PROGRESS OF THE MAKING HOME AFFORDABLE PROGRAM: WHAT ARE THE OUTCOMES FOR HOMEOWNERS AND WHAT ARE THE OBSTACLES TO SUCCESS?

HEARING

BEFORE THE

SUBCOMMITTEE ON
HOUSING AND COMMUNITY OPPORTUNITY

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED ELEVENTH CONGRESS

FIRST SESSION

SEPTEMBER 9, 2009

Printed for the use of the Committee on Financial Services

Serial No. 111–72

U.S. GOVERNMENT PRINTING OFFICE

54–863 PDF WASHINGTON : 2010

For sale by the Superintendent of Documents, U.S. Government Printing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
Fax: (202) 512–2104 Mail: Stop IDCC, Washington, DC 20402–0001

HOUSE COMMITTEE ON FINANCIAL SERVICES

BARNEY FRANK, Massachusetts, *Chairman*

PAUL E. KANJORSKI, Pennsylvania
MAXINE WATERS, California
CAROLYN B. MALONEY, New York
LUIS V. GUTIERREZ, Illinois
NYDIA M. VELÁZQUEZ, New York
MELVIN L. WATT, North Carolina
GARY L. ACKERMAN, New York
BRAD SHERMAN, California
GREGORY W. MEEKS, New York
DENNIS MOORE, Kansas
MICHAEL E. CAPUANO, Massachusetts
RUBÉN HINOJOSA, Texas
WM. LACY CLAY, Missouri
CAROLYN MCCARTHY, New York
JOE BACA, California
STEPHEN F. LYNCH, Massachusetts
BRAD MILLER, North Carolina
DAVID SCOTT, Georgia
AL GREEN, Texas
EMANUEL CLEAVER, Missouri
MELISSA L. BEAN, Illinois
GWEN MOORE, Wisconsin
PAUL W. HODES, New Hampshire
KEITH ELLISON, Minnesota
RON KLEIN, Florida
CHARLES A. WILSON, Ohio
ED PERLMUTTER, Colorado
JOE DONNELLY, Indiana
BILL FOSTER, Illinois
ANDRÉ CARSON, Indiana
JACKIE SPEIER, California
TRAVIS CHILDERS, Mississippi
WALT MINNICK, Idaho
JOHN ADLER, New Jersey
MARY JO KILROY, Ohio
STEVE DRIEHAUS, Ohio
SUZANNE KOSMAS, Florida
ALAN GRAYSON, Florida
JIM HIMES, Connecticut
GARY PETERS, Michigan
DAN MAFFEI, New York

SPENCER BACHUS, Alabama
MICHAEL N. CASTLE, Delaware
PETER T. KING, New York
EDWARD R. ROYCE, California
FRANK D. LUCAS, Oklahoma
RON PAUL, Texas
DONALD A. MANZULLO, Illinois
WALTER B. JONES, JR., North Carolina
JUDY BIGGERT, Illinois
GARY G. MILLER, California
SHELLEY MOORE CAPITO, West Virginia
JEB HENSARLING, Texas
SCOTT GARRETT, New Jersey
J. GRESHAM BARRETT, South Carolina
JIM GERLACH, Pennsylvania
RANDY NEUGEBAUER, Texas
TOM PRICE, Georgia
PATRICK T. MCHENRY, North Carolina
JOHN CAMPBELL, California
ADAM PUTNAM, Florida
MICHELE BACHMANN, Minnesota
KENNY MARCHANT, Texas
THADDEUS G. McCOTTER, Michigan
KEVIN McCARTHY, California
BILL POSEY, Florida
LYNN JENKINS, Kansas
CHRISTOPHER LEE, New York
ERIK PAULSEN, Minnesota
LEONARD LANCE, New Jersey

JEANNE M. ROSLANOWICK, *Staff Director and Chief Counsel*

SUBCOMMITTEE ON HOUSING AND COMMUNITY OPPORTUNITY

MAXINE WATERS, California, *Chairwoman*

NYDIA M. VELÁZQUEZ, New York
STEPHEN F. LYNCH, Massachusetts
EMANUEL CLEAVER, Missouri
AL GREEN, Texas
WM. LACY CLAY, Missouri
KEITH ELLISON, Minnesota
JOE DONNELLY, Indiana
MICHAEL E. CAPUANO, Massachusetts
PAUL E. KANJORSKI, Pennsylvania
LUIS V. GUTIERREZ, Illinois
STEVE DRIEHAUS, Ohio
MARY JO KILROY, Ohio
JIM HIMES, Connecticut
DAN MAFFEI, New York

SHELLEY MOORE CAPITO, West Virginia
THADDEUS G. McCOTTER, Michigan
JUDY BIGGERT, Illinois
GARY G. MILLER, California
RANDY NEUGEBAUER, Texas
WALTER B. JONES, JR., North Carolina
ADAM PUTNAM, Florida
KENNY MARCHANT, Texas
LYNN JENKINS, Kansas
CHRISTOPHER LEE, New York

CONTENTS

WITNESSES

Wednesday, September 9, 2009

APPENDIX

Additional Material Submitted for the Record

PROGRESS OF THE MAKING HOME AFFORDABLE PROGRAM: WHAT ARE THE OUTCOMES FOR HOMEOWNERS AND WHAT ARE THE OBSTACLES TO SUCCESS?

Wednesday, September 9, 2009

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON HOUSING AND
COMMUNITY OPPORTUNITY,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10:39 a.m., in room 2128, Rayburn House Office Building, Hon. Maxine Waters [chairwoman of the subcommittee] presiding.

Members present: Representatives Waters, Cleaver, Green, Clay, Donnelly, Kilroy, Himes; Capito, Biggert, Miller of California, Marchant, Jenkins, and Lee.

Ex officio present: Representatives Frank and Bachus.

Also present: Representative Bean.

Chairwoman WATERS. Good morning. This hearing of the Subcommittee on Housing and Community Opportunity will come to order. Good morning, ladies and gentlemen.

I would like to thank our ranking member and the other members of the Subcommittee on Housing and Community Opportunity for joining me today for this hearing on, "Progress of the Making Home Affordable Program: What are the Outcomes For Homeowners and What are the Obstacles to Success?"

I would also like to thank Melissa Bean. She asked to sit in on today's hearing, and I request unanimous consent that Representative Melissa Bean be considered a member of the subcommittee for this hearing.

Today's hearing will revisit the Making Home Affordable Program, the Administration's systemic loan modification and refinance program, 6 months after its introduction. In March, we held a hearing on the rollout of the program and heard from government officials and housing experts about how the program could assist struggling homeowners. Today we will hear from witnesses about some of the obstacles and challenges with the program, and gain a better understanding of what has worked and what is not working for homeowners.

As unemployment continues to soar, reaching a record high of 9.7 percent in August, the number of homeowners entering foreclosure has also increased. According to the Mortgage Bankers Association, the rate of home loans in the foreclosure process has quadrupled from 1 percent in 2006 to over 4 percent in 2009. Furthermore, foreclosures have only accelerated in 2009, with RealtyTrac reporting a 7 percent increase in foreclosures from June to July of this year. In my own home State of California, the foreclosure rate jumped from 2.15 percent in June 2008 to 3.37 percent in June 2009. And the foreclosure crisis shows no sign of slowing down, with Credit Suisse estimating that 8.1 million homes will enter foreclosure over the next 4 years.

In response to the ongoing foreclosure crisis, President Obama established the Making Home Affordable Program to help up to 7 to 9 million homeowners stay in their homes. The program consists of three main parts, including the Home Affordable Refinance Program and the Home Affordable Modification Program.

The Home Affordable Refinance Program is designed to help underwater homeowners whose property is worth less than the amount owed on the loan. However, only 600,000 borrowers with loan-to-value ratios higher than 80 percent have been able to refinance.

The Home Affordable Modification program was intended to help up to 3 to 4 million homeowners with loans not held by Fannie Mae or Freddie Mac by reducing their monthly mortgage payments. Because the program is voluntary, the government provides incentives to servicers for participation; however, to date, only 15 percent of the eligible 2.7 million homeowners have received assistance under this program, with 400,000 offers extended and 230 trial modifications underway. The Administration has requested that servicers ramp up implementation to a cumulative 500,000 started by November 1, 2009. However, more needs to be done.

I have been hearing about homeowners and counselors waiting months to hear back from mortgage servicers for the processing of trial modifications. There are also complaints about participating servicers who often give incorrect information or are unable to answer general questions about the Home Affordable Modification Program. There are even servicers who continue to initiate foreclosure proceedings while the Modification Program application is pending.

