



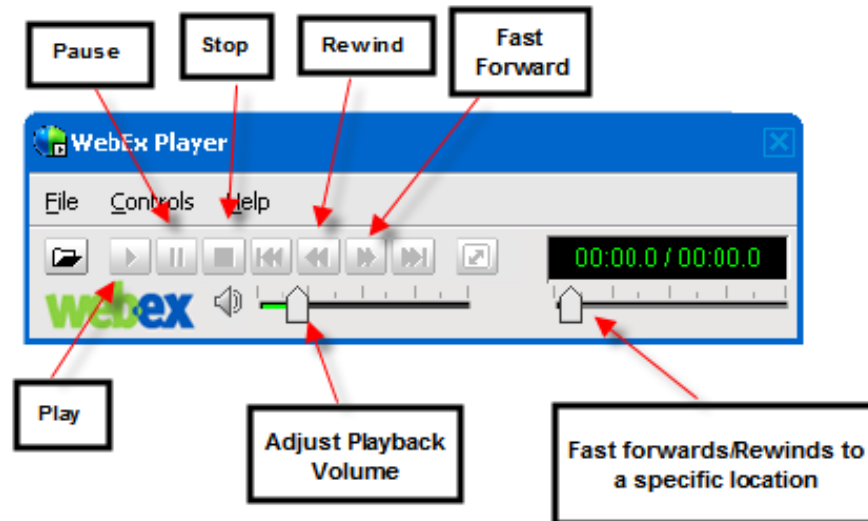
*Freddie Mac Customer Education*

***Short Payoff  
and  
Make-whole Preforeclosure Sale  
Overview***



# Tools and Tips

- ✓ Close all other applications to enhance your workstation's performance.
- ✓ Maximize the window used for viewing this recording.
- ✓ For technical Support, call (866) 229-3239.



Visit our Learning Center to view other distance learning offerings  
[www.freddiemac.com/learn](http://www.freddiemac.com/learn)



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# Objectives

After you complete this session, you will:

- Understand the difference between a short payoff and make-whole preforeclosure sale.
- Understand the eligibility requirements, and be able to determine if a borrower is eligible for a short payoff or make-whole preforeclosure sale.
- Be able to document short payoffs and make-whole preforeclosure sales.
- Understand how to obtain approval for short payoffs.
- Be able to complete short payoffs and make-whole preforeclosure sales.





# Background

- Loan modifications have been the workout of choice for the last several years.
- As property values decrease, there will likely be an increase in the number of short sales which will keep REO inventories down and preserve neighborhoods.



# Background

- It's becoming more difficult to negotiate short sales due to the frequency and size of junior liens.
- Many real estate professionals are new to the short sale experience.
- As short sales increase, the default servicing industry must re-develop relationships with all parties.



# Key Statistics

## Delinquent loan inventory:

- 30-day delinquent loans are at a record number.
- 90 days and greater continue to increase.
- Foreclosure sales are at an all-time high.



## Environment:

- House values are falling in many areas of the US.
- There is a high inventory of properties on the market with few sales.
- Tighter credit market makes it more difficult to finance.



# Key Statistics

## Data:

- We are completing a high number of workouts per year.
- 75 percent of loan modifications cure for good.
- 70 percent of late stage repayment plans fail versus 40 percent of early stage.
- Servicers report less than a 50 percent contact rate with borrowers that went to foreclosure sale.
- Roper survey shows that the majority of borrowers do not contact their Servicer, but are willing to talk to a financial counselor.





# Workout Options That Enable the Borrower to Retain Homeownership

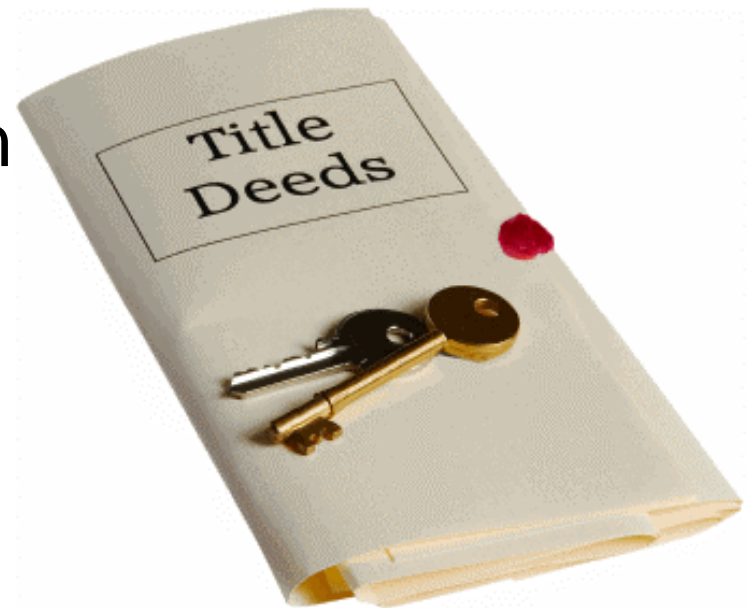
- Full and partial reinstatement
- Short- and long-term forbearance
- Repayment plan
- Loan modification
- FHA partial claim/MI claim advance

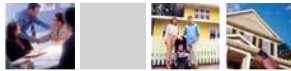




# Workout Options to Consider When the Borrower is Unable to Retain Ownership

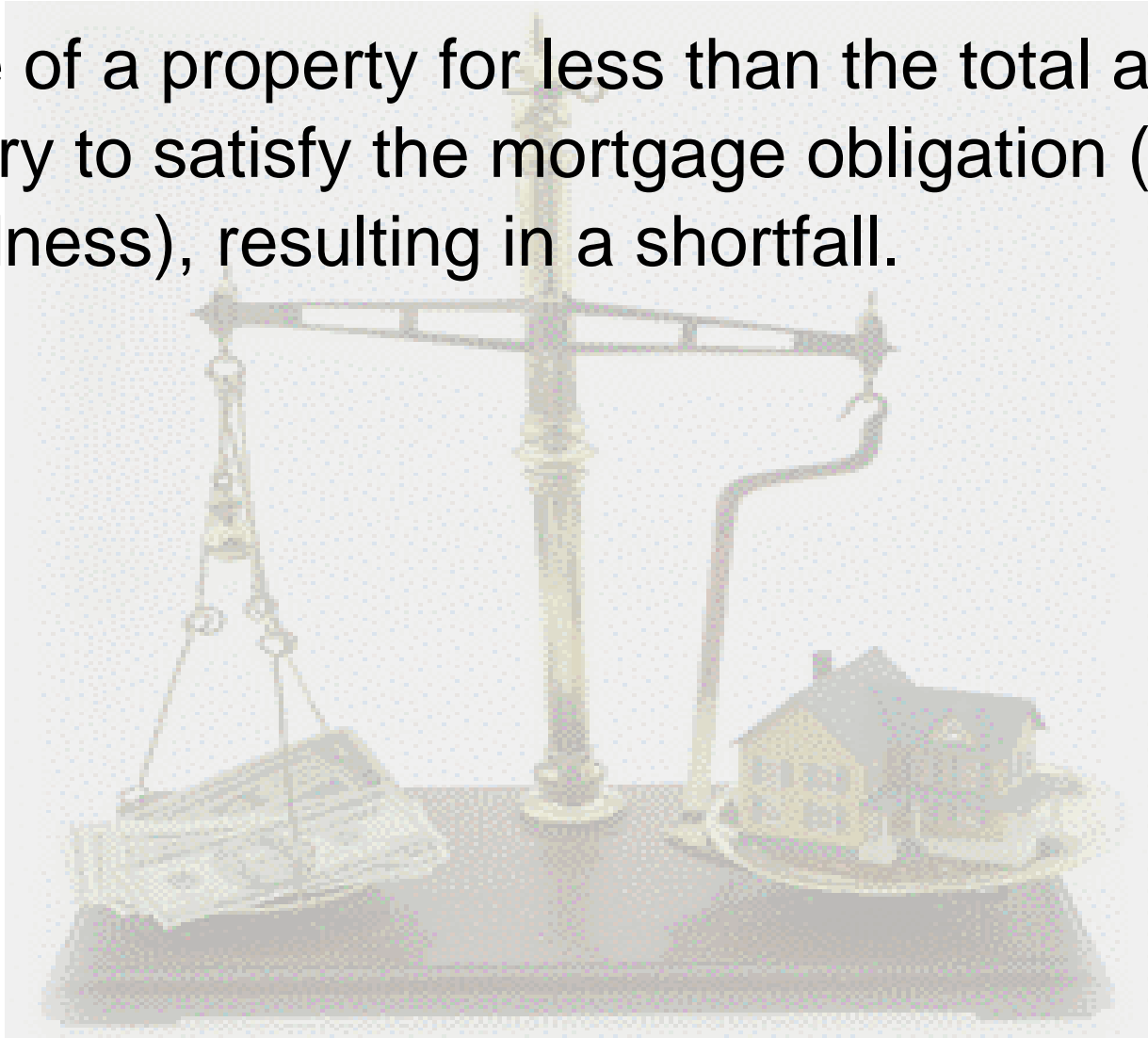
- Make-whole preforeclosure sale
- Short payoff
- Deed-in-lieu of foreclosure
- Workout mortgage assumption





