA does not require the Special Forbearance or Repayment Plan events to be reported for a loan that is less than 61 days delinquent.

i. Loans that have been reported with an EDN using the VALERI Events Bulk Upload will not automatically generate the Default Cured Loan Reinstated (DCLR) event. Servicers must manually report the DCLR event when the loan reinstates.

j. Information on loss mitigation event reporting can be found in Chapter 2 of this Manual.

### 5.03 ACCEPTANCE OF ELECTRONIC SIGNATURES

a. VA has no objection to the use of electronic signatures on repayment, forbearance, or modification agreements between servicers and borrowers, provided they are readily identifiable during a Post Audit review. The Electronic Signatures in Global, and National Commerce Act (15 U.S.C. § 7001) provides that with respect to any transaction in, or affecting interstate, or foreign commerce that "a signature, contract, or other record relating to such transaction may not be denied legal effect, validity, or enforceability solely because it is in electronic form." However, VA cautions servicers to ensure compliance with all regulations governing VA-guaranteed home loans, including the requirement to obtain and maintain a lien of proper dignity (38 C.F.R. § 36.4354), which requires compliance with all federal, State, and local laws, especially concerning contracts and the documenting of modifications to existing loans.

### 5.04 SPECIAL FORBEARANCE (38 C.F.R. §36.4301)

a. A Special Forbearance is a documented agreement, by, and between the borrower and holder where the holder agrees to suspend all payments or accept reduced payments for 1 or more months on a loan that is 61 or more calendar days delinquent (a reportable default), and the borrower agrees to pay the total delinquency at the end of the specified period or enter into a Repayment Plan. To qualify for an incentive, the Special Forbearance must be established for at least 30 days. No events should be reported when a Special Forbearance is approved on a loan before it reaches 61 days delinquent.

b. During the forbearance period, servicers must monitor the agreement and take appropriate action if the borrower does not comply. Agreements may be renegotiated at any time.

c. Servicers must offer the Special Forbearance when the borrower agrees to repay the missed payments in a lump sum, as outlined in the Waterfall.

5.05 REPAYMENT PLAN (38 C.F.R. §36.4301)

a. A Repayment Plan is a documented agreement by and between the borrower and the holder to reinstate a loan that is 61 or more calendar days delinquent (a reportable default), by requiring the borrower to pay the normal monthly payment, plus an agreed upon portion of the delinquency, each month. To qualify for an incentive, the Repayment Plan must be established for at least a three-month period. No events should be reported when a Repayment Plan is approved on a loan before it reaches 61 days delinquent.

b. If the loan's current interest rate is less than the current Maximum Allowed Modified Rate, as outlined in 38 C.F.R. § 36.4315(a)(8)(i), servicers are encouraged to offer Repayment Plans with terms up to 24 months. Extending the terms of the Repayment Plan up to 24 months will provide borrowers with a more affordable option to reinstate the loan, without raising their interest rate.

c. During the repayment agreement, servicers must monitor the agreement each month and take appropriate action if the borrower does not comply. Plans may be renegotiated at any time.

d. Servicers must discuss and offer, if appropriate, the Repayment Plan when the borrower indicates they can repay the current loan payment plan plus additional amounts to bring the loan current, as outlined in the Waterfall.

5.06 LOAN MODIFICATIONS (38 U.S.C. 3720(a)(2))

a. A loan modification is a documented agreement by and between the holder and all obligors on the loan, which permanently changes one or more of the terms of a loan, and may include re-amortization of the balance due. VA considers the execution date of the loan modification agreement to be the date of the borrower's signature. The loan modification must be consistent with this Manual and sound lending practices. If the loan originated prior to January 1, 1990, and includes a transferee, servicers must ensure that no previous obligor is released from liability by the completion of a loan modification. All loan modifications must meet the following conditions:

1. The loan is in default.
2. The event or circumstance that caused the default has been or will be resolved and it is not expected to re-occur.
3. The loan modification will reinstate the loan and cure the default.
4. The current owner(s) is obligated to repay the loan and is party to the loan modification agreement.
5. The servicer cannot charge a processing fee and must waive all unpaid late fees. Any other actual costs that are incurred by the servicer but cannot be capitalized in the

modified indebtedness, may be collected directly from the borrower or waived, at the discretion of the servicer, if they were legally chargeable under applicable law.