Although I recognize that servicers are dealing with an unprecedented volume of troubled mortgages, I also recognize that unless more modifications are done, the foreclosure crisis will not end any time soon. It is appalling that 6 months after the implication of the Making Home Affordable Program, some servicers here today reported enrollment of only 4 percent of all eligible borrowers in the program. I hope that our witnesses today will discuss the major obstacles with the program so that we may identify potential resolutions to these issues. Millions of families are losing their jobs and millions more are losing their homes. We need to know we have a system in place that will truly work for struggling American families and keep them in their homes.

I would now like to recognize our subcommittee's ranking member to make an opening statement, and then I am going to call on our Chair of the full Financial Services Committee, Chairman Frank, to make an opening statement. Thank you very much.

Mrs. CAPITO. Thank you, Madam Chairwoman. I would like to yield and have our first opening statement be given by the ranking member of the full committee, Mr. Bachus.

Mr. BACHUS. Thank you, Mrs. Capito. Chairwoman Waters, I also thank you for holding this hearing on the Obama Administration's foreclosure prevention plan.

Despite recent encouraging news on home sales, we are still experiencing an unprecedented number of foreclosures, and it has become apparent that the program that the Administration rolled out with great fanfare some 6 months ago is likely to fall well short of expectations. I believe that the overall approach of the Administration's foreclosure prevention initiative was flawed from the inception. I think the best way, in fact the only way I think to stop this epidemic of foreclosures is to get our economy rolling again. As long as people are losing jobs, they are going to lose their homes, and we basically have no alternative other than to what I think is get the government out of the spending spree that we are witnessing in Washington and the cumulation of massive debts and allow the private sector to create those jobs. I think that is how you save these homes. And I think until Washington restores its fiscal discipline and stops the spending spree we are on, we are going to continue to just substitute public funds and taxpayer funds for the lack of private funds. A homeowner who has lost his job needs a job and not a government handout.

Let me say this: The message I think that our constituents gave us over the August break, and they gave it loud and clear, is that they don't want to pay the bill for another untested government program. And I think this is one of those programs and, unfortunately, I don't think it is going to demonstrate a lot of success.

Another concern about the Administration's foreclosure mitigation plan is with all these programs is the opportunity for fraud and abuse that it presents to those who charge upfront fees for loan modifications which never happen, as well as the borrowers who misrepresent their financial situation to secure more favorable terms. Going forward, transparency and strict oversight of the program is imperative to prevent future abuses and limit taxpayer losses.

On another note, I notice that the chairman of the full committee is here and I want to express to him and the committee that I am troubled by his announcement yesterday that he intends to include a bankruptcy cramdown in his broader package of regulatory reform. A bankruptcy cramdown, which was rejected by the Senate earlier this year, would severely undermine recent measures taken to unfreeze credit by private markets and, I think, would prolong our housing recovery by adding uncertainty to the market and increasing mortgage costs for the vast majority of Americans and would precipitate some of the very things that we are attempting to prevent or the Administration is attempting to prevent in its legislation.

I know the terrible cost of foreclosure not only for the families involved but for the communities. It is a terrible thing that we are all witnessing with these high foreclosure rates. But I still think that the government simply has to end its substitution of public debt for private debt. If we don't, not only I think are we going to continue to drag this economy down and cause greater losses of jobs, but we are also going to pile up an unpayable debt on our children and grandchildren.

And I will close by saying I note in the Wall Street Journal that the dollar has hit a new low. I believe, importantly, that we have had a strong dollar, and that that has been a real benefit for us. But I think all these spending programs are undermining our currency, and I think that would be a disaster for this country.

Thank you.

Chairwoman WATERS. Thank you very much. Mr. Chairman?

The CHAIRMAN. Thank you, Madam Chairwoman. And I think a very stark difference in approach to the foreclosure issue has just been put before us. The gentleman from Alabama says we should do nothing to alleviate the specifics of foreclosures. His proposal is to increase jobs. I will point out that according to the single most important appointment to an economic post that George Bush made, Chairman Ben Bernanke of the Federal Reserve, the economic recovery program that the gentleman voted against and still apparently laments significantly increased jobs. Mr. Bernanke said that there would be fewer jobs if we did not have this. He in his report to us volunteered several instances in which he—several specifics which had that increase.

So I do agree jobs are better. But I also think that the analysis we just heard is badly flawed because it lumps together all kinds of foreclosures. Yes, unemployment is causing a new wave of foreclosures. These are people who got mortgages that were perfectly sensible for them at the time they got them, but you can't pay your mortgage out of unemployment. But that ignores the fact that the foreclosure crisis is one that was inherited by this Administration from the Bush Administration back at a time when we were not in an unemployment crisis. That is a result of mortgages that should not have been made. That is the result of mortgages that should not have been made because officials like Alan Greenspan refused to use authority he was given to prevent bad mortgages from being made. That is what we are trying to deal with when we talk about new legislation to stop irresponsible mortgages.

So, yes, it would be a useful thing to get more jobs for a lot of reasons. And some of the foreclosures are caused by job loss, but a large number are not related to job loss. And so what the gentleman says is he doesn't like this program, he doesn't like the notion of bankruptcy. His only approach is to get more jobs. And that is, obviously, wholly inadequate to the problem of those mortgage foreclosures that are happening because things were not done appropriately at the time the mortgages were granted.

The final thing I would say is, yes, I do think bankruptcy has become relevant. We are talking about a bankruptcy bill that would be limited in time to mortgages already granted. The notion that this would somehow stop the flow of credit is hard to maintain in that case. It would have nothing to do with credit going forward.

And I will reiterate, I am disappointed at the pace of this program. I also believe that there are legal obstacles here. We have second mortgages. We have a problem with nobody having the authority, we are told in some cases, to modify the mortgage because of the way the servicing model has gone forward. And one of the things that we will do next year, I hope, is to change the law so that you will not have this situation in which no one can modify the mortgage. It is very bad public policy for us to allow to exist in law a situation in which there are important decisions that should be made in everybody's interest and no one to make them. And we know that. There are people who say, yes, it would be good if we could modify this, if we could reduce the principal or do this. But no one has the authority do it and no one can decide how you arbitrate between first and second mortgages. So we will do that going forward. But to cut through that current tangle, I think bankruptcy is effective.

And let me just say about bankruptcy, the notion that there are people out there eager to go bankrupt is of course fallacious. Bankruptcy is no picnic. We do believe that the possibility of bankruptcy will be an important incentive to getting things done.

And I would say finally, to the servicers in particular, many of whom are in large banks who don't like the notion of bankruptcy, to a great extent whether or not that gets done this fall will be up to them. Yes, it is true, as the gentleman points out, in the Senate, that was defeated. In the House, it passed. But if we continue to have a situation in which people are so frustrated by the inability to get the mortgage foreclosure modifications that we need, not just for individuals but for the economy, for all of the negatives that the foreclosure rate has in the economy, they are—let me put it this way. The best lobbyists we have for getting bankruptcy legislation passed are the servicers who are not doing a very good job of modifying mortgages. And if they do not improve their performance, then they improve the chances of that legislation.

Finally, let me just thank the Chair of this subcommittee who has been as effective and dedicated in fighting this as any Member. And she was one of the first to say that we need to change the legislation so that going forward we don't find ourselves in this tangle, and she will be in a major role next year as we do that.

Thank you, Madam Chairwoman.

Chairwoman WATERS. Thank you very much, Mr. Chairman. Mrs. Capito.

Mrs. CAPITO. Thank you. I would like to thank Chairwoman Waters for holding this hearing this morning and for her continued dedication to helping families in need. Today's hearing is a follow-up to a hearing this subcommittee had in March of this year when the Administration first rolled out the Making Home Affordable Program. Introduced with the promise of helping 7 to 9 million troubled borrowers, this program to date has assisted approximately 6 percent of that population.

While Making Home Affordable has been somewhat more successful than the troubled HOPE for Homeowners, I do have significant concerns with the potential overestimation of the populations assisted by the programs and the pace, as the chairman said. There are certainly Americans who received complicated mortgage products that they did not completely understand and now cannot afford; however, we should be good stewards of the taxpayers' money to ensure that we help those families who truly need assistance the most. We need to be fair to the millions of Americans who are cutting their family budgets to stay current on their mortgages and monthly expenses, and make certain that we extend that helping hand to those who most need the help. Furthermore, there needs to be strict oversight of these programs to prevent fraud by both the borrowers who misrepresent financial information and fraudulent modification businesses that we have heard testimony about in this committee that seek only to collect fees without modifying the loans.

The difficulties in the housing market are not static; rather, they have continually evolved over the last several years. Initially, delinquencies and foreclosures began increasing because of resetting adjustable rate mortgages, but now we are seeing increases in foreclosures from more traditional economic events like the loss of a job or excessive debt. And, I would add to that, falling real estate prices. Rapidly approaching on the horizon are new problems like the resetting of interest only and option adjustable rate mortgages. The programs that we create must have the flexibility to address the ever-changing issues in the housing market.