# Short Payoff

The sale of a property for less than the total amount necessary to satisfy the mortgage obligation (total indebtedness), resulting in a shortfall.





# Make-whole Preforeclosure Sale

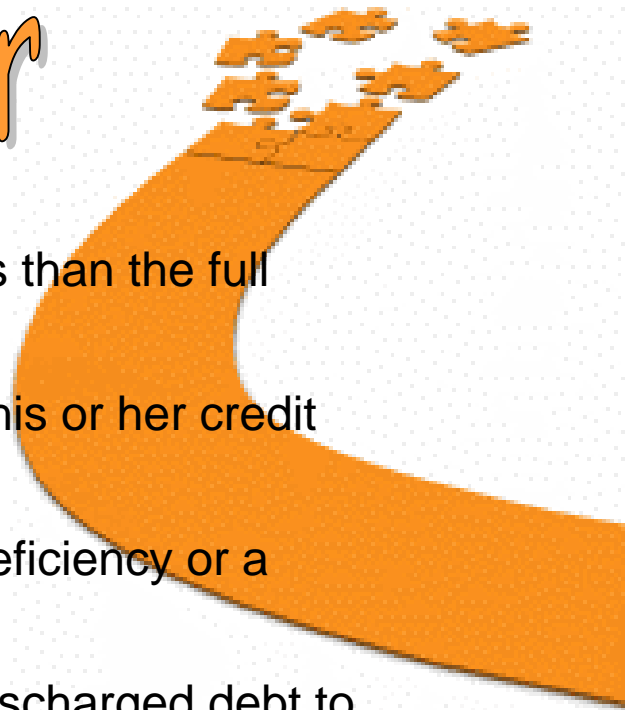
- A short payoff becomes a make-whole preforeclosure sale when you determine that the shortfall between the net sale proceeds and total indebtedness will be paid at settlement so that Freddie Mac does not sustain a loss.
- The shortfall may be paid by:
  - ✓ MI
  - ✓ Cash contribution
  - ✓ Insurance proceeds
  - ✓ Combination of sources



# Who Benefits From a Short Sale?

## Homeowner

- Satisfies the debt for less than the full amount
- Avoids a foreclosure on his or her credit record
- Avoids the pursuit of a deficiency or a deficiency judgment
- May avoid reporting of discharged debt to the IRS



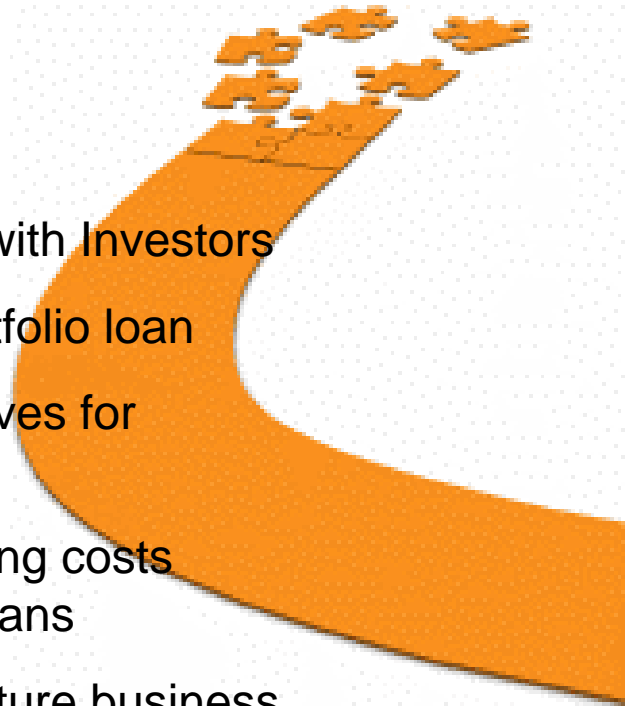
Source – “Effective Short Sale Workouts” – Genworth Financial, Inc



# Who Benefits From a Short Sale?

## Servicer

- Enhances relationships with Investors
- Avoids an REO on a portfolio loan
- Potential investor incentives for completed Short Sales
- Avoids expensive servicing costs incurred on delinquent loans
- Enhances goodwill for future business



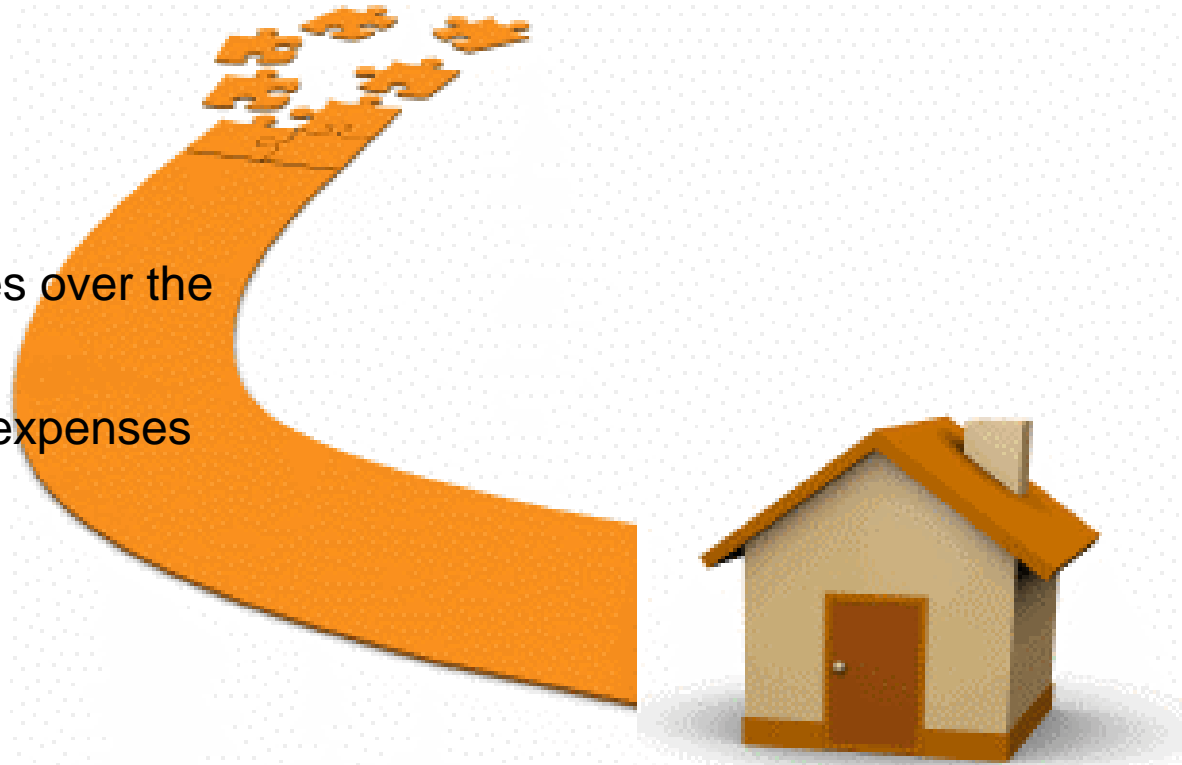
Source – “Effective Short Sale Workouts” – Genworth Financial, Inc