6. The servicer has ensured the first lien position remains intact.

7. The guaranty dollar amount will not exceed the greater of:

(a) The original guaranty amount of the loan being modified (if loan modified amount is less than the original loan amount, the amount of guaranty will be equal to the original guaranty percent applied to the modified loan amount), or

(b) 25 percent of the loan being modified subject to the statutory maximum specified at 38 U.S.C. § 3703(a)(1)(B).

8. Borrower does not receive any cash back from the modification.

9. The property securing the mortgage loan must not have been abandoned or condemned.

10. Unless specifically noted in this chapter, the general loan modification provisions outlined in 38 C.F.R. § 36.4315 apply. VA notes that market circumstances can change rapidly, meaning that the regulation is not a limitation on the Secretary's statutory discretion in 38 U.S.C. § 3720(a)(2) to consent to various terms of modification. If it were, the Secretary would not be able to adjust to the market circumstances in real time, at the speed of business, and Veterans could be at serious risk of foreclosure, solely due to bureaucratic obstacles. Thus, servicers must stay apprised of all the terms to which VA consents via regulation and administrative guidance (such as this Manual and VA Circulars).

(a) If a requirement for a loan modification is not met but the servicer believes the option would be in the best interest of the borrower and the Government, the servicer must submit a request for pre-approval consideration in VALERI for VA review. Refer to Chapter 6 of this Manual for more information on pre-approvals.

(b) While a servicer must take steps, as outlined in the Waterfall above, to confirm the borrower can afford the payment, servicers are not required to evaluate borrower creditworthiness under other criteria.

11. Standard servicer incentives for a completed modification will apply. Refer to Chapter 7 of this Manual for more information on incentives.

12. Servicers must offer the appropriate modification, as outlined in the Waterfall in section 5.01 of the chapter. The modification options in the Waterfall and further described below are those for which VA provides advance consent to servicers. VA's advance consent means that a servicer does not need to submit a proposed modification to VA for prior approval if the conditions are met.

13. Servicers can request Pre-Approval to proceed with a modification that does not conform to the loan modifications requirements listed below. VA technicians will review each request and make a determination based on what VA believes would be the best outcome for the borrower and VA. For more information on the Pre-Approval process, review Chapter 6 of this Manual.

b. TRADITIONAL LOAN MODIFICATION

1. When the borrower indicates the ability to afford the current mortgage payments but does not have the funds to reinstate the past due amount or repay additional funds each month, servicers must review for the Traditional VA Modification. If the modification does not increase the monthly principal and interest payment, the servicer must offer the borrower a Trial Payment Plan (TPP) that, if successful, will result in a traditional loan modification. Servicers must offer the Traditional VA Modification upon successful completion of the TPP.

If the borrower has an adjustable rate mortgage (ARM), the Traditional VA Modification monthly principal and interest payment cannot exceed the current monthly principal and interest payment.

2. The modified loan must bear a fixed-interest rate. The rate must not exceed the weekly Freddie Mac Primary Mortgage Market Survey Rate for 30-year fixed rate conforming mortgages, rounded to the nearest one-eighth of one percent (0.125%), as of the date the modification TPP is approved, plus 50 basis points. The posted maximum allowable interest rate will be effective Friday through Thursday. Servicers may offer an interest rate below the maximum allowable rate at their discretion, without VA preapproval.

3. The unpaid principal balance of the modified loan will be re-amortized over the remaining life of the loan, or if the loan term is to be extended, the maturity date will not exceed the shorter of:

(a) 360 months from the due date of the first installment under the modification, or

(b) 120 months after the original maturity date of the loan (unless the original term was less than 360 months, in which case the term may only be extended to 480 months from the due date of the first installment of the original loan).

4. The borrower must successfully complete a Trial Payment Plan (TPP). Refer to section 5.06 of this chapter for more information on VA requirements for TPPs.

5. The following are not prerequisites for a Traditional Loan Modification:

(a) At least 12 monthly payments have been paid since the closing date of the loan.

(b) A loan has not been modified more than once in a three-year period or more than three times during the life of the loan.

(c) After being determined and selected in accordance with section 5.06 b.2., the fixed-rate of interest is not more than one percent higher than the existing rate on the loan.

c. 30-YEAR MODIFICATION

1. If a Traditional VA Modification would result in an increase to the current monthly principal and interest payment and the loan is at least 3 full months past due, the servicer instead considers the terms for the 30-Year Modification. If the 30-Year Modification results in no more than a 15% increase to the principal and interest payment, the servicer offers the borrower a TPP, which if successful, will result in the 30-Year Modification. Servicers must offer the 30-Year Modification upon successful completion of the TPP. If the borrower has an adjustable rate mortgage (ARM), the 30-Year Modification monthly principal and interest payment can result in no more than a 15% increase to the current monthly principal and interest payment.