Additionally, we need to foster an environment for private sector job growth in this. We need the economy to improve dramatically. But the trend on our unemployment has risen drastically. Returning Americans to the workforce will allow them to pay their monthly expenses, which they want to do, and return us to the road towards prosperity.

I look forward to hearing from the witnesses today, and I thank the chairwoman for holding this hearing today.

Chairwoman WATERS. Thank you very much. We are now going to welcome our distinguished first panel.

Let me just inform our members here today that we basically have an agreement that we will do 10 minutes on each side, so we are going to move forward with our first panel. One of our witnesses must leave, so I want to make sure that we get some good questions in. Thank you very much.

Our first witness will be Mr. Michael Barr, Assistant Secretary for Financial Institutions, U.S. Department of the Treasury. Our second witness will be Mr. David Stevens, Assistant Secretary for Financial Institutions and Federal Housing Administration Commissioner, U.S. Department of Housing and Urban Development. Welcome. Mr. Barr.

STATEMENT OF THE HONORABLE MICHAEL S. BARR, ASSISTANT SECRETARY FOR FINANCIAL INSTITUTIONS, U.S. DEPARTMENT OF THE TREASURY

Mr. BARR. Thank you very much, Chairwoman Waters, and members of the subcommittee. Thank you for the opportunity to testify today about our comprehensive initiatives to stabilize the U.S. housing market and to support homeowners. I want to outline the steps that President Obama and his Administration have taken to strengthen the housing sector, help millions of homeowners, and lay the foundation for economic recovery and for financial stability.

President Obama worked with Congress to enact the largest economic recovery plan since World War II to help the private sector create jobs. As part of the Recovery Act, we boosted housing by implementing a new home buyer credit. We announced Making Home Affordable, a plan to stabilize the U.S. housing market, lower interest rates, and offer assistance to millions of homeowners by reducing mortgage payments and preventing affordable foreclosures.

This plan includes three main elements. First, broad support to Fannie Mae and Freddie Mac to support mortgage refinancing and affordability across the market. We have supported lower interest rates by strengthening confidence in Fannie Mae and Freddie Mac, including through an additional $200 billion in the stock purchase agreements and continued support for market liquidity.

Second, we have increased refinancing flexibility for the GSEs, providing more homeowners an opportunity to refinance to lower monthly payments. Low rates have enabled over 2.7 million borrowers with GSE loans to refinance since the announcement of the Administration's comprehensive housing plan.

Third, a key part of the Administration's broad housing plan is a comprehensive initiative to lower monthly mortgage payments for borrowers, providing modifications on a scale never previously attempted.

There are signs the plan is working. Forty-five servicers have signed up for the program. More than 85 percent of loans in the country are covered by the program. And servicers have extended over 570,000 trial modification offers. Over 360,000 trial modifications are already underway under the program. We are above our target pace of 20,000 to 25,000 trial modifications started per week, and we are now on track to reach our goal of 500,000 modifications, a half a million modifications, started by November 1st. But we can do better.

On July 28th, we held a meeting with servicers at Treasury where we told servicers that they needed to ramp up faster and to treat borrowers better. We ask servicers to commit to doing more. Servicers must add more staff than previously planned, expand call center capabilities, provide a process for borrowers to escalate servicer performance and decisions, bolster training, enhance online offerings, and send additional mailings to potentially eligible borrowers. Servicers must report the reason for modification denials both to Treasury and to the borrowers. And we are working with servicers and Fannie Mae to streamline application documents and develop Web tools for borrowers.

We also are committed to transparency and to accountability. On August 4th, we began publicly reporting servicer-specific results on a monthly basis. The second public report was published just this morning. These reports provide a transparent and public way of accounting for individual servicer performance as well as performance under the program as a whole.

Second, we are working to establish specific operational metrics to measure the performance of each servicer, and these metrics will be included in our public reports.

Third, we have asked Freddie Mac as compliancy agent to develop a second-look process pursuant to which Freddie Mac will audit a sample of MHA modification applications that have been declined by each servicer. This second-look process began August 3rd, and is designed to minimize the likelihood that borrower applications are overlooked or inadvertently denied. In addition, we are improving borrower outreach which is essential to success in the program. We have launched a consumer-focused Web site, established a call center for borrowers, and launched a series of borrower outreach events in cities facing high foreclosure rates across the country.

There are a number of challenges to implementation, but we believe the program is on track. The program has strong antifraud protection. It has strong compliance protection. It is consistent with the ranking member's suggestion of flexible enough to handle the onset of new problems, new programs, new kinds of issues coming up.

The program has made significant progress in increasing the flow of mortgage credit, bringing down mortgage rates, and providing many families with a second chance to stay in their homes. We can and we must redouble our efforts to broaden the reach of these programs.

Thank you very much.

[The prepared statement of Assistant Secretary Barr can be found on page 56 of the appendix.]

Chairwoman WATERS. Thank you very much. Mr. Stevens.

STATEMENT OF THE HONORABLE DAVID STEVENS, ASSISTANT SECRETARY FOR HOUSING/FHA COMMISSIONER, U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

Mr. STEVENS. Chairwoman Waters, Ranking Member Capito, and members of the subcommittee, thank you for the opportunity to testify on the Making Home Affordable Program and other Administration efforts to homeowners and neighborhoods suffering in the foreclosure crisis.

Madam Chairwoman, I would like to thank you for your leadership, your commitment as Chair of this subcommittee to ensuring that the Administration's efforts help as many families as possible. That is always important, but particularly important during this difficult time.

My colleague has done an excellent job describing the progress to date in the Making Home Affordable Program. And while I have submitted lengthier testimony for the record, I would like to focus my remarks on HUD's efforts to stem the tide of foreclosures, both in our work in Washington and, just as importantly, on the grounds and neighborhoods across this country.

First, the Neighborhood Stabilization Program: Recognizing that concentrated foreclosures can wreak havoc on once stable communities, HUD is working to ensure that nearly $6 billion appropriated by Congress for NSP help stabilize housing markets, and combat blight through the purchase and redevelopment of foreclosed and abandoned homes and residential properties. HUD worked quickly to allocate $4 billion in funds under NSP-1 to 309 grantees in 55 States and territories and 254 selected local governments. And we allocated another $2 billion on a competitive basis to States, local governments, and nonprofit organizations under the second round of funding authorized by the Recovery Act.

NSP has emerged as an essential tool as we facilitate the transformation of foreclosed homes into affordable housing.

Second, I want to talk about our counseling efforts, which are critical to turning back the foreclosure crisis. With more than half of all foreclosures occurring without servicers or borrowers ever engaging in a discussion about potential options to prevent foreclosures, HUD is mobilizing its vast network of counselors and nonprofits to provide critical assistance to the record numbers of homeowners at risk of foreclosure. Armed with this wealth of information, HUD-approved counselors provide assistance over the phone and in person to those seeking help with understanding the MHA program. They explain options available to FHA-insured homeowners, and often work with borrowers eligible for the Administration's refinancing modification programs to compile an intake package for the servicers. These services are provided free of charge by nonprofit housing counseling agencies working in partnership with the Federal Government and working in part by HUD and NeighborWorks America.

In addition, HUD, working with Treasury and the Home Ownership Preservation Foundation, is encouraging distressed borrowers to contact the Homeowners HOPE hotline. The 24-hours-a-day, 7-days-a-week hotline utilizes many HUD-approved counselors who can also help the homeowners reach and resolve issues with servicers.

As part of the Administration's nationwide campaign to promote the Making Home Affordable Program in communities most in need, we are also involved in a series of outreach events to engage local housing counseling agencies, community organizations, and others to build public awareness of Making Home Affordable, educate at-risk borrowers, and prepare borrowers to work more efficiently with their servicers.

As HUD leverages its own relationships with local housing partners on the front lines, we are also encouraging servicers to leverage their relationships with nonprofits to expedite the processing and approval of modification applications. With Treasury, we are working to establish guidelines for servicers entering relationships with trusted advisers to guide borrowers through the application process, and help them complete application packages and troubleshoot if the borrower appears to have been improperly deemed ineligible for the program.

Third, we are launching the HOPE for Homeowners Program as a result of the new legislative improvements featured in the Helping Families Save Their Homes Act of 2009 and its integration into MHA. We believe it should be a more attractive option for more homeowners, particularly for underwater borrowers ineligible for GSE refinancing programs seeking to refinance their homes and gain equity in their homes. Servicers will now be required to offer the option for an H for H refinancing in tandem with an MHA, Making Home Affordable, trial modification option.

Lastly, as Commissioner of FHA, I should note that homeowners with FHA-insured loans have long been eligible for a variety of loss mitigation programs to help protect them from foreclosure. Last year, more than 500,000 families were assisted through forbearance, partial claim, loan modification, pre-foreclosure sale, or a deed in lieu of foreclosure, amongst others. That is in part because the servicers of FHA-insured loans are required to notify delinquent homeowners about the options available to them to help them make their monthly payments and to take such steps before initiating foreclosure proceedings. As a result, we expect another half million families will be protected from foreclosure in 2009 through benefits provided by FHA insurance.