# Who Benefits From a Short Sale?

## Investor

- Potentially reduces losses over the insured amount
- Avoids an REO and the expenses incurred



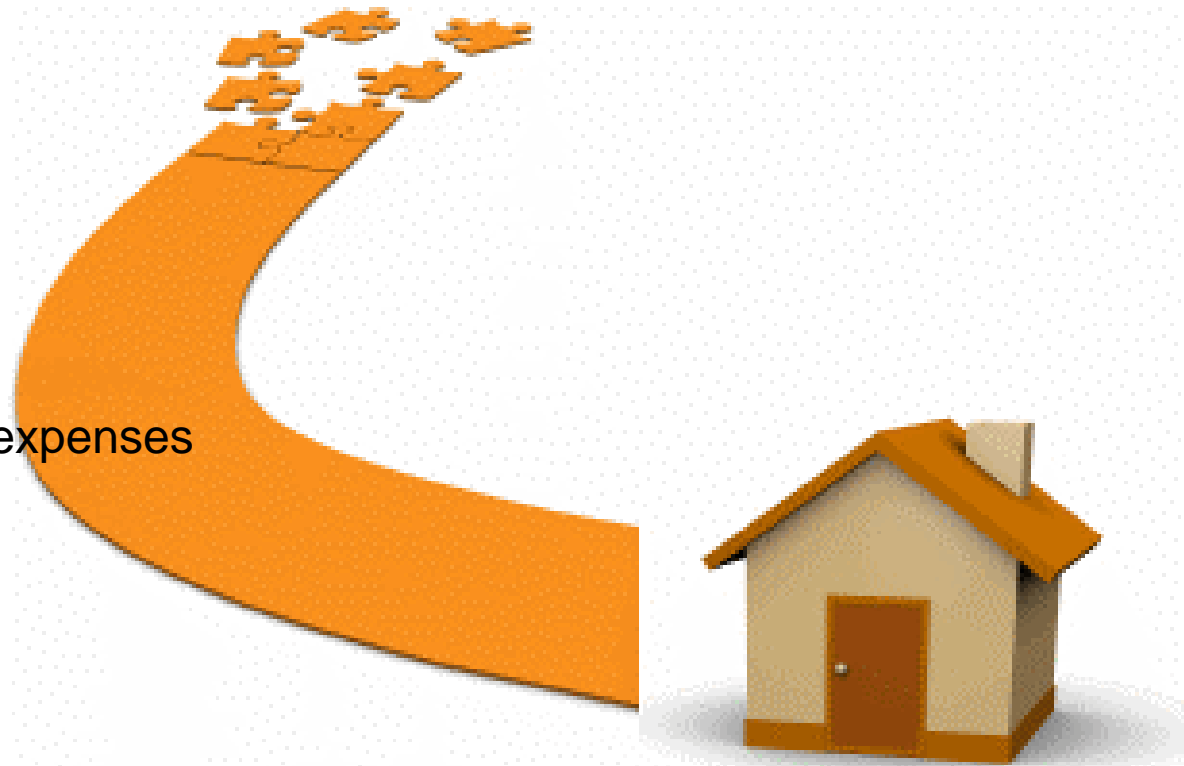
Source – “Effective Short Sale Workouts” – Genworth Financial, Inc