2. As with the Traditional Loan Modification, the loan modified under a 30-Year Modification must bear a fixed-interest rate. The rate must not exceed the weekly Freddie Mac Primary Mortgage Market Survey Rate for 30-year fixed rate conforming mortgages, rounded to the nearest one-eighth of one percent (0.125%), as of the date the modification TPP is approved, plus 50 basis points. The posted maximum allowable interest rate will be effective Friday through Thursday. Servicers may offer an interest rate below the maximum allowable rate at their discretion, without VA approval.

3. The unpaid balance of the modified loan will be re-amortized over a term of 360 months.

4. Borrower must successfully complete a TPP. Refer to section 5.06 of this chapter for more information on VA requirements for TPPs.

5. The following are not prerequisites for a 30-Year Modification:

(a) At least 12 monthly payments have been paid since the closing date of the loan.

(b) A loan has not been modified more than once in a three-year period or more than three times during the life of the loan.

(c) After being determined and selected in accordance with section 5.06 c.2., the fixed-rate of interest is not more than one percent higher than the existing rate on the loan.

(d) The maturity date will not exceed the shorter of:

- i. 360 months from the due date of the first installment under the modification, or
- ii. 120 months after the original maturity date of the loan (unless the original term was less than 360 months, in which case the term may only be extended to 480 months from the due date of the first installment of the original loan).

d. 40-YEAR MODIFICATION

1. When the borrower is at least 3 full months past due and wants to retain home ownership but does not qualify for any other home retention options in the Waterfall, the servicer reviews the terms of the 40-Year Modification. If the borrower indicates the ability to afford the terms of the 40-Year Modification, the servicer offers the borrower a TPP, which if successful, will result in the 40-Year Modification. Servicers must offer the 40-Year Modification upon successful completion of the TPP.

2. As with other loan modifications, the 40-Year Modification must bear a fixed-interest rate. The rate must not exceed the weekly Freddie Mac Primary Mortgage Market Survey Rate for 30-year fixed rate conforming mortgages, rounded to the nearest one-eighth of one percent (0.125%), as of the date the modification TPP is approved, plus 50 basis points. The posted maximum allowable interest rate will be effective Friday through Thursday. Servicers may offer an interest rate below the maximum allowable rate at their discretion, without VA pre-approval.

3. The unpaid balance of the modified loan will be re-amortized over a term of 480 months.

4. The modification is offered after successful completion of a TPP. Terms of the TPP are outlined in section 5.06 of this chapter.

5. The following are not prerequisites for the 40-Year Modification:

- (a) At least 12 monthly payments have been paid since the closing date of the loan.
- (b) A loan has not been modified more than once in a three-year period or more than three times during the life of the loan.
- (c) After being determined and selected in accordance with section 5.06 d.2., the fixed-rate of interest is not more than one percent higher than the existing rate on the loan.
- (d) The maturity date will not exceed the shorter of:

- i. 360 months from the due date of the first installment under the modification, or

ii. 120 months after the original maturity date of the loan (unless the original term was less than 360 months, in which case the term may only be extended to 480 months from the due date of the first installment of the original loan).

e. VA DISASTER MODIFICATION – Allows servicers to offer a permanent modification of loan terms to provide payment relief to impacted delinquent borrowers, without requiring the borrower to submit a complete loss mitigation application. All impacted borrowers should have an opportunity to be considered for a VA Disaster Modification.

1. Evaluation of Borrower - Servicer evaluation of the borrower's financial information is not required for a VA Disaster modification. To qualify for the VA Disaster Modification option, borrowers must successfully complete a 3-month TPP. Servicers must offer the VA Disaster Modification upon successful completion of the TPP.

2. Must bear a fixed-interest rate. The rate must not exceed the weekly Freddie Mac Primary Mortgage Market Survey Rate for 30-year fixed rate conforming mortgages, rounded to the nearest one-eighth of one percent (0.125%), as of the date the modification agreement is approved, plus 50 basis points. Servicers may offer an interest rate below the maximum allowable rate at their discretion, without VA prior approval.

3. VA Disaster Modifications can only be offered up to 12 months after the Presidentially-declared disaster.

4. Additional Qualifying Requirements:

(a) The borrower has been impacted by a Presidentially-declared disaster.

(b) The mortgage loan was not more than 30 days past due at the time of the disaster.