We recently unveiled FHA Home Affordable to give qualified FHA-insured borrowers the opportunity to obtain assistance under terms comparable to those under MHA without increasing costs to the taxpayer. By offering a partial claim of up to 30 percent of the unpaid balance, deferring repayment of mortgage principal through an interest free subordinate mortgage that is not due until the mortgage is paid off, we can permanently reduce the family's monthly mortgage payment to an affordable level.

HUD is also working with Treasury and other Administration agencies as we continue to monitor the progress of the Making Home Affordable programs. With home prices declining, the sale of existing and new homes increasing for 5 consecutive months, and homebuyer confidence on the rise, the Administration is exploring a series of programmatic options to build on these initial signs of stabilization. Collectively, Madam Chairwoman, these efforts should signal to every American that the Obama Administration is absolutely committed to helping as many families as possible avoid foreclosures.

Once again, I would like to thank you for the opportunity to participate in today's hearing and for your continued leadership and commitment. And while we have seen progress in the Administration's efforts to address this crisis and make changes where necessary, HUD shares your concern about the speed of progress. We are working hard to resolve the issues related to the implementation of core programs, and to develop new elements that improve and refine MHA. And, as always, we stand committed and ready to help and explore any options that Congress or other participants of the industry may have to improve results at this time of crisis.

Thank you.

[The prepared statement of Assistant Secretary Stevens can be found on page 157 of the appendix.]

Chairwoman WATERS. Thank you very much. I will now recognize myself for 5 minutes.

Mr. Barr, while 45 servicers, as you described, have signed up for the Home Affordable Modification Program, representing nearly 85 percent of the mortgage market, only 15 percent of the eligible 2.7 million borrowers have received assistance. At the time the program was introduced, what was the expected rate of enrollment? How many eligible homeowners were expected to be enrolled? And within what time period, moving forward, what is the expected rate of enrollment in the next 3 months, 6 months, a year?

Mr. BARR. Thank you, Madam Chairwoman. In the initial design of the program, our expectation was that there was going to be a period of ramp-up in the program. We are on track to meet the goals that we designed the program to meet in February.

Chairwoman WATERS. Excuse me one moment, please. All right. Thank you.

Mr. BARR. In the initial design of the program, we expected there to be a ramp-up in the program given the significant time servicers would need to change their basic systems and for Treasury and the other participants, Fannie Mae and Freddie Mac, to put their systems in place.

We are on track to meet the goal that we enunciated at the beginning of the program, which is to reach 3 to 4 million borrowers over the 3-year period beginning from initiation of the program. When we announced the program, I explained that we wanted to be at a rate of 20,000 to 25,000 trial modifications begun each week. We expected to hit that level in August. We actually hit it in July. So we are on track or exceeding the goals that we established. We are on track now with 360,000 modifications started, we are on track to reach the goal by November 1st of half a million modifications begun by November 1st. And, we expect that we will be continuing to ramp up the program going forward.

Now, it doesn't mean that there is perfection out there in the world. There are lots of problems and program implication that could be done better, that need to be done better. There is unevenness in performance, as you can see from our public reports, unevenness in performance between and among the servicers involved. We think all the servicers can do more than they are doing now, and we would like to continue to work with them to see better results.

Chairwoman WATERS. How will the Treasury respond if the rates of loan modifications and refinancing continue to fall short? You say you are on track.

Mr. BARR. I think there is more that we can do. We can continue to make improvements in the implementation of the program, as I suggested, better operational metrics so we know that servicers are treating borrowers the way we would like them to be treated; that borrowers are getting good response time at the call centers; that we are doing a better job reaching out to borrowers to be sure we can reach everybody we can under the program, and that borrowers say yes whenever they are contacted. We need to be sure that borrowers are not being inappropriately turned down. And that is why we have put in place the Second Look Program, to audit compliance under the program to be sure borrowers aren't turned down.

So there are a number of steps, including the Web portal, additional compliance, additional second-look programs that we think can continue to ramp up performance under the program.

Chairwoman WATERS. Thank you. I am now going to recognize the ranking member of the full committee.

Mr. BACHUS. Thank you, Chairwoman Waters.

Secretary Barr, as a professor at the University of Michigan Law School, you, along with Harvard professor Elizabeth Warren, are widely recognized as the chief architects of the conceptual framework behind the Consumer Financial Protection Agency. I want to ask you a few questions about the reasoning behind the Consumer Financial Protection Agency, because I think you are probably best able to give us that answer, you or Professor Warren.

In a 2008 paper you published, "Behavioral Informed Financial Services Regulation," that has been referred to in many articles about the new agency, you advocated repeatedly for limiting consumer choice and expressed concerns about consumers having too much choice. Is the proper role of the government to limit consumer choice, or is that a part of what this new agency would do?

Mr. BARR. Mr. Chairman, I would not characterize my article about behavioral regulation as being about limiting choice. It is about understanding how people make decisions in the real world and taking that into account in the structure of regulations.

So, for example, if a borrower is going to be offered a pay option ARM, shouldn't they have the benefit of knowing what the risks and costs of that are in relation to a regular ARM? The basic idea behind the approach is, let's give people the tools they need to make better financial decisions.

So on the credit card bill, one of the things that Congress did is to require the credit card companies to say, what are the actual consequences of only paying the minimum balance? The actual consequence in terms of additional time and cost to pay off a credit card bill. And I think that is an important behavioral tool. That is good regulation, it is smart regulation. That is the kind of regulation the Consumer Financial Protection Agency would be empowered to offer. It empowers people to make better decisions. It doesn't limit consumer choice; it provides room for innovation, but it provides protection for consumers when they need it.

Mr. BACHUS. Well, you say you wouldn't want to limit choice. That is not what the article said. In fact, it says: "Product regulation would also reduce emotional pressures related to potential bad decision making by reducing the number of choices."

Mr. BARR. Right. So in that article, I am describing in distinction to product regulation, which has certain costs associated with it, to financial innovation, I offer an alternative to that, which is less restrictive in the marketplace. So the particular provision that you are describing is describing a form of regulation that is heavier handed than the one that I prefer and I advocated for in the article.

Mr. BACHUS. So you are advocating in the article a more heavy handed approach than you are now advocating?

Mr. BARR. No. The article is describing a lighter approach to regulation. In the particular provision you are referring to, I am contrasting the form that I prefer to the form that you are describing.

Mr. BACHUS. Okay. You say here individuals consistently make choices that they themselves agree diminish their own wellbeing in significant ways.

Mr. BARR. Yes. The empirical literature, Representative Bachus, suggests that in many instances, consumers make decisions that they later regret and that if they had been given full information about the financial consequences of their decisions, they would have made different choices. So if we are able to empower them in advance with the knowledge about what those decisions actually would mean to them, they are likely to make much better decisions.

Mr. BACHUS. So the new agency would not either make those choices or suggest certain choices to them? Or maybe establish a government proposed solution?

Mr. BARR. That is right, Mr. Bachus. I think there is some misunderstanding, for example, about the idea of standard products. The idea of standard products is what I articulated before. So if you offer somebody a pay option ARM, you should give them a best case comparison. So a pay option ARM poses defined kinds of additional risks as compared to, say, a hybrid ARM, a 5/1 ARM with the following characteristics. It is a way of anchoring consumer decisionmaking so they can make better choices.

Mr. BACHUS. So you are not going to suggest a certain choice to them?

Mr. BARR. The government suggests the choice? No, sir.

Mr. BACHUS. All right. I think that is all. Thank you.

Chairwoman WATERS. Thank you very much. Mr. Green.

Mr. GREEN. Thank you, Madam Chairwoman. And as an aside, Madam Chairwoman, I would like to thank you for the hearing that we held in Louisiana over the August break. It was very enlightening and perhaps worthy of a topic of discussion at another time.

Madam Chairwoman, I would like to, if I may, quote what I believe to be a quote from a Republican President, Theodore Roosevelt, who reminded us that: "It is not the critic who counts: not the man who points out how the strong man stumbles or where the doer of deeds could have done better. The credit belongs to the man who is actually in the arena, whose face is marred by dust and sweat and blood, who strives valiantly, who errs and comes up short again and again, because there is no effort without error or shortcoming, but who knows the great enthusiasms, the great devotions, who spends himself for a worthy cause; who, at the best, knows, in the end, the triumph of high achievement, and who, at the worst, if he fails, at least he fails while daring greatly, so that his place shall never be with those cold and timid souls who knew neither victory nor defeat."

