

EQUIDEBT
SOLUTIONS, LLC
Writing a new American Dream

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Diversifying Mortgage Risk Through Equity Sharing

An Alternative to Debt Only Financing for the Residential Real Estate Market

The HEFI Solution:

The HEFI (Home Equity Fractional Interest) is a consumer finance innovation to augment debt-only home financing. This patented security instrument allows homeowners to offer fractional equity stakes in their homes while retaining all of the benefits of home ownership. It could be used in several different situations, such as:

- *A workout tool for a loan modification that allows for principal reduction*
- *Facilitating down payment support for builders, REO holders and municipalities*
- *An alternative to owning rental properties for the residential real estate investor*
- *A cash-out mechanism for homeowners with adequate equity*

***The HEFI is an equity instrument; it is NOT A DEBT INSTRUMENT (e.g. a note or a mortgage)!**

The HEFI conveys to its owner an “in-the-money call option” with two components:

- *A fixed, intrinsic value portion (the “HEFI Consideration”) equal to the down payment contribution (cash/equity infusion or forgiven principal between the new loan amount and the current market value of the property)*
- *A contingent, variable value portion (the “HEFI Percentage”) equal to a specific percentage* of future appreciation until the home is sold or the HEFI is redeemed*

So, how is this done?

These situations can be addressed by allowing home financing to include a *minority, passive equity* partner.

With such a partner, the homeowner can “right-size” their financial obligation by owning less than 100% of the equity in their home, while maintaining all the benefits of homeownership.

With a properly standardized “Home Equity Fractional Interest” security, institutional investors could and would be that partner. Collateral integrity is maintained because the HEFI is a tangible asset that can help offset the costs associated with reducing the principle balance or contributing equity/cash into the deal..

* Percentage (or HEFI Percentage) can be a fixed number or customized as a waterfall over time. This percentage is the amount that would be converted into tenant-in-common (TIC) ownership in the event of a default.

A loss mitigation workout tool for preventing foreclosures:

The majority of *preventable* foreclosures consist of situations where the homeowner wishes to retain the home, but (i) only has the financial capacity to maintain a mortgage that is less than the current balance and (ii) owes more than the home is worth.

A foreclosure could be prevented if the lender reduced the principal of the mortgage to some X% of the home's *current* market value and swapped the principal reduction for a HEFI security.

Because the homeowner is no longer *underwater* and has a new sustainable mortgage expense, subsequent foreclosure is unlikely and the homeowner now has the incentive to maintain and improve the property.

Opportunities for Builders, REO holders and Municipalities:

Builders, lenders, REO holders and municipalities are all struggling to move their inventory at the price point and velocity necessary to maximize profits (or minimize losses). Two of the major contributing factors to this struggle are: (i) the lack of available secondary financing and (ii) the lack of borrowers that can secure financing for a high LTV loan with mortgage insurance or afford the debt load associated with a first and second lien.

The HEFI is the perfect solution in that it allows the holder of this inventory to contribute equity into the deal in the form of a HEFI through the HEFI Home Partnership (HHP) program. This typically results in (i) DEBT in the form of an 80% LTV (1st lien) loan without mortgage insurance and (ii) EQUITY in the form of a HEFI. Borrowers will more easily qualify for the current DTI ratios used in the underwriting process while simultaneously allowing them to afford more house. Inventory will begin to move at a higher velocity and at higher market prices. Municipalities will be able to protect their investment into the community while maintaining more control over how their monetary contributions are handled.

Opportunities for Investors:

A Residential Real Estate Investor may look to cash flow for their return on investment, Home Price Appreciation or both. Many layers of risk come with direct residential real estate investment. That risk may come in the form of cash flow risk due to vacancy, depreciation of the home due to degradation of condition of the home, marketing and leasing costs, credit risk and liability as the borrower for the mortgage, etc.

The HEFI presents an opportunity to mitigate or remove many of those risks. The investor would participate in the down payment on an owner occupied transaction, in the form of a HEFI. This allows the investor to become a passive equity partner with the homeowner, versus becoming their landlord. Because the property is owner occupied the homeowner is incentivized to maintain the property, assume all of the credit risk associated with the mortgage itself as the obligor on the mortgage, etc. The investor has no debt obligation, maintenance, upkeep, marketing or leasing costs.