(c) Servicers may offer a VA Disaster modification to a borrower if clear evidence exists that the borrower is ready to resume monthly installments.

(d) The borrower must successfully complete a TPP. Refer to section 5.06 of this chapter for more information on VA requirements for TPPs.

(e) The borrower has not submitted a complete loss mitigation application currently under review, and/or is not performing under a default curing loss mitigation option.

5. The following are not prerequisites for a VA Disaster Modification:

(a) At least 12 monthly payments have been paid since the closing date of the loan.

(b) A loan has not been modified more than once in a 3-year period or more than 3 times during the life of the loan.

f. DISASTER EXTEND MODIFICATION – Allows servicers to offer permanent payment relief by extending the maturity date, up to 12 months, to impacted delinquent borrowers, without requiring the borrower to submit a complete loss mitigation application. All impacted borrowers should have an opportunity to be considered for a VA Disaster Modification.

1. Evaluation of Borrower - Servicer evaluation of the borrower's financial information is not required for a Disaster Extend modification. A TPP is not necessary for the Disaster Extend Modification, but the servicer must waive the delinquent interest accrued on the loan as a result of the delinquency.

2. The interest rate must be fixed and not exceed the lesser of:

(a) the borrower's current interest rate;

(b) the most recent Freddie Mac Weekly Primary Mortgage Market Survey Rate for 30-year fixed-rate conforming mortgages, rounded to the nearest one-eighth of one percent (0.125%), plus 50 basis points.

3. The servicer may re-amortize the loan, if necessary, to meet any investor restrictions, as long as the new monthly payment is the same as, or less than, the current monthly installment.

4. VA Disaster Modifications can only be offered up to 12 months after the Presidentially-declared disaster

5. Additional Qualifying Requirements:

(a) The borrower has been impacted by a Presidentially-declared disaster.

(b) The mortgage loan was not more than 30 days past due at the time of the disaster.

(c) Servicers may offer a Disaster Extend Modification to a borrower if clear evidence exists that the borrower is ready to resume monthly installments.

(d) The terms of the loan are extended by the equal number of months the loan is delinquent due to the disaster. For example, if the loan is 4-months delinquent, the loan term may only be extended by 4 months. The limit of the term extension is 12 months, without prior approval from VA.

(e) The modification does not raise the borrower's current interest rate or monthly principal and interest amounts.

(f) Servicer waives the delinquent interest.

(g) The borrower has not submitted a complete loss mitigation application currently under review, and/or is not performing under a default curing loss mitigation option.

6. The following are not prerequisites for the Disaster Extend Modification:

(a) At least 12 monthly payments have been paid since the closing date of the loan.

(b) A loan has not been modified more than once in a 3-year period or more than three times during the life of the loan.

### 5.07 TPP

a. The TPP allows borrowers to demonstrate their ability to make monthly mortgage payments, prior to the completion of a loss mitigation option. TPPs are offered when the Waterfall indicates a need for a TPP and all other qualifying criteria are met for the applicable loss mitigation option. Upon successful completion of a TPP, servicers must offer the appropriate loss mitigation option to the borrower.

b. When a TPP is offered, the servicer must provide to the borrower a written TPP to outline the terms and payment amounts, not later than 15-calendar days from the date that VA accepts the appropriate TPP event in the VALERI application. TPPs must comply with the following requirements:

1. All TPPs will be three (3) consecutive months in duration.

2. TPP payments must equal the full monthly payment that would be due after the applicable loss mitigation option is complete.

(a) VA does not require an escrow analysis prior to establishing a TPP. For loan modifications, the TPP payment includes the current tax and insurance collection (i.e. T&I), plus the principal and interest payment after the modification is complete.

(b) For VA Partial Claims, the TPP payment includes the current tax and insurance collection (i.e., T&I), plus the current principal and interest payment.

3. If the servicer sends the TPP agreement to the borrower on or before the 15th day of a calendar month, the first TPP payment will be due on day 1 of the successive calendar month. If the servicer sends the TPP to the borrower after day 15 of the calendar month, the first TPP payment will be due on day 1 of the successive month following the next month. The remaining two payments will be due on the same day for the next two consecutive months.

For example, if the TPP is sent on January 5, the first TPP payment would be due on February 1. The remaining two TPP payments would be due March 1 and April 1.

As another example, if the TPP is sent on January 17, the first TPP payment would be due on March 1. The remaining two TPP payments would be due April 1 and May 1.

c. Upon receipt of the first TPP payment, the servicer must provide the borrower foreclosure protection, by placing any foreclosure proceedings on hold.

d. The borrower must make each of the 3 scheduled trial payments by the 15th day of the month in which the payment is due.