We are in the arena. Dr. King reminds us that the greatest measure of a person is not where he stands in times of comfort and convenience, but where do you stand in times of challenge and great controversy? When you are in this arena and you have 46 million people uninsured, unemployment is 9.7 percent, where do you stand? I stand with the American people. I stand for augmenting what we are doing today with bankruptcy. We bailed out Bear Stearns, tens of millions of dollars. We bailed out the auto industry, scores of billions of dollars. We bailed out AIG, $180 billion. We can bail out people who are having a crisis in their home foreclosures not because they are not hard workers but because of the cascading impact of the financial crisis that had impacted their jobs. They are losing their jobs. I want jobs right now, too. But we don't have them right now. So since we don't have them right now, the question isn't really do we want jobs right now. The question is, what do we do right now? What do we do when we don't have the jobs for people to come back and make their own way through life? Fend for themselves? What do we do when they are losing jobs and about 16 percent of all mortgages are predicted to go into foreclosure within the next 4 years? What do we do now, is the question.

I think what you are doing is admirable, both of you Secretaries, but I also think that there is a place for bankruptcy. That allows the consumer an option that will afford the consumer the opportunity to, when the servicers can't serve, to go to court and take additional action, action that we should have taken earlier and hence restructured loans. That is what this is all about today, whether we are going to restructure loans or simply refinance loans. Bankruptcy allows for the restructuring of loans in an orderly, systematic way when servicers cannot do so. When servicers cannot do, bankruptcy can allow to be done. These are the American people who will be bailed out, if you want to call it a bailout. American people who worked hard, played by the rules, a lot of them with prime loans that they can't afford to pay now because they are losing jobs because of the financial crisis.

So I see in this an opportunity for us to fashion a bankruptcy bill that is retrospective, not prospective. We won't have the problem of this impacting new loans because it won't apply to new loans. Let me repeat that. Some things bear repeating. This will not apply to new loans. It will not be prospective; it will be retrospective. Some things bear repeating. It will be retrospective, it won't be prospective. You can't make the argument that this is going to impact new loans because it will be retrospective, not prospective.

I risk embarrassing myself by repeating it a third or fourth time, but you know what, sometimes you ought to embarrass yourself to make a point. It will be retrospective, not prospective. We ought not make that false choice. Let's do something for the American people. We are talking about a targeted group of loans that were made, many of which forced people into subprime loans when they qualified for prime loans. We know what happened. The empirical evidence is there. It is time to help the homeowners to maintain homeownership and protect the country from a loss of homes that ultimately will drive down prices even more. We have to do something. We are in the arena. We can make a difference.

One quick question to each.

Do you find any adverse impact that bankruptcy will have on the programs that you are implementing currently? Let's start with you, Secretary Barr. Will bankruptcy adversely impact what you are doing?

Mr. BARR. Would a bankruptcy reform measure?

Mr. GREEN. Bankruptcy bill that is—

Mr. BARR. No.

Mr. GREEN. Retrospective?

Let's move now to Mr. Stevens. Retrospective bankruptcy, not prospective, will it adversely impact what you are doing?

Mr. STEVENS. Not on the retrospective book necessarily.

Mr. GREEN. On the retrospective, that is what we are talking about. I would beg that we not discuss things—no disrespect—that I am not calling to your attention. There are many things that we can talk about today that I quite frankly want to talk about but my time is limited.

With reference to retrospective bankruptcy, will it adversely impact what you are doing?

Mr. STEVENS. No.

Mr. GREEN. Thank you. I yield back.

Chairwoman WATERS. Thank you very much. Mrs. Capito.

Mrs. CAPITO. Thank you, Madam Chairwoman. I would like to ask unanimous consent to submit a statement from the Housing Policy Council.

Chairwoman WATERS. Without objection, it is so ordered.

Mrs. CAPITO. Thank you. I have a couple of comments, specific questions, and then I am going to have ask a general question on your Making Home Affordable graph that as of August 30th, you have the trial modifications started. Do you have any statistics on actual modifications that are considered past the trial period? Because the trial period is if you are on time for 3 months. What are you finding there? People staying on time? Have any of these moved into what, I don't know, what are you going to call it, a solid modification?

Mr. BARR. The trial modifications are real modifications. They really reduce people's payments down to 31 percent debt to income. The question is when they are finalized. They get finalized if the borrower pays on time for 3 months at the end of that time period.

Because the program takes a while to ramp up and there is a 3-month time period through which borrowers need to pass that test, there are very few borrowers who have reached that moment in time between the 3-month trial period and the final period. So we don't have solid enough statistics on those in the final modification yet.

Mrs. CAPITO. So you don't have any preliminary indications of people falling behind or staying on it? Or, is it too early to tell?

Mr. BARR. It is just too early to tell. I want to be hesitant about using information unless I know exactly what the numbers are.

Mrs. CAPITO. I want to ask about the incentives. For instance, CitiMortgage here has 191,000 eligible, they have identified eligible delinquencies. So they get paid $1,000 for identifying each one of those?

Mr. BARR. No. They don't get paid anything for identifying any mortgage. The list here is eligible 90-day delinquencies to provide a baseline of comparison among the different servicers. The determination that a loan is eligible is nothing more than a data point in the chart. What they get paid for doing is for doing a modification that is successful, that reaches the status of a finalized modification. No payment is made unless borrowers successfully reach the point of a final modification, and then they get paid—

Mrs. CAPITO. So we have had none of those, then, because we have had no final modifications.

Mr. BARR. There has been a small amount of payments going to the final amount, but it is too early in the program to assess again exactly those numbers.

Mrs. CAPITO. Just using CitiMortgage.

Mr. BARR. But there are no significant dollars out the door yet.

Mrs. CAPITO. Using them as an example, the Citigroup got $45 billion in the TARP plan, and they have the most to gain if they actually go this direction. I realize, in terms of their bottom line, it is probably a minimal thing. But it is taxpayer dollars going out. Are you finding that servicer payments are proving to be an incentive for people to get, for the servicers to get more involved in this program?

Mr. BARR. We believe a combination of two things are providing strong incentives for servicers to participate. One is having clear program rules, Treasury guidance, establishing an industry standard for modifications. And, second is the structure of the incentive payments both to the servicers as well as to investors.

Mrs. CAPITO. Last question. This is a more general question. We have heard, and I mentioned in my opening statement, too, that rising unemployment is what is contributing now to probably more and more of the foreclosure issues that we are seeing presently. So then we have the question, if you are going to look at loan modifications, how do you modify a loan for somebody who has no income or maybe has such minimal income that it is going to be very difficult for them to have a loan modification? What do you see on that horizon?

Mr. BARR. Servicers generally have in place temporary forbearance programs for people who lose their jobs to give them an opportunity to get back on their feet. And I think there are measures we could take consistent with the program rules to formalize that within the program structures. So I do think we need to be attentive to precisely the circumstance you describe.

Mrs. CAPITO. But in some sense, if certain servicers have a program in place, maybe a 3-month moratorium if you have lost your job, are we kicking the can down the road here, too, to try to help this family the best way that we can?

Mr. BARR. I think there is a balance. I think that if the program goes on too long or is too generous, it is not going to be helpful to anybody. But if it is confined within a set period of time, a lot of people are going to be able to get back on their feet, and you want to give them a temporary respite to do that.

Mrs. CAPITO. And finally, I would like to ask if you could make the committee, or at least me specifically, I am interested in knowing, once the trial modifications are made, how many are sustaining their modification? I hope it is 100 percent. That of course is what we would all want. But what are you seeing in the trend? Because there could be something in statistics very quickly there that we could make adjustments to, to target our dollars more efficiently.

Mr. BARR. As soon as we have data that we think is robust enough to withstand empirical testing, we are going to make that public as part of our regular reporting and make it available to the committee.

I just want to say that although our hope would be that everybody can succeed, I don't think that is a realistic measure of success under the program. We know that some people aren't going to be able to make it, and I think we need to be realistic about our expectations in that regard.

Chairwoman WATERS. Thank you very much. Clarification, Mr. Barr. Did you say that servicers had forbearance for individuals with no income who are approaching foreclosure, that they were doing something to help people who have no income?

Mr. BARR. What I said is many servicers have forbearance programs for people who are temporarily unemployed. And I do think it makes sense within our program to try and formalize that more, and that is one of the areas where I think that we could—

Chairwoman WATERS. Do you know of any who are doing that now?

Mr. BARR. That do temporary forbearance?

Chairwoman WATERS. Yes.

Mr. BARR. I would be happy to have our staff get back with your staff with particular examples.

Chairwoman WATERS. We work with them every day, and we haven't found any yet. I would certainly like to talk to you about that. But, meanwhile, let me move to Mrs. Biggert for 5 minutes.

Mrs. BIGGERT. Thank you, Madam Chairwoman. My question is for Mr. Stevens.

Do you believe that the resources at FHA are enough or do you think that there is a need, particularly in the area of administrative funding, staff increases, and/or extended information technology capabilities to accomplish FHA's oversight needs?