Why the HEFI Program Works for:

1) Loss Mitigation

- a) Achieves a sustainable monthly mortgage expense for the homeowner
- b) Gives the homeowner the opportunity to earn equity which will incentivize him/her to maintain and improve the home
- c) Together 1 and 2 mitigate the likelihood of a re-default by decreasing recidivism rates
- d) To create a new saleable mortgage that will allow the mortgage lender (note holder) to sell the mortgage to FNMA, FHLMC, GNMA, MBS, etc.
- e) The HEFI provides for a *fair* solution in that it requires a “give-up” by the homeowner, making it a useful part of any modification program. There is **no Moral Hazard!**
- f) This program doesn’t “kick the can down the road” – it is a permanent solution that is implementable today
- g) The HEFI provides the lender with the economic offset necessary, while suppressing any potential moral hazards, to engage in principle reduction activities

2) Purchase – Builders, REOs and municipalities:

- a) Increases the pool of buyers that can secure financing
- b) Increase the affordability of existing housing inventory
- c) Increases market demand for properties, thus increasing sales velocity
- d) Homes can sell at full market price due to attractive financing option (80% 1st plus a HEFI)
- e) Create higher valued “comps,” leading to market (neighborhood) appreciation

3) Investors:

- a) Mitigates Risks: debt obligation, insurance liability, tenant issues, etc.
- b) Smaller cash investments per property means greater diversification by splitting investment across multiple properties
- c) Investment in a HEFI qualifies under the 1031 exchange tax code

4) General benefits:

- a) Protect your investment by having a built-in loss mitigation tool:
 - 1) The HEFI will convert into tenant-in-common ownership in an event of default under the HEFI Agreement
 - 2) HEFI owner can sell the home in a non-distressed environment to protect their investment
 - 3) Avoid the costs and elongated timeframes associated with foreclosure

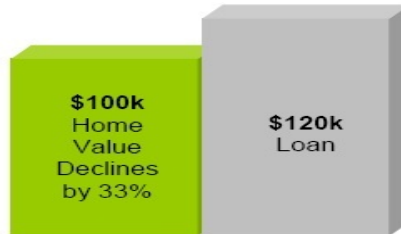
LOSS MITIGATION:

Original Situation



Equity 20%

After Price Fall



Equity (-17%)

After: Foreclosure



Result: Equity 0%
Bank Write-down 42%

After: Modification with HEFI*



Result: Equity 0%
Bank Write-down 17%*

**This is only an estimate and is contingent on the book value given to the HEFI Consideration during accounting determination. The upside of the appreciation share is not shown and the percentage of HEFI appreciation sharing is flexible and specific to each HEFI owner.*

PURCHASE:

Current Option



Seller Net at closing: \$100K
Borrower Payment: \$582 / month

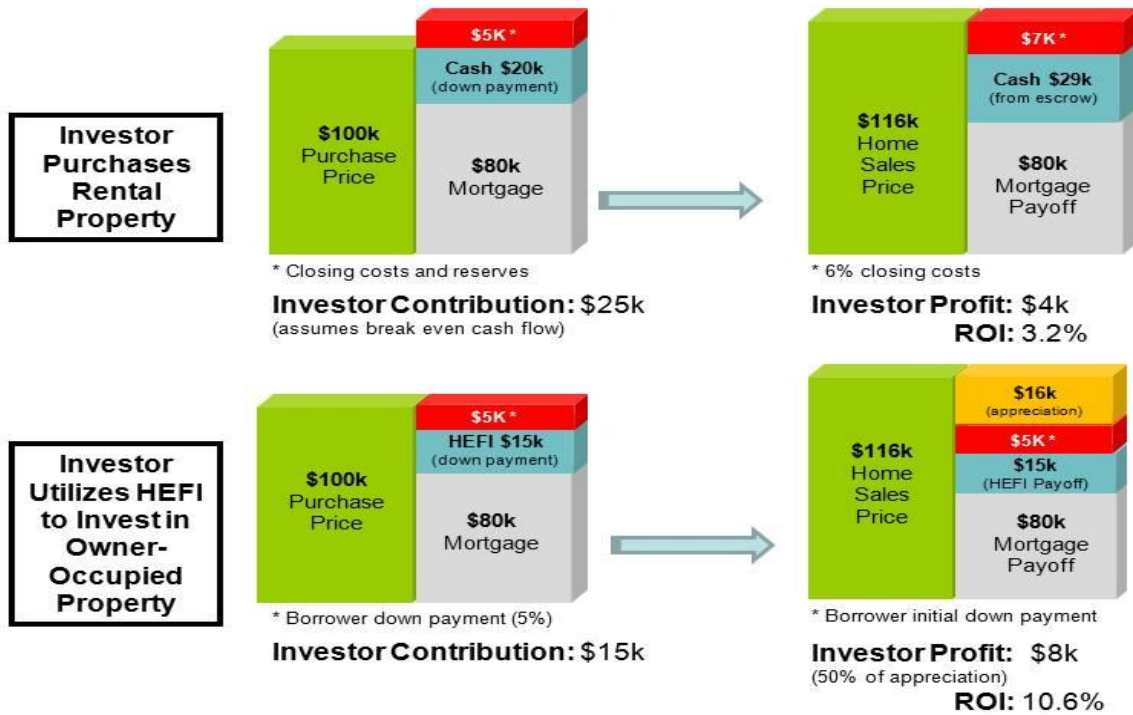
HHP Program With HEFI



Seller Net at closing: \$102K
Borrower Payment: \$510 / month
Additional Seller Net* at year 5: \$27,550

** Assumptions are based on house selling at year 5 with 3% growth per year and a 50% HEFI appreciation share. Percentage of HEFI appreciation sharing is flexible and specific to each HEFI owner*

INVESTORS:



* Assumptions are based on house selling at the end of year 5 with 3% growth per year and a 50% HEFI appreciation share. Percentage of HEFI appreciation sharing is flexible and specific to each transaction.

Equity sharing concepts:

Businesses have embraced the concept of debt and equity for hundreds of years. It is not only seen as practical but as an intelligent way to diversify risk.

The Business Solution: Firms that have distressed revenues, but remain viable with lower debt, undergo *financial restructuring*:

- Lenders *reduce debt* in exchange for a fraction of *equity*
- The resulting deleveraged firm can continue in business
- Costly liquidation is avoided
- Equity retained by managers provides proper incentives

The HEFI Solution: The business solution has a direct equivalent in the residential housing market:

- Homeowners can avoid foreclosure by granting a fraction of homeowner equity in exchange for a reduction in their mortgage balance
- Homeowners continue to remain in homes and retain benefits and obligations of ownership
- Foreclosure costs to bank and community are avoided

- Homeowners' residual equity provides proper incentives for continued mortgage service and maintaining the property
- Value of equity fraction received mitigates lender's write-down

Why is the HEFI unique?

- The HEFI represents a passive investor interest
 - Similar to corporate equity
 - Not tied to the mortgage
 - Homeowner retains full ownership rights and obligations
- HEFIs can be sold into capital markets
- The HEFI is the *only* fair solution available
 - Eliminates moral hazards and is fair to taxpayers and non-participants
 - Subsidies are not required
- The HEFI is the only practical way to diversify residential equity exposure
- The HEFI provides a much needed alternative to down payment assistance programs that can be utilized by builders and homeowners
- In an event of default, a costly and lengthy foreclosure process is avoided
- The HEFI introduces equity financing to the residential real estate market, a concept that has been accepted and utilized by the commercial real estate market for over 100 years.

Capital markets interest in the HEFI:

The HEFI security represents a passive investor interest in a home; just as a share of stock represents a passive investment in a company. The HEFI security is analogous to a call option.

Institutional investors such as pension and endowment funds would be interested in HEFIs to achieve diversification beyond stocks and bonds. The residential equity asset class is as large as the entire US stock market. To be properly diversified, institutional investors might want to hold about as much in the residential equity asset class as they do in stocks.

Right now, though, there is no practical way for them to invest in residential equity; HEFIs and a HEFI trading market would create an attractive and practical way for them to invest in this asset class.

Q&A:

Q: Is HEFI the first equity sharing idea to come to market?

A: *No, equity sharing concepts have been utilized by affordable housing initiatives for over 30 years and on over 800,000 different homes: <http://www.nhi.org/pdf/SharedEquityHome.pdf>
The HEFI is a standardized delivery system for shared equity that makes it viable outside of the affordable/subsidized housing market.*

Q: How is the HEFI recorded on title since it is not a debt?

A: *The HEFI is recorded as a lien against the property, much the same as a mechanics lien, a tax lien or a legal judgment lien is recorded.*

Q: Why is the HEFI structured as an option instead of the HEFI owner taking title today?