# Who Benefits From a Short Sale?

MI Company

- Reduces claim losses
- Avoids an REO and the expenses incurred

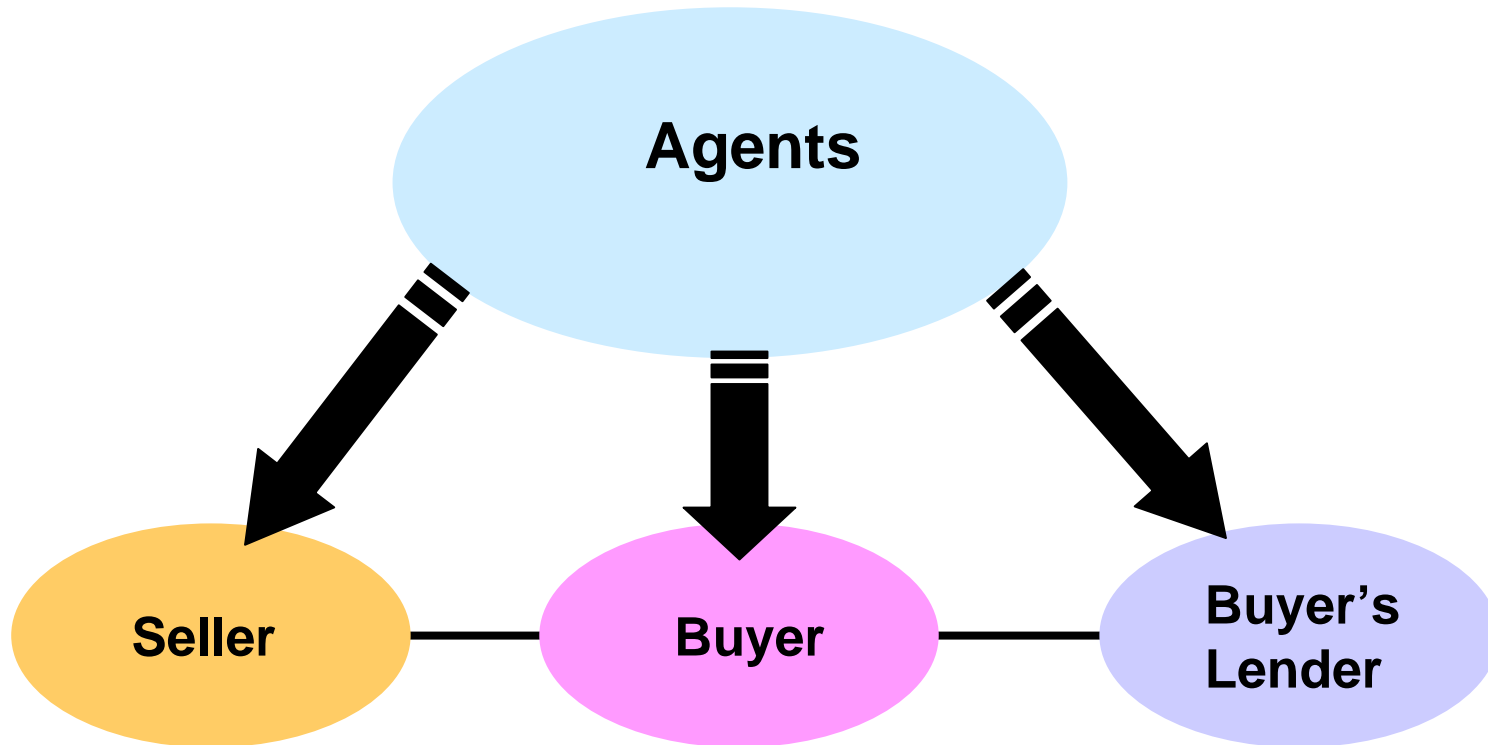


Source – “Effective Short Sale Workouts – Genworth Financial, Inc





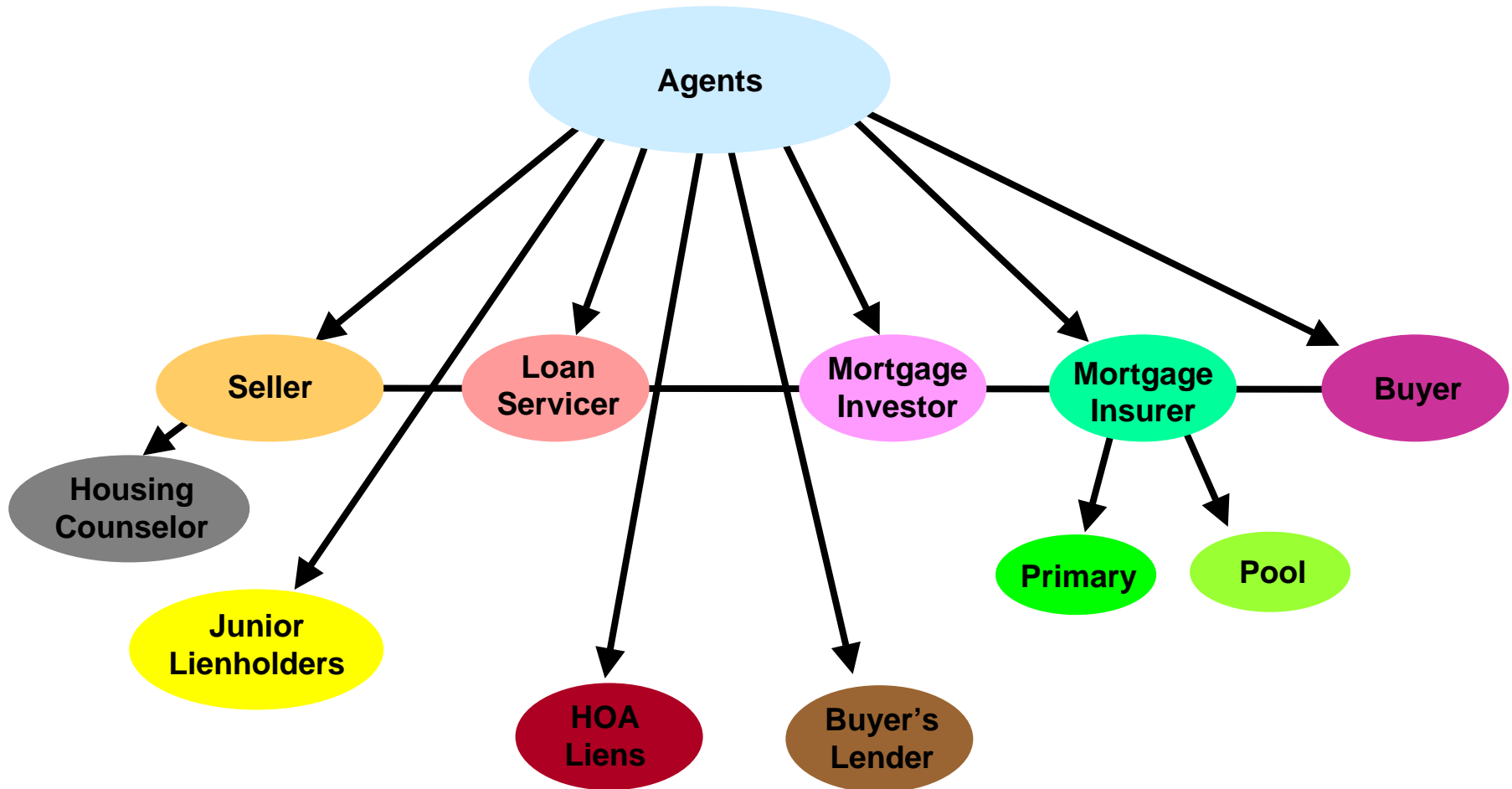
# Parties in Typical Real Estate Transactions



Source – Effective Short Sale Workouts, Genworth Financial, Inc.



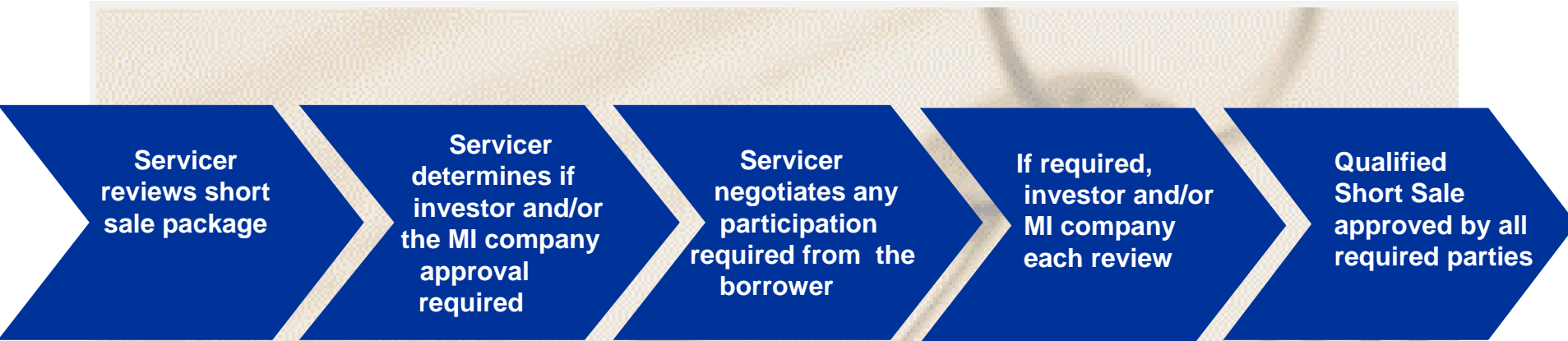
# Parties in a Short Sale



Source – “Effective Short Sale Workouts, Genworth Financial, Inc



# Short Sale Process



- Short sale closes
- Borrower contributes to minimize the loss based on ability
- Borrower avoids foreclosure
- The investor and the MI company minimize losses
- Real Estate Professional closes an additional sale
- Neighborhood avoids the stigma of foreclosure

Source – “Effective Short Sale Workouts” Genworth Financial, Inc



# Short Payoff or Make-whole Preforeclosure Sale?

When you decide to pursue a short payoff, you must determine if it can become a make-whole preforeclosure sale or remain a short payoff.





# Determine if Short Payoff Can Be a Make-whole Preforeclosure Sale

Once you have the borrower's executed sales contract

- Calculate the difference between estimated net sales proceeds and the total indebtedness.
- Calculate the MI claim payment.
- Determine the approximate amount of cash due from the borrower.
- Determine other sources for the shortfall.