Mr. STEVENS. I appreciate the question. I have stated previously and others have as well that we do believe some additional investment is needed from a resource standpoint, particularly in the area of technology as you have mentioned, to help bring our systems into line.

Mrs. BIGGERT. How long will that take? Because we have been worried for several years on this technology issue and it hasn't been resolved in HUD, or it is not completed yet. Is this going to be in time to do all of the things that are necessary to do now?

Mr. STEVENS. Well, that is a great question. I think at the end of the day there is some deferred investment into systems into FHA in general. And there is a budget request in. Budget requests I know have been made in past years as well. But we are hoping, and we have an initiative, a transformation initiative right now in HUD. We have mapped out the specific investments that we would like to see to upgrade the systems and perhaps replace systems in their entirety. And it won't happen overnight. These are programs that will stretch out over a number of years in order to get them fully implemented.

Mrs. BIGGERT. The Administration plans call for servicers to determine if borrowers are eligible for the HOPE for Homeowners programs. It requires the lenders to write down to 90 percent of the original mortgage the loan to value ratio, and then to pay a 3 percent insurance premium. And often I think there is a need for servicers and lenders to have the flexibility as they go forward to help these borrowers. Do you think that the HOPE for Homeowners program is too restrictive? Should there be more flexibility?

Mr. STEVENS. Well, we certainly weren't satisfied with the results from the first HOPE for Homeowners. We are just now rolling out the revised improvements that were recently legislated, and those will be introduced to the market here in the very near future. Whether it has gone far enough, it is too soon to tell. I think there are some improvements to it; I do believe that it is likely that we may recommend some additional improvements to make it more effective.

Mrs. BIGGERT. Thank you. And then, Mr. Barr, coming back, I think what we are all concerned about is this loss of jobs and then trying to do something to help those people. And I think that is going to grow as we see this. So by what standards should we judge the effectiveness of the Administration's Making Home Affordable plan? If a borrower receives a loan modification and has lower payments but builds no equity over the modification terms, can the plan be deemed successful?

Mr. BARR. Well, I think the basic structure of the modification is designed to improve the borrower's equity position from the moment of modification. It does that in two primary ways. The first is the basic requirement that the structure of the mortgage amortize. And the second is the basic requirement that, a basic incentive for the borrower to keep paying on time. As long as the borrower pays on time, the government will provide an additional small monthly reduction in their principal. So it is a way of keeping borrowers in the program, providing further incentives, building up equity over time. And I think both those measures are important elements of the program.

Mrs. BIGGERT. The borrower thinks they are going to be able to make those payments, but let's say they get into trouble and they get behind 1 or 2 or 3 months. What happens then, and how does that affect the equity?

Mr. BARR. Under our program, we made a basic decision that borrowers were being given a second chance under the modification program; and if they don't perform under that second chance, they don't have the right to continue to participate in the program.

Mrs. BIGGERT. So if they fall 1 month behind, they are out of the program?

Mr. BARR. Not 1 month behind. But if they fall seriously delinquent, then they are not in the program and not eligible to receive these further reductions in equity.

Mrs. BIGGERT. Is that true for all the servicers, then? They have to follow that rule?

Mr. BARR. The servicers would prefer a rule that is even less generous to the borrowers.

Mrs. BIGGERT. I yield back.

Chairwoman WATERS. Thank you very much. Mr. Miller.

Mr. MILLER OF CALIFORNIA. Thank you, Madam Chairwoman. I have really enjoyed the testimony today. This is an unusual market. I have been in it almost 40 years as a developer, and I have never seen anything like this and I applaud you for what you are trying to do, because it is like you are chasing a tail that doesn't exist trying to find it. We have gone through the first round of foreclosures, which are the subprimes, and that still continues. But you are having a second round today that you are having to deal with. That is people who had good homes, good loans, very good business people who are having serious trouble, people who lost their jobs and are just unable to make their payments. And negative home equity has been a huge problem.

I introduced a bill, and I want to thank Chairman Frank and Spencer Bachus for agreeing to cosponsor, that allows banks to take the foreclosed properties and lease them for up to 5 years, or give a lease option to buy to a former homeowner or anybody who wants to, to try to get the distressed property sales off the market. The problem you are having and we are having in California, California has on distressed property sales about 82 percent of the houses in the market are distressed. In L.A. County, it is about 55 percent. Even in Orange County, California, which is a robust housing market, you see about 45 percent. We are trying to chase the bottom of a marketplace that you can't get to. And the purpose of the bill I introduced is to try to allow the marketplace to find a reasonable bottom and start to work its way up, which would help you and your situation trying to deal with individuals who can't make their payments. I applaud you on the loan modification efforts you are attempting, but I want to highlight the fact that those are voluntary on your part.

My good friend, and I have great respect for him, talked about bankruptcies and applying to the residential marketplace. And the problem I have with that is lenders in good faith make a loan to individuals they encumber by a deed of trust which the lender holds at that point in time. And allowing a bankruptcy judge to arbitrarily have the right and go in and restructure that bilateral contractual agreement between the lender and the buyer I think could have horrible consequences in the long run, because it puts the lender in a situation where they believe they are making a loan that they can secure, a residential structure or whether it be a commercial or industrial, it doesn't matter. And if that default occurs, they have the right if they want to voluntarily restructure it, but they also have the right to secure their asset that they have made their loan on. And I think—and with great respect to my good friend, because I have great respect for him and he knows that. I just think in the long run we are going to create great harm to the lending industry because a lender, whether it be a mortgage broker, a bank making this loan—

Mr. GREEN. Would the gentleman yield?

Mr. MILLER OF CALIFORNIA. I would be happy to.

Mr. GREEN. Thank you. We currently allow contracts that are for automobiles to be restructured. We currently allow contracts for farmland to be restructured. We currently allow contracts for your second home, your third home, your fourth home, your fifth home, anything beyond your first home, to be restructured. I would just add equality to the equation, and allow first home buyers to have the same opportunity as that second and third.

Mr. MILLER OF CALIFORNIA. Reclaiming my time, I respect your comments. I really do. I think, though, that heading in this direction could be very dangerous to the marketplace in the long run.

But a question I have for you is, we announced a vote on a bill out of the House that allows banks to basically take properties back, enter as option to buy, or they can hold them off the marketplace and lease them for 5 years to allow the market to create some form of stability. What is your opinion as to that?

Mr. BARR. Representative Miller, I haven't read the legislation. I need to focus—I think conceptually there are attractive features to—in the short term to that kind of approach. I think that in normal economic times the basic approach of the regulatory community is the opposite for reasons that you know—you know far better than I do—in terms of worrying about forbearance and managerial and operational capacity and other factors.

The question is, in the short term does it make sense to have those kinds of approaches? I am attracted conceptually. I think that the—

Mr. MILLER OF CALIFORNIA. I don't expect you to have a firm opinion. But you know how mark-to-market applies to banks in their dealing with distressed properties. They have additional set-asides required based on the principals. If we can get the homes off the marketplace and legally allow these lenders to take those nonperforming assets and make them performing assets through leasing them, I think it puts the lenders in a much better financial situation and I think it removes a tremendous amount of stress and pressure on a down-sliding market.

I will let you continue.

Mr. BARR. So I think that, again, I am conceptually attracted, given the extraordinary circumstances we are in. Again, not in normal times. In normal times, you wouldn't take that kind of measure at all.

Mr. MILLER OF CALIFORNIA. Five years to allow this market to turn around.

Mr. BARR. Well, I think in the particularly strict financial circumstances we are in now, it is worth considering that kind of approach, and I think the concern would be that some financial institutions have the operational managerial capacity, the expertise to do that well, but other firms lack such structures.

Mr. MILLER OF CALIFORNIA. I agree.

Mr. BARR. You would want to make sure that if you took that approach, it was carefully vetted with the supervisors of those institutions and there were no kind of blanket-policy permissiveness, rather really quite institution-focused—

Mr. MILLER OF CALIFORNIA. No. I—

Mr. BARR. —approach. So I think there is room for that within those set of parameters.

Mr. MILLER OF CALIFORNIA. Thank you. I yield back.

Chairwoman WATERS. Thank you.

Ms. Kilroy.

Ms. KILROY. Thank you, Madam Chairwoman. I appreciate it.

It's interesting to note that as foreclosure rates continue to rise—and they are continuing to rise in my community which has been hit so hard by high foreclosure rates over the last 8 years—to see that continue to go on and yet to see a very slow pace of the Help for Homeowners Program being implemented in the district. And my district office gets calls on a routine basis from homeowners who have tried to get help from the program and tried to get help from their banks and are facing delays or denials or higher payments from the program.

I want to know if your office has any benchmarks or standards that you are holding the mortgagers to or particularly those who have taken TARP funds as to how many or what percentage of the borrowers qualify for this program should be getting help from this program by this point in time. What's the standard here?