1. Upon failure of a TPP, the servicer must proceed with delinquent loan servicing.  
Definition of a failed TPP:

(a) Failure to make a payment by the 15th day of the month in which the payment is due.

(b) If the servicer discovers a TPP payment was returned for non-sufficient funds (NSF), the TPP fails. If a servicer has already notified VA of a successfully completed TPP, the servicer must notify VA of the failed plan.

(c) If the borrower files either a Chapter 13 or Chapter 7 bankruptcy before successful completion of the TPP, VA the TPP is failed.

2. If the borrower fails a TPP, the borrower may be reviewed under the Waterfall again, as outlined in section 5.01 c. However, if a borrower has failed three (3) TPPs during the current default episode, the loan can no longer be reviewed for options that require successful completion of a TPP during the current default episode.

e. After successfully completing the TPP, the servicer must provide the borrower with the final loss mitigation agreement.

1. For loan modifications, the servicer must complete the modification agreement so the modification becomes effective on the first day of the second month, following the month the final TPP payment was due. The borrower must sign and return the loan modification agreement before the effective date. If the borrower does not return the executed loan modification agreement before the effective date, the loan is not modified.

For example, if the final TPP payment was due on January 1, the first payment due on the loan modification agreement must be March 1. If the borrower fails to return the executed loan modification agreement by March 1, the modification is denied.

2. For information on the steps following a successful TPP for a VA Partial Claims, review Chapter 22 of this Manual.

3. The borrower is not required to make an additional TPP payment during the (interim) month in between the month the final TPP payment was due and the month in which the loan modification becomes effective.

#### 5.08 SHORT SALE (38 C.F.R. §36.4322(e))

a. A short sale is a sale to a third party for an amount less than the borrower's total eligible indebtedness (TEI) on the loan. This alternative should be considered when a private sale is not feasible due to little or no equity. The servicer must agree to release the lien in exchange for the proceeds of the sale. The servicer may complete a short sale under the following conditions:

1. The servicer has determined the loan insoluble. **Note:** Servicer evaluation of the borrower's financial information is not required if the loan is 60 or more days delinquent, and the borrower has requested a short sale. In those instances, it is not necessary for the servicer to establish employment status, present income of the borrower(s), current monthly expenses of the borrower(s) including household, or debt obligations.

2. The net proceeds equal or exceed the net value of the property securing the loan.

3. The current owner of the property will not receive any proceeds from the sale of the property.

b. Any liquidation appraisal for a property originally scheduled for foreclosure will not require a second appraisal if a subsequent short sale offer is made on the property. The exterior-only liquidation appraisal will be sufficient to complete the short sale without any further delays.

c. If regulatory requirements for a short sale are not met, and the servicer believes the option would be in the best interest of both the borrower and the Government, the servicer must submit a request for pre-approval in VALERI. Refer to Chapter 6 of this Manual for more information on pre-approvals.

d. In any case where the borrower has an outstanding partial claim interest, servicers must submit a request for pre-approval in VALERI. Refer to Chapter 6 of this Manual for more information on pre-approvals. An outstanding partial claim interest includes any of the following:

1. a VA Partial Claim under 38 U.S.C. § 3737;

2. a COVID-19 Veterans Assistance Partial Claim Payment under subpart F, part 36, title 38, C.F.R.; or

3. a COVID-19 Refund Modification.

#### 5.09 DIL (38 C.F.R. §36.4322(f))

a. A DIL is a voluntary transfer of a property from the borrower to the servicer in exchange for a release of all obligations under the mortgage.

b. In cases when a loan is insoluble and there is little or no likelihood of a private sale, consideration should be given to accept a DIL. Completing a DIL may save on foreclosure costs, cut down on possible decreases in the value of the security, and reduce negative impacts to the borrower. A DIL is completed when the borrower executes a deed to the servicer and the deed is sent for recording, or is recorded. VA considers the custody of the property transferred to VA when the servicer reports the Transfer of Custody (TOC) event in VALERI, and the event is accepted. An accepted event will have an event status of Accepted or Requires VA Review. Servicers must submit the full title package to VA's property management contractor. [Refer to the Title Documentation, Insurance, and Timeframe Requirements on the VALERI Internet for additional information.] Servicers may complete a DIL if all the following conditions are met:

1. The loan is insoluble. **Note:** Servicer evaluation of the borrower's financial information is not required if the loan is 60 or more days delinquent, and the borrower has requested a DIL. In those instances, it is not necessary for the servicer to establish employment status, present income of the borrower(s), current monthly expenses of the borrower(s) including household, or debt obligations.