# Example

|                                  |                   |                     |
|----------------------------------|-------------------|---------------------|
| Property value -                 | \$150,000         |                     |
| Total amount due on first lien   | \$178,000         |                     |
| Sales price -                    | \$148,000         | (99% of value)      |
| 6% Commission and closing costs  | (\$ 13,000)       | (9% of sales price) |
| Less funds from homeowner for cc | \$ 1,000          |                     |
| Payment to \$20K lienholder      | (\$ 2,000)        |                     |
| Net proceeds -                   | \$134,000         | (90% of value)      |
| Shortage/loss -                  | <b>(\$44,000)</b> |                     |
| 20% MI Claim (100% of claim)     | \$35,600          |                     |
| Shortage/loss                    | <b>(\$ 8,400)</b> |                     |



# Determine if Short Payoff Can Be a Make-whole Preforeclosure Sale

## Scenario 2:

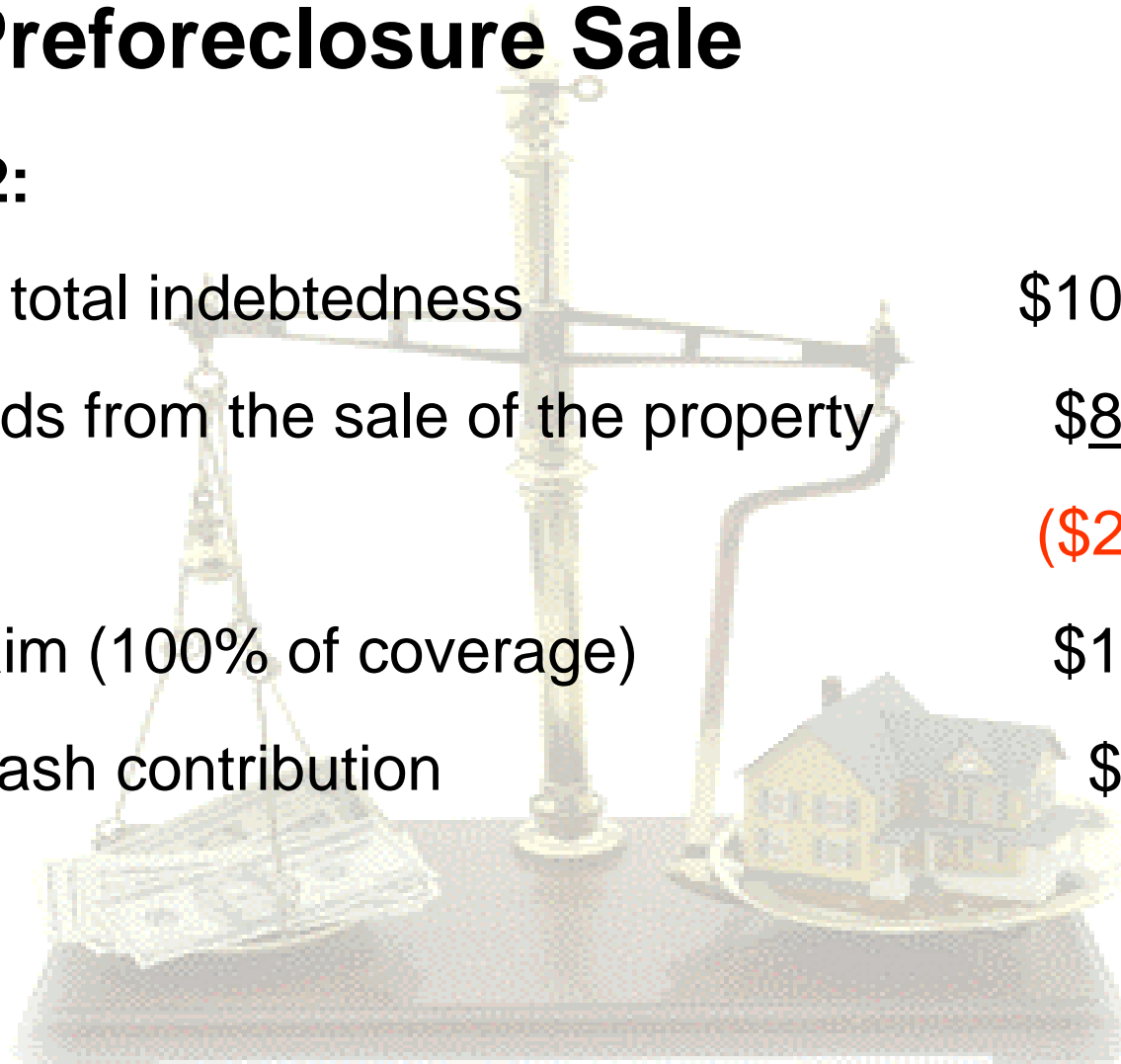
Borrower's total indebtedness \$100,000

Net proceeds from the sale of the property \$80,000

**Shortfall** (\$20,000) ←

15% MI claim (100% of coverage) \$15,000 ↙

Borrower cash contribution \$5,000 ↘





A short payoff with a note to cover the shortfall is a make-whole preforeclosure sale.

- True
- False

Scenario:

|  |                   |
|--|-------------------|
| Borrower's total indebtedness              | \$100,000         |
| Net proceeds from the sale of the property | <u>\$80,000</u>   |
| <b>Shortfall</b>                           | <b>(\$20,000)</b> |
| MI claim payment                           | \$15,000          |
| Borrower signs a promissory note           | \$5,000           |







A short payoff with a note to cover the shortfall is a make-whole preforeclosure sale.

**False**

A promise to pay is not the same as making Freddie Mac whole at closing.





# Compensation for Short Payoffs and Make-whole Preforeclosure Sales

| Situation   | Incentive Amount |
|---|------------------|
| You process and settle the short payoff or make-whole preforeclosure sale   | \$2,200          |
| Freddie Mac or a third party retained by Freddie Mac processes and settles the short payoff or make-whole preforeclosure sale | \$200            |



# How to Execute Short Payoffs and Make-whole Preforeclosure Sales

- Step 1: Identify candidates.
- Step 2: Determine eligibility.
- Step 3: Negotiate the terms.
- Step 4: Document and submit your recommendation to us.
- Step 5: Complete the short payoff or make-whole preforeclosure sale.



# Step 1: Identify Candidates

- Leverage technology to identify potential candidates.
  - ✓ EarlyIndicator®
  - ✓ Workout Manager®
    - Enhanced Short Payoff Program Report (SPEED List)
    - Re-defaulted Mod Analysis
  - ✓ Timeline Manager<sup>SM</sup>
    - Past Standard Report
    - Past Standard Detail Report
- Leverage your in-house data.
  - ✓ In-house delinquency tracking and reporting systems
  - ✓ Property inspections
  - ✓ Collection notes



# Enhanced Short Payoff Program

- Uses EarlyIndicator<sup>®</sup> scores to proactively identify borrowers who may qualify for a short payoff.
- Available to all Servicers with one or more 60+ delinquent mortgages.
- Review the Enhanced Short Payoff Program Report (SPEED List) available in Workout Manager<sup>®</sup>.



# Benefits of the Enhanced Short Payoff Program

- Reduced documentation requirements
- Expedited approval process
- Increased workout-to-REO ratio
- Reduced credit losses



# Enhanced Short Payoff Program Requirements

- The EarlyIndicator loss mitigation score must be 350 or less.
- The credit report must reflect that
  - ✓ The borrower has not taken out a new mortgage in the last 12 months.
  - ✓ Our mortgage is not the only delinquent account.



# Enhanced Short Payoff Program Requirements

- The net sale proceeds to Freddie Mac (including all pay outs to any junior lienholders) must be based on the 90-day marketing timeframe from the interior BPO. Refer to the SPEED List for the minimum percentage of net sales proceeds that is due to Freddie Mac.
- Attempt to negotiate the maximum contribution possible from the borrower.
- Obtain MI approval, if applicable.