Mr. BARR. Let me say a few words about that, and maybe Mr. Stevens would like to add a note, too.

I said at the outset that we recognize the programs take a period of time to ramp up. We are on target to hit the goal for the program that we set of hitting 500,000 modifications, a half million modifications, by November 1st. But servicer performance is uneven. It is uneven among servicers. There is also geographic—a likely geographic unevenness as well. Servicers need to do a better job of reaching out to borrowers and finding the eligible borrowers.

We have in place a second-look process that Freddie Mac has just instituted on our behalf, launched last month to look at loans that are being denied to make sure that eligible borrowers are not being excluded from the pool and also to check the eligible pool to make sure that borrowers in that pool are being offered modifications. There is more that we could do in this regard, but I think we are on the right track.

Mr. STEVENS. Just one comment that I would add, and I think one of the common foreclosure numbers that gains a lot of publicity are the RealtyTrac numbers. We were looking at the previous month's numbers, and when you break down the numbers, they show an aggregate amount of, say, 350,000 homeowners received some sort of notice of foreclosure in that month's period. If you break it down, a large portion of those are first notices; a large portion of those are second notices that received a first notice the previous month.

In last month's numbers, the number of homeowners who actually had their homes put into REO, into foreclosure, was under 100,000. And I would say that one of the positive signs we are seeing is that the current ramp rate of the HAMP program, those entering the modification period, is exceeding the actual inventory coming into foreclosure on a run-rate basis. It isn't dealing with the enormous inventory issue yet. It is not reducing it in a significant way. But we do believe that the program is keeping pace with new foreclosures coming into that market. So I think that is a very positive sign about the program.

I mean, the question we ask is, will the program sustain itself? Will it cover a broad enough percentage of the population in real— ultimately, in real numbers to be impactful? What will be the impact ultimately when some of the other large servicers who are slower to ramp up their call center capabilities as they do so?

And we are getting positive signs from some of the larger servicers that give us reason to suspect that the numbers should increase, at least in the short term, as more of the servicing industry gets online here and gets behind the HAMP program.

So the duration questions are real, questions about option ARMs are real. There are a lot of other issues. Unemployment is a real concern. But in terms of the HAMP current process, the activity, we believe it is showing positive signs, at least exceeding the actual foreclosure rates. We will just see if that continues.

Ms. KILROY. Thank you very much.

I yield back.

Chairwoman WATERS. Thank you very much.

Mr. Marchant.

Mr. MARCHANT. Thank you, Madam Chairwoman.

During the recent work period—I have a major servicer lender in my district, and I had the servicing department come in to talk to me, and we spent about 2 hours talking about the problems that they were having implementing this program. In this case, they are lenders and the servicers; and many of the loans that they service, they make. So they have a strong incentive to work these loans out.

Their overall sense of why the program—the drop between the 570,000 and the 360,000— 570,000 people have been offered a modification. Of those, only 360,000 have said, yes, we will accept that modification.

I guess we should know the number of people who tried to enter the pipeline that the 570,000 was derived from. Is that a million? Is that that one out of two? They said that they are getting three to four calls and inquiries per finding a person that actually they can put into the pipeline. That's number one. They find that they have spent far in excess of the $1,000 that they are being offered to modify these loans.

They are also finding out that there is a new phenomena and dynamic among consumers now, and I heard this discussed a couple of nights ago. If the modified payment does not allow them to continue to make their credit card payments, to continue to make their other debt payments, they in many instances are making the decision not to make a mortgage payment.

In traditional terms, we think that the first thing that people are going to make is their mortgage payment and then all other; and what they are finding is that, when they are recalculating these mortgages, their other debt ratios in many instances are 60, 70 percent, and the people simply, even after every one of these modifications that have been offered here, the servicer decides that there is over a 50 percent chance that even if we modify in this program, these people are not going to make their loans.

So the incentive that it appears that they have to modify it and get $1,000 and then be paid back for every year, they are looking at these loans and saying, I am getting four phone calls. Two of the people get to step two or three. One of those two gets into the modification process, and then half of those people aren't going to make their payments under the modification. And the $1,000 isn't enough and the incentive programs that are offered in this just aren't enough because of what they are experiencing.

Now, since they are the lender, they may want to modify the program in spite of all that. But this is a major company. This is what they are experiencing. I don't know if that is what they are telling you, but they are telling their Congressman this.

The people—and I will end on this. The danger that I see in resurrecting the discussion about bankruptcy and the ability to mitigate the debt in bankruptcy is we have a great number of borrowers now that, if we begin to send the signal that that is a possibility again, we will have people who will make the decision to stop making their payments on their homes and wait for that solution.

That's my objection to resurrecting that idea, and I can't believe that it does not—it would have a negligible effect on HUD. I just can't believe that answer it will have a negligible effect on HUD.

Thank you, Madam Chairwoman.

Chairwoman WATERS. Thank you.

Mr. Himes.

Mr. HIMES. Thank you, Madam Chairwoman, and I thank the Assistant Secretaries for being with us today. Thank you for your hard work in addressing one of the more challenging aspects of our financial crisis.

I won't take a lot of time. I just want to recount something that I heard quite a bit in the last 5 weeks as I was in the district. In between those rare moments when I could turn the discussion off of health care reform, I heard very consistently what I know you hear as well, which is just a great deal of frustration with the pace with which these programs have actually addressed the real needs of people.

And of course you understand this here, targeting with the financial institutions, 500,000 modifications started by November, and of course we all know that the estimates are in the next 4 years, we may see as many as 8 million properties enter into foreclosure. The net result of that, which is felt very keenly and very pointedly by somebody like me, is that we are really striving to help 1 in 16 people who are in households that are in a lot of trouble.

So I don't have a question, but I did want to convey the intensity, again amidst the intensity of the health care reform debate, of the sentiment in my district of how the government really could do more.

And I know you are working very, very hard, but I would just urge big thinking. Housing was at the core of the crisis, and as much as I applaud the very tough and good work that you are doing, the remedy at this point is not adequate to the magnitude of the challenge.

Mr. BARR. Thank you.

And if I could just say a couple of words about that, I think that people may lose sight of the breadth of the housing programs that are out there. The program Making Homes Affordable with respect to loan modifications is one important piece of that. The 500,000 loans we are on track to hit by November 1st obviously is part of a larger pool of 3 to 4 million loans we have to reach under the program.

In addition to that, we have added flexibility to Fannie Mae and Freddie Mac to do refinancing; 2.7 million households have refinanced since the announcement of those flexibilities. We have additional funding supporting the capital base, if you will, of Fannie Mae and Freddie Mac to ensure market stability. Treasury and the Federal Reserve's purchases of mortgaged-backed securities are ensuring liquidity in the market. Together with FHA, Fannie and Freddie—Fannie, Freddie, and FHA are providing the only mortgage financing effectively we have in the country today. Without the government initiatives from FHA and support for Fannie Mae and Freddie Mac, we would not see mortgage financing occurring. So there has been an enormous amount of energy focused on intervention in the home finance system to give people a way of staying in their homes, of refinancing, of having affordability.

We can do better. We can do more. We need to do more. But let us broaden the lens a little bit.

Mr. HIMES. Thank you. I appreciate the observation, and I know much is being done.

But, again, I just wanted to report back on what I heard in 5 weeks in the district and just remind all of us that many of these institutions—and I applaud the work that was done by everyone in the government to really push the banks over the course of July to really accelerate this. And, of course, this is not simple. We don't want to push the banks into doing imprudent things. But I come back to the fundamental truth that many of these banks that perhaps haven't acted quite as fast as we would like them to act exist solely due to the munificence of the American taxpayer. So I would just urge you to keep steeling the spine with respect to really urging them to, when prudent, to just act as fast as possible to alleviate the very real pain that my constituents are feeling. So thank you for your efforts.

Madam Chairwoman, I yield back the balance of my time.

Chairwoman WATERS. Thank you very much.

Mr. Clay.

Mr. CLAY. Thank you so much, Madam Chairwoman.

Thank you both for being here today.

According to your testimony, Mr. Barr, the Treasury asked Freddie Mac to devise a second-look process beginning on August 3rd in which Freddie Mac will audit a sample of MHA modification applications. How will the Treasury ensure that the sample is a cross-representation of actual borrowers seeking MHA modifications?

Mr. BARR. We have asked Freddie Mac to do a sample audit not only of the denied borrowers but also of the eligible pool at each institution, and Freddie Mac in the first instance will be doing that analysis. That analysis will be made available to us. We will be checking it. We will be ensuring that it is appropriately designed, and we will be gathering the information they provide to us to help us inform our relations with individual servicers as well as to spot program design flaws that we need to correct.

Mr. CLAY. Just describe for us the provisions of the second-look process. What does it test for and how and what documents are required to be submitted?