2. The VA net value of the property has been determined by subtracting the estimated costs to VA for the acquisition, and disposition of the property from the "as is" value available on the Notice of Value (NOV).

3. The quantum and quality of the title to the property meet VA's regulatory requirements.

4. An agreement, signed by the borrower, to vacate the property when the deed is recorded or to give possession of the property to VA immediately upon notification to do so.

c. In any case where the borrower has an outstanding partial claim interest, servicers must submit a request for pre-approval in VALERI. Refer to Chapter 6 of this Manual for more information on pre-approvals. An outstanding partial claim interest includes any of the following:

1. a VA Partial Claim under 38 U.S.C. § 3737;

2. a COVID-19 Veterans Assistance Partial Claim Payment under subpart F, part 36, title 38, C.F.R.; or

3. a COVID-19 Refund Modification.

#### 5.10 RELOCATION ASSISTANCE FOR VA BORROWERS

- a. VA authorizes servicers to advance \$1,500 in relocation assistance to borrower occupants who complete a short sale or who execute a DIL. VA will treat this as a

reimbursable expense that may be included in the Basic Claim event in VALERI. More information on requesting reimbursement for the relocation expense can be found in Chapter 14 of this Manual.

b. VA expects servicers to proactively notify borrowers of the availability of alternatives to foreclosure and, where the Waterfall requires a servicer to offer one of the alternatives, to encourage completion of a short sale or DIL. If an alternative to foreclosure is the route taken, the servicer must also obtain the homeowner's written agreement regarding the requirements for receipt of relocation assistance. In the case of a DIL, the agreement must specify that the property must be unencumbered by other liens or unallowable restrictions on title, that it will be kept in good and safe condition, and that it will be left ready for sale in "broom clean" condition (i.e., clear of all personal belongings, and reasonably clean) upon the homeowner's departure.

c. Relocation assistance is a way that VA helps provide necessary funds to conduct a move or pay for lodging for borrowers who are faced with the loss of their home. For servicers, the transfer of ownership via DIL or short sale is typically shorter than a foreclosure time period. Additionally, the property is left in better condition via DIL than foreclosure, which helps preserve the value of the property by minimizing the time it is vacant and subject to vandalism and deterioration. Also, alternatives to foreclosure options generally provide borrowers and communities a substantially improved outcome compared to a foreclosure sale.

### 5.11 LOAN MODIFICATION OVERSIGHT

a. VA performs several reviews during the life of the loan. Reviews are performed to ensure that VA's liability was not increased due to non-compliance with VA requirements.

b. Suspicious Loan Modification. VA performs a review of a loan modification if the servicer failed to report all necessary data elements in the Loan Modification Complete event, and/or VALERI determines the data has failed VA requirements. When this occurs, VALERI will open a Review Suspicious Loan Modification process for review by the VA-assigned technician. All broken business rules in the Loan Modification Complete event must be reviewed to determine the validity of infractions. VA will review the loan modification to ensure the servicer followed the requirements of the modification option used. Infractions could result in VA requesting a revision to the loan modification or in VA possibly adjusting a claim. VA will also recover any incentive VA paid to the servicer for the completion of the loan modification. VA may require the servicer to make corrections if the terms negatively impact the borrower or the Government. Servicers must complete all corrections within 60 days of notification by VA. Failure to make corrections within the required timeframe could result in VA making an adjustment to the claim if the loan becomes delinquent and subsequently terminates. VA may also take other administrative action, depending on the seriousness or frequency of the servicer's infractions. The following are some errors that may require further VA review:

1. The loan modification did not cure the default.
2. The interest rate on the modified loan exceeds the maximum allowable rate.
3. The term of the modified loan exceeds the maximum allowable term.
4. The new loan does not amortize to within \$50 of zero over the new term.

c. EPD on a Modified Loan. VA reviews EPDs any time a servicer reports that the loan became delinquent within the first 6 months of the first payment due date on the loan modification agreement. When this occurs, VALERI will open a Review Early Payment Default process for review by the VA-assigned technician. An EPD may be the result of an improper decision by the servicer to modify the loan. VA will complete an analysis of the loan modification underwriting package, if applicable, to ensure it complies with VA requirements. Servicer errors may result in an infraction being added and a possible future claim adjustment, along with other possible administrative enforcement, depending on the seriousness or frequency of the servicer's infractions.