# Enhanced Short Payoff Program (Speed List)

BEST SERVICING, INC. / 123789

For Period Ending Thursday, January 14, XXXY

Last Updated Friday, January 15, XXXY at 6:34 am.

| <u>Servicer/<br/>FHLMC<br/>Loan #</u> | <u>Servicer</u> | <u>Property<br/>City</u> | <u>Property<br/>State</u> | <u>MI</u> | <u>Occupancy<br/>Status</u> | <u>New<br/>Inflow</u> | <u>Date<br/>Referred</u> | <u>Loan<br/>Status</u> | <u>Pre-Qual<br/>Status</u> |
|---------------------------------------|-----------------|--------------------------|---------------------------|-----------|-----------------------------|-----------------------|--------------------------|------------------------|----------------------------|
| 9977741                               | 123789          | Beachtown                | SC                        |           | Borrower                    |                       |                          | 60                     | Green                      |
| 931648526                             |                 |                          |                           |           |                             |                       |                          |                        |                            |
| 2221111                               | 123789          | Georgetown               | VT                        | Y         | Unknown                     | Y                     | 02/13/xxxx               | FCL                    | Green                      |
| 731666665                             |                 |                          |                           |           |                             |                       |                          |                        |                            |
| 7771111                               | 123789          | Grand<br>Valley          | CA                        |           | Unknown                     |                       | 05/29/xxxx               | FCL                    | Yellow                     |
| 133322222                             |                 |                          |                           |           |                             |                       |                          |                        |                            |
| 9965488                               | 123789          | Hillsboro                | NY                        |           | Borrower                    |                       | 07/20/xxxv               | FCL                    | Yellow                     |
| 911144447                             |                 |                          |                           |           |                             |                       |                          |                        |                            |
| 9995413                               | 123789          | Sunset                   | CA                        |           | Borrower                    |                       | 09/19/xxxv               | FCL                    | Red                        |
| 311166625                             |                 |                          |                           |           |                             |                       |                          |                        |                            |

**GREEN:** If there is no new mortgage in last 12 months AND borrower is delinquent on more than just their FHLMC mortgage.

**YELLOW:** If there is not enough data to determine whether borrower has a new mortgage OR borrower is delinquent on more than just their FHLMC mortgage.

**RED:** If borrower's only delinquency is on their FHLMC mortgage OR borrower has a new mortgage tradeline.



If the net proceeds do not meet the minimum percentage requirements, the loan does not qualify for a short payoff.

- True
- False





If the net proceeds do not meet the minimum percentage requirements the loan does not qualify for a short payoff.

False

If the offer does not meet the minimum requirements determine if it meets our standard short payoff program requirements or submit the deal to us for a possible exception.





## Step 2: Determine Eligibility

The borrower must:

- Be experiencing involuntary inability to pay (or allowable exception).
- Be delinquent or in imminent danger of default.
- Be cooperative and allow access to the interior of the property for a BPO. <https://www.bpodirect.net> [bpoquestion@freddiemac.com](mailto:bpoquestion@freddiemac.com)
- Complete and sign Form 1126, *Borrower Financial Statement*.
- Have the property listed with licensed real estate broker at fair market value.



# Determine Eligibility

The borrower must:

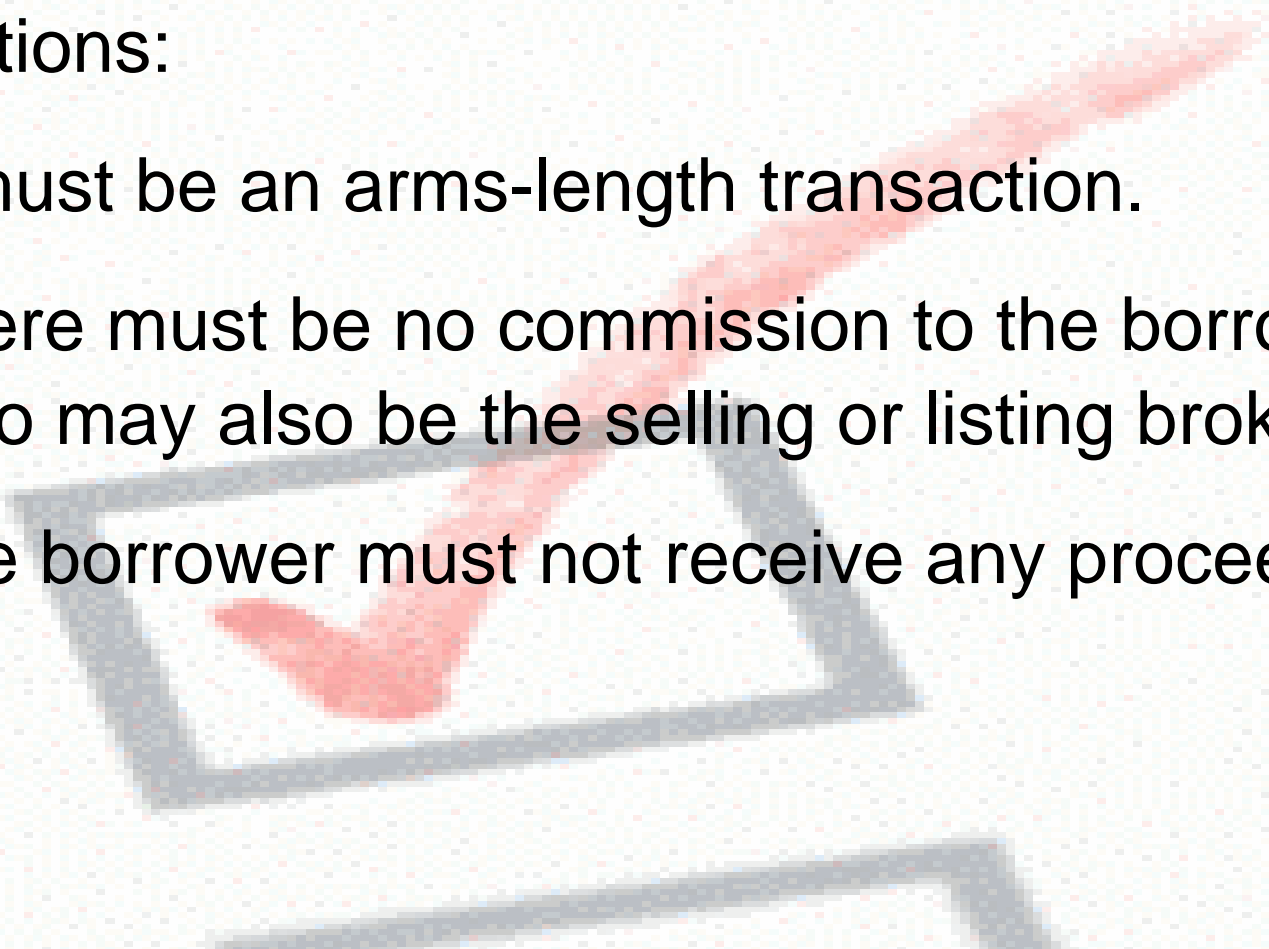
- Make the maximum contribution possible.
- Not be participating in a program that involves a third-party taking title and arranging the short payoff for a fee.
- Waive escrow, buydown funds, prepaid items and assign any insurance proceeds.



# Determine Eligibility

The sales transaction must meet the following conditions:

- It must be an arms-length transaction.
- There must be no commission to the borrower who may also be the selling or listing broker.
- The borrower must not receive any proceeds.