A: *Being structured as an option is important in that it allows the homeowner to remain vested on title as 100% owner. It also allows the HEFI owner to remain silent and passive; unless an event of default occurs.*

Q: When would a HEFI owner exercise their option to take a tenant-in-common interest?

A: *The HEFI owner may only exercise their option if an event of default occurs. Some of the events of default are: failure to keep payments current (mortgage, insurance, taxes, etc.), a non-permitted ownership transfer occurs, failure to maintain the property in good working condition, false or misleading representations and warranties, etc.*

Q: Why would a HEFI owner exercise their option to become a tenant-in-common owner in the case of a default?

A: *Because, as a tenant-in-common owner the HEFI owner can step into the homeowner's shoes and effect a sale of the property to protect their collateral, as opposed to how a second mortgage lien would be left to wait for the first mortgage to perform a foreclosure.*

Q: How would a HEFI owner know when an event of default occurs?

A: *HEFIs will be managed and serviced through a platform called HEX, Home Equity Xchange. HEX will monitor and track all HEFIs and their underlying collateral on a monthly, quarterly and yearly basis.*

Q: When can a homeowner redeem/buy-back the HEFI?

A: *The homeowner may redeem/buy-back the HEFI at any time* he/she wishes. A procedure is built into the system to assure the HEFI Owner that the buyback price is fair at the time the buyback is requested.*

Q: What effect does the HEFI have on other programs?

A: *The HEFI would not preclude borrowers or lenders from availing themselves of other government programs, such as HAMP, homebuyer tax credits or interest reductions. Those programs add to the attractiveness of HEFIs.*

** In most cases the redemption/buy-back is restricted to after the first 12 months*

Home Equity Xchange (HEX):

HEX, short for Home Equity Exchange, is a cutting edge process that simplifies how HEFI ownership and servicing rights are originated, sold and tracked. No longer is there the burden of preparing and recording assignments when issuing and trading HEFIs. The chain of title is simplified as well because it begins and ends with HEX. The HEX system can report the status of all HEFIs: beneficial interests, investors, and servicing.

- HEX functions as the singular portal where Homeowners and HEFI owners can be interfaced with the highest concern for security and information management.
- HEX combines the services of a legal document preparation system, a security instrument tracking system (similar to MERS), a servicing platform and a singular repository of relevant data for proper analytics to be applied for secondary trading of HEFI's.
- From origination to securitization, HEX will be the singular repository where all equity transactions can be processed and coordinated.

Benefits of HEX:

- Automates the processes of origination through issuance to servicing of the HEFI
- Allows for a simplistic hands-off management of the HEFI collateral by the HEFI owner:
 - Monitors the homeowner's obligations under the HEFI Agreement:
 - Mortgage payment, including taxes and insurance, are paid on time
 - Property maintenance is properly kept up
 - Property has owner's insurance
 - Monitors the title:
 - No unauthorized subordinate liens become attached to the property
 - No unauthorized transfers of title are made
- Acts as the liaison between the homeowner and the HEFI owner:
 - Allows the homeowner to make inquiries about pertinent issues the HEFI owner will want to stay abreast of, such as home improvements, etc.
 - Calculates the payoff during a HEFI redemption, whether the homeowner wishes to sell the property or buy out the HEFI owner
- Functions as a virtual trading platform to transfer the HEFI ownership amongst different parties with the click of a button
- Provides an interface to work with the capital markets once HEFIs become saleable in the securities market
- Allows for the aggregation of all HEFI data to improve on the execution of HEFI sales and/or securitization
- Provides easy access to all relevant HEFI data to perform granular level analytics

EquiDebt Solutions:

EquiDebt has positioned itself as a structuring and advisory agent for entities in the residential real estate arena.

- EquiDebt Currently holds the *only* unrestricted license to represent the HEFI
- EquiDebt controls HEX, LLC (Home Equity Xchange), the platform that issues, services, tracks and manages the HEFI instruments
- The HEFI is licensed to EquiDebt by Home Equity Securities, the inventor and author of the patents solidifying the proprietary nature of the HEFI security

Focus and opportunity:

EquiDebt's primary focus today is on the implementation of the HEFI (Home Equity Fractional Interest) in loss mitigation efforts and as an alternative to down payment assistance for builders and REO sellers. Ultimately these efforts will open the door for the HEFI to be used as a retail product, presenting a financing alternative to today's 2nd liens and HELOCs.