# Additional Requirements

- Interior broker's price opinion (BPO) with the 90-day "as is" marketing timeframe.
  - ✓ Sale is always "as is."
  - ✓ Will accept more recent comps to support current value.
- Net proceeds required:
  - ✓ Percentage of interior BPO value
  - ✓ Closing costs and commissions
  - ✓ Includes any payment to junior lienholders
- Borrower's financial participation in the transaction

As is Sale



# Documentation to Help You Determine Eligibility

Obtain a copy of the following:

- The fully executed sales contract, with addenda
- Listing agreement
- The original loan application
- An estimate of the seller's closing costs



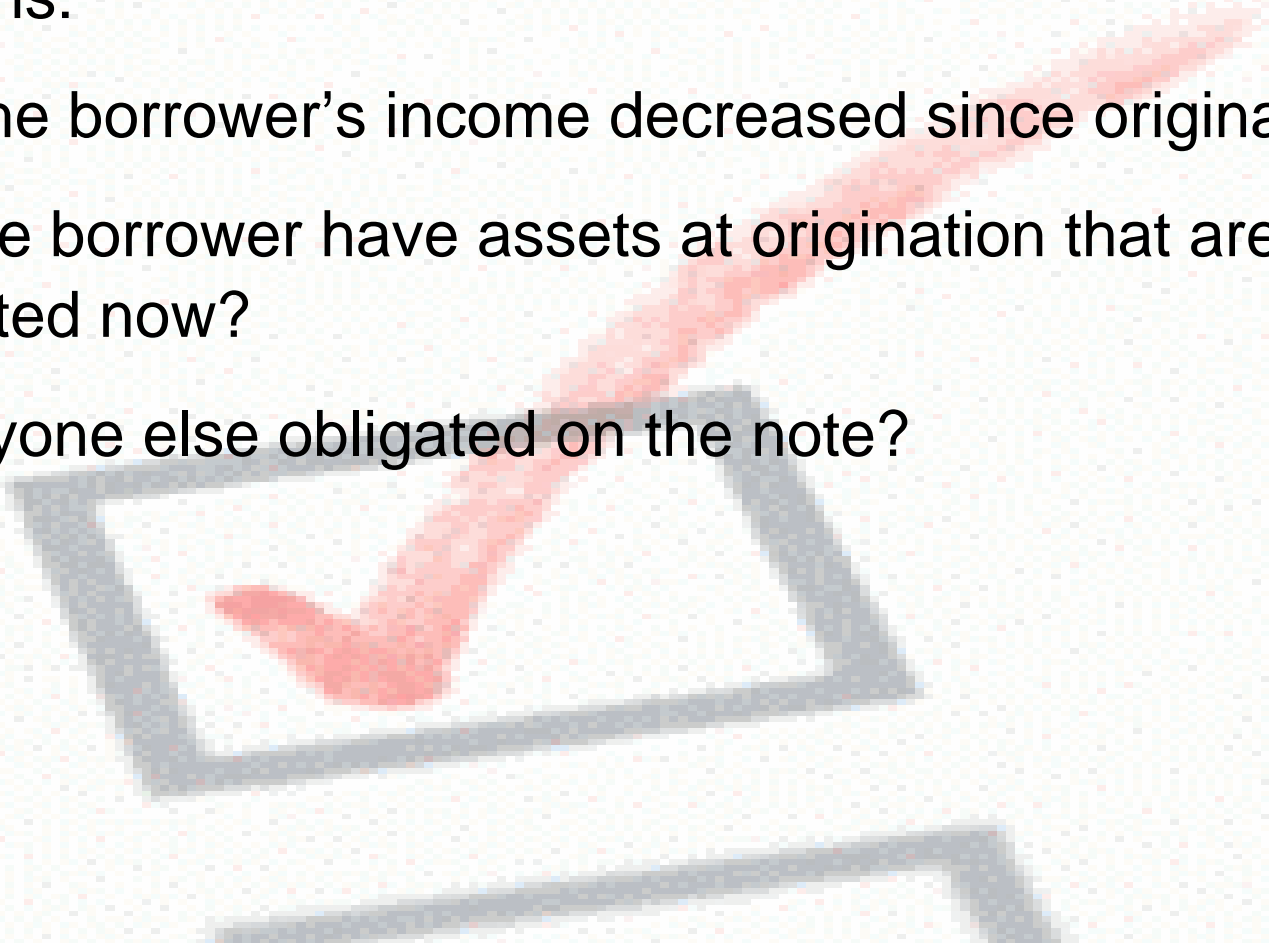




# Review the Borrower's Financial Information

Review borrower financial information and ask the following questions:

- Has the borrower's income decreased since origination?
- Did the borrower have assets at origination that aren't reflected now?
- Is anyone else obligated on the note?





# Borrower Is Not Eligible for Short Payoff

If either the borrower or sales transaction don't meet the eligibility requirements, take one of the following actions:

- If you still believe a short payoff is the best solution, submit a recommendation to us. We will consider exceptions on a case-by-case basis.
- Pursue another alternative.
- Proceed with foreclosure.

# Determine Savings Over REO

| Circumstance/Data   | Finding   |
|---|-----------|
| Unpaid Principal Balance  | \$120,596 |
| Mortgage Interest Rate  | 8%        |
| Due Date of Last Paid Installment (DDLPI)   | 11/1/xx   |
| Schedule Short Payoff Settlement Date   | 3/29/xy   |
| Scheduled/Estimated Foreclosure Sale Date   | 7/20/xy   |
| Date of BPO   | 3/1/xy    |
| Interest accrued to estimated short payoff close date   | \$4,020   |
| Interest accrued to the foreclosure sale date   | \$6,970   |
| Escrow Advance (estimate to short payoff close date)  | None      |
| Escrow advance (estimate to foreclosure sale date)  | \$1,300   |
| Foreclosure fees and costs (incurred to date)   | \$800     |
| Foreclosure fees and costs (estimate to foreclosure sale date) Note: includes the \$800 already incurred. | \$2,000   |
| Short payoff offer  | \$95,000  |
| As-is BPO value (90-day marketing time frame)   | \$92,000  |
| Short Payoff closing costs  | \$8,000   |
| MI?   | Yes       |
| MI Coverage %   | 25%       |
| Borrower contribution to the loss from the short payoff   | 0         |

| <b>Short Payoff</b>  |                    |
|--|--------------------|
| Unpaid Principal Balance   | \$120,596          |
| Interest accrued to estimated short payoff close   | + \$4,020          |
| Escrow Advance (estimate to short payoff close date)   | + \$0              |
| Other advances, fees and costs   | + \$0              |
| Foreclosure fees and costs (incurred to date)  | + \$800            |
| <b>Total Debt</b>  | <b>= \$125,416</b> |
| Short Payoff Offer   | \$95,000           |
| Short Payoff closing costs   | - \$8,000          |
| Short Payoff Net Proceeds  | = \$87,000         |
| Mortgage insurance proceeds (total debt x mortgage insurance percent coverage)                             | + \$31,354         |
| Borrower contribution (cash)   | + \$0              |
| <b>Total Proceeds</b><br>(Short payoff net proceeds + mortgage insurance proceeds + borrower contribution) | <b>= \$118,354</b> |
| <b>Estimated Short Payoff Loss</b><br>(Total debt - total proceeds)  | <b>\$7,062</b>     |

| <b>Short Payoff</b>  |                    |
|--|--------------------|
| Unpaid Principal Balance   | \$120,596          |
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| <b>REO</b>  |                    |
|---|--------------------|
| Unpaid Principal Balance  | \$120,596          |
| Interest accrued to the foreclosure sale date                                       | + \$6,970          |
| Escrow advance (estimate to foreclosure sale date)                                  | + \$1,300          |
| Other advances, fees and costs  | + \$0              |
| Foreclosure fees and costs (estimate to foreclosure sale date)                      | + \$2,000          |
| <b>Total Debt</b>   | <b>= \$130,866</b> |
| As-is BPO value (90-day marketing time)   | \$92,000           |
| As-is BPO value x .10   | - \$9,200          |
| Estimated REO Net Proceeds  | = \$82,800         |
| Mortgage insurance proceeds (total debt x mortgage insurance percent coverage)      | + \$32,717         |
| <b>Total Proceeds</b><br>(Estimated REO net proceeds + mortgage insurance proceeds) | <b>= \$115,517</b> |
| <b>Estimated REO Loss</b><br>(Total debt - total proceeds)                          | <b>\$15,349</b>    |



# Savings Over REO

|   |                |  |                 |
|---|----------------|--|-----------------|
| <b>Estimated Short Payoff Loss</b><br>(Total debt - total proceeds)                       | <b>\$7,062</b> | <b>Estimated REO Loss</b><br>(Total debt - total proceeds) | <b>\$15,349</b> |
| <b>Estimated Savings Over REO</b> (Estimated REO Loss minus estimated Short Payoff Loss): |                |  | <b>\$8,287</b>  |





## Step 3: Negotiate the Terms

- Focus on the bottom line.
- If the borrower is not willing to make a contribution, suggest that he or she pay closing costs and commission rather than paying toward the loss.
- Always consider the loss resulting from the short payoff compared to the loss resulting from foreclosure.
- Know what the MI will contribute, and the borrower contribution required by the MI before you negotiate with the borrower, if possible.



## Step 4: Document and Submit Your Recommendation

To request approval for a short payoff or notify us of a make-whole preforeclosure sale electronically, what should you do?

- Send an e-mail to [distressed\\_property@FreddieMac.com](mailto:distressed_property@FreddieMac.com).
- Transmit the recommendation via Workout Prospector®.
- Send an e-mail to [foreclosuresales@FreddieMac.com](mailto:foreclosuresales@FreddieMac.com).







# Workout Prospector®

A web-based application, available on FreddieMac.com, that gives you the ability to analyze, structure, and send alternative to foreclosure recommendations to Freddie Mac electronically.

<http://www.freddiemac.com/singlefamily/service/tools.html>



# Benefits of Workout Prospector®

- Reduces labor-intensive data entry and minimizes the potential for data entry errors.
- Displays warning messages when the parameters of your recommendation do not meet Freddie Mac's requirements for a selected alternative to foreclosure.
- Delivers your workout recommendation to Freddie Mac electronically.
- Guards against subjectivity in decision making.
- Can help reduce credit losses.



# Documenting Borrower Financial Data in Workout Prospector®

- Borrower Income screen
- Borrower Expenses screen
- Borrower Assets and Liabilities screen



# Document Short Payoff and Obtain Approval

Submit the following to Freddie Mac for review and approval:

- Form 1126, *Borrower Financial Statement*
- Copies of the following:
  - ✓ Borrower letter
  - ✓ Pay stub
  - ✓ Federal income tax return (if self-employed)
  - ✓ Previous year's & YTD profit and loss statement (if self-employed)
- Copy of fully executed sales contract with addenda
- Estimated seller closing costs
- Copy of MI approval letter





# Document Make-whole Preforeclosure Sale

- Freddie Mac's approval is not required when there is no shortfall due to MI proceeds, a cash contribution, insurance proceeds, or a combination of these sources.
- Obtain MI approval (primary and pool), if applicable, before notifying us of the make-whole preforeclosure sale.
- Notify us:
  - ✓ Form 1126, *Borrower Financial Statement*
  - ✓ Copy of fully executed sales contract with addenda
  - ✓ Estimated seller closing costs
  - ✓ Copy of MI approval letter, if applicable





# Where to Send Your Recommendation

- Include name, phone and fax number on Form 1126.

## Regular or overnight mail:

Attention: File Preparation  
Freddie Mac  
8250 Jones Branch Drive  
Mailstop A61  
McLean, VA 22102

## Fax:

(703) 918- 8019

- Fax title report and MI approval letter within two business days of receipt.
- If the foreclosure timeline will exceed our state timeline, contact your Loss Mitigation Representative.



## Step 5: Complete the Short Payoff or Make-whole Preforeclosure Sale

- Pay all delinquent real estate taxes and assessments.
- Ensure the borrower pays all settlement cash contributions in cash or certified funds.
- Ensure title will be conveyed to the buyer identified in the sales contract.
- Complete the short payoff within timeframe specified in Freddie Mac's approval letter.



# Complete the Short Payoff or Make-whole Preforeclosure Sale

- Waive your rights to any accrued fees or late charges.
- Obtain MI approval, if applicable.
- Follow any specific approval conditions in Freddie Mac's approval letter.
- Complete Investor Accounting activities.







# Complete the Short Payoff or Make-whole Preforeclosure Sale

Ensure your loss mitigation area submits the following to us:

- A copy of the settlement statement
- A copy of the proceeds check
- The original promissory note(s), if applicable (must be sent by overnight mail)
- Copies of any addenda to the sales contract subsequent to our approval



# Complete the Short Payoff or Make-whole Preforeclosure Sale

- If the loan is scheduled/scheduled, for each month of delinquency include a list of
  - ✓ All ending principal balances reported to us
  - ✓ Interest advanced to us
- If the loan is a cost of funds (COF), for each month of delinquency include a list of
  - ✓ The accounting net yield in effect
  - ✓ Interest advanced to us
  - ✓ All ending principal balances reported to us



# Avoiding Short Payoff Hurdles

- Obtain borrower financial participation in the usual seller's closing costs.
- Have better or recent comps available.
- Get buyers pre-approved through reputable lenders.
- Must be an arms-length transaction. Obtain a notarized affidavit if relationship is unclear.





# Avoiding Short Payoff Hurdles

- Know who the owner (Investor) of the loan is.
- Offers should reflect the property's present market value.
- Negotiate with all junior lien holders.
- Provide clear, easy to read documentation.



# Avoiding Short Payoff Hurdles

- The buyer on HUD-1 must be same buyer on approval letter.
- The borrower must receive no commission or proceeds from the sale.
- Include POA when sending the HUD-1 to the Servicer.
- HUD-1 must be certified true final.”



Who certifies that the HUD-1 is a “certified true final?”

- a) Servicer
- b) Closing Agent
- c) Real Estate Agent
- d) Investor





Who certifies that the HUD-1 is a “certified true final?”

Closing Agent





# Avoiding Short Payoff Hurdles

- Freddie Mac must prepare the promissory notes.
- The executed promissory note must accompany HUD-1.
- Do not reduce the seller cash contribution.
- Changes on the HUD-1 to the contract sales price or buyer will negate the short sale.





# Review

- A short payoff becomes a make-whole preforeclosure sale when you determine that the shortfall between the net sales proceeds and the total indebtedness will be paid at settlement, so that Freddie Mac does not sustain a loss.
- The Enhanced Short Payoff Program uses EarlyIndicator scores to proactively identify borrowers that may qualify for a short payoff.

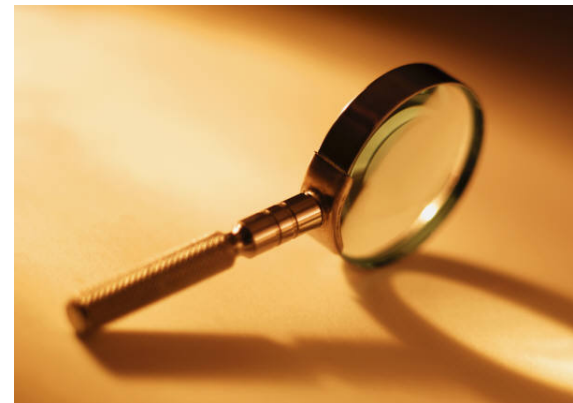
This program is available to all Servicers with one or more 60+ day delinquencies.





# Review

- With a make-whole preforeclosure sale, the shortfall is usually paid by:
  - ✓ Mortgage insurer (MI) through a claim payment
  - ✓ Borrower cash contribution
  - ✓ Hazard insurance proceeds
  - ✓ Combination of sources
- The sale must be an arms-length transaction.
- If the borrower and sales transaction do not meet all of the eligibility requirements, but you still believe that a short payoff is the best solution, submit a recommendation to us.





# Resources

- Servicing Technology Tools

<http://www.freddiemac.com/singlefamily/service/tools.html>

- For questions about specific loans, contact your Freddie Mac Workout Representative.

- Default Servicing Training

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- The Learning Center

[www.FreddieMac.com/learn](http://www.FreddieMac.com/learn)



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