Mr. BARR. The second-look process is designed to determine whether any of two things happen: whether, first, a borrower who was eligible was inappropriately denied a modification; or second, that a pool of borrowers who ought to have been brought into the modification system for a look aren't even being looked at. And in both instances, the question is, given the characteristics of the borrower and the loan, why were they denied or not looked at? If there are individual servicer problems, those will be addressed in an individual servicer level corrected at that level; and if there is a systematic problem, we can bring it into improved program design overall. So we will be looking at using the full range of audit tools to make sure that happens.

Mr. CLAY. And are servicers given notice before they are audited? Are they given prior notice and—

Mr. BARR. There are two separate things. There is a second-look process with respect to being sure that borrowers are not inappropriately denied access to a modification. There is an addition to that, a broader compliance effort that Freddie Mac puts in place—has put in place for us that includes both announced and unannounced visits with respect to the servicers.

Mr. CLAY. I see. Thank you for that response.

Mr. Stevens, according to your testimony, Administration officials have detailed plans to take three important steps to improve the program's performance, including public reporting, setting more operational metrics, and developing a second-look review process. Please describe each step and how it will help improve quality control and performance of the program.

Mr. STEVENS. Congressman, the steps that were outlined in my comments were in support of the initiatives that Mr. Barr has already spoken about. It is the same second-look process. The reporting is the report that—actually, a copy was issued today that was released, and it is the scorecard that is used.

Mr. CLAY. How will these steps further incent servicers to perform better? How do you think—

Mr. STEVENS. I think it's having a direct impact. The meeting that was held some weeks back in Washington with all the servicers that both Mr. Barr and I attended and some people who will be on the next panel attended as well, it clearly highlighted the impact of those that had first applied the modification terms in their operations against those that hadn't. Best practices were discussed, a clear understanding that there would be a strong inspection process and expectations about hitting this goal. There was consensus in the room at the end of the meeting that, if there are no more issues on the table, everybody is on board to move these things forward.

And I will tell you, for some of the larger servicers which will impact the numbers, while they may have been slow to build up their operations, I believe and I hold these senior executives who have spoken to us and I hold them at their integrity in their communication to us even in recent meetings this past week, that they are ramping up and they are aggressively concerned about the report card showing them in a worse light than their peer.

So I think from an intended effect for the scorecard—Mr. Barr may have some additional comments—I think it is having, at least at this point, a desired impact. And there is a lot more detail about who came on first, the processes they used, some of the issues involved. But I think at the end of the day this kind of scorecard really helps benchmark servicer against servicer, and nobody wants to be a low performer on that scorecard.

Mr. CLAY. I see.

Thank you, Madam Chairwoman. I yield back.

Chairwoman WATERS. We have no more members who wish to raise questions of this panel, so I would like to dismiss this panel, and we will reserve the right to ask further questions in writing.

We will now call on the second panel.

Mr. BARR. Thank you very much.

Mr. STEVENS. Thank you.

Chairwoman WATERS. Our first witness will be Mr. Mark Calabria, director of financial regulation studies, the Cato Institute. Our second witness will be Ms. Mary Coffin, executive vice president, Wells Fargo Home Mortgage Servicing. Our third witness will be Ms. Alys Cohen, staff attorney, National Consumer Law Center. Our fourth witness will be Mr. Jack Schakett, mortgage executive, credit loss mitigation strategies, Bank of America. Our fifth witness will be Ms. Molly Sheehan, senior vice president, Chase Home Lending, JPMorgan Chase. And our sixth witness will be Mr. Paul Willen, senior economist and policy advisor, Federal Reserve Bank of Boston.

Without objection, your written statements will be made a part of the record. You will now be recognized for a 5-minute summary of your testimony.

We will start with our first witness, Dr. Mark Calabria.

STATEMENT OF MARK A. CALABRIA, DIRECTOR, FINANCIAL REGULATION STUDIES, CATO INSTITUTE

Mr. CALABRIA. Thank you, Chairwoman Waters, Ranking Member Capito, and distinguished members of the subcommittee. I thank you for the invitation to appear at today's important hearing. I am Mark Calabria, director of financial regulation studies at Cato.

My testimony today will address two specific questions, the first of which is, why have the current Administration and the previous Administration efforts along with those of the mortgage industry to reduce foreclosures had so little impact on the overall foreclosure numbers? My second question that I am going to try to answer is, given what we know about the first question, what policy options should we look at? What policy options do we have?

My short answers to the first question of why previous efforts have not worked well is that these efforts have largely misdiagnosed the causes of mortgage defaults. An implicit assumption behind the HOPE NOW program, behind FDIC's IndyMac model, and behind the current Administration efforts is that the current wave of foreclosures is almost exclusively the result of predatory lending practices and exploding adjustable rate mortgages where payment shocks upon the reset caused mortgage payments to become unaffordable.

The simple truth is that the vast majority of mortgage defaults are being driven by the same factors that have always driven mortgage defaults, generally a negative equity position on the part of the homeowner coupled with a life event that results in substantial shock to their income, most often a job loss or reduction in earnings. Until both of these components—negative equity and negative income shock—are addressed, foreclosure rates will remain at highly elevated levels.

If payment shock alone were the dominant driver of defaults, then we would observe most defaults occurring around the time of reset, specifically just after the reset. Yet this is not what has been observed. Of loans with reset features that have defaulted, the vast majority of defaults have occurred long before the reset.

Additionally, if payment shock were the driver of default, the fixed rate mortgages without any payment shock would display default patterns significantly below those of adjustable rate mortgages. When one controls for homeowner equity, credit score, and other characteristics, the differences in these mortgage products largely disappear. This high level of foreclosures—

Chairwoman WATERS. Will you speak a little bit slower so we can keep up with you?

Mr. CALABRIA. Yes.

Chairwoman WATERS. Thank you.

Mr. CALABRIA. This high level of foreclosures has understandably left all of us frustrated and looking for answers.

To be effective, I think these answers have to be grounded in solid analysis. So I would suggest, first of all, that the Administration, Congress via GAO, CBO, should present detailed estimates of how many foreclosures are driven by what causes, and how many of those foreclosures can be reasonably avoided.

I would say I am not sure if we could measure the success of a program without having a baseline for what that success should be. And currently, whatever the number of modifications that are occurring, it is very hard to tell whether that is anywhere near the right level of modifications.

I also want to note, before discussing specific policy suggestions, we should keep in mind that approximately 50 percent of foreclosures are currently driven by job loss. So I would say the most significant way we could reduce foreclosures is to foster an environment that is conducive to private sector creation.

I think it is also important, in addition to focusing on owners currently in foreclosure, to reach families before they fall behind. For instance, about 4 million of the jobs that have been lost since the start of the recession have been in mass layoffs. These represent a double shock to the household. Because you not only have a job loss, you also have a shock to the housing market because a major employer is downsizing.

But as damaging as mass layoffs can be, they do have an advantage. We know about them ahead of time. The Department of Labor collects data on mass layoffs. Workers get notice. But despite the strong connection between mass layoffs and foreclosures, there is very little coordination between the Department of Labor and HUD.

One of the things we can do and should do is, when you know there is going to be a factory closing in a town and you know the last date that the workers are there, you can get counselors in there because you know that some significant percentage of these workers are going to have problems within the next 6 to 8 months. Yet there is very little of that done. So I would greatly encourage the pushing of appropriated dollars already on housing counseling funds toward factories and workers experiencing mass layoffs.

I think we could also look at encouraging bank regulators to give lenders more flexibility to lease out foreclosed homes to their current residents. Typically, banks come under considerable pressure from the regulators not to engage in long-term property leasing or management as these activities are not considered a core function of banks. So in addition to many owners who may wish to stay in their home as renters, we know that approximately 20 percent of foreclosures are occurring on renter-occupied properties. So, in many cases, if these renters want to continue to pay their rent and we allow them to actually stay and there are many banks that may prefer to keep them as renters and keep that income stream going rather than to proceed to a foreclosure sale.

I would also stress that I think we need to focus our resources on those households most in need, those households who, but for some intervention, will lose their home. And I make this point to say that, broadly, lots of our programs—for instance, the GSE refinance programs—are aimed at households who are not facing foreclosure but simply cannot refinance due to being underwater on their mortgages. We should be downsizing those programs because they draw off important resources that are limited both to servicers and lenders. So we have spent a lot in terms of the programs focusing on low-hanging fruit rather than putting our resources on those most in need.

Wrapping up, I will conclude with my previous observation that the current foreclosure efforts haven't been successful because they have misdiagnosed the problem. We need to focus on negative equity. We need to focus on some sort of income shocks via job loss to households. Until we deal with those, we will both see very high levels of foreclosures going forward.

Thank you.

[The prepared statement of Mr. Calabria can be found on page 63 of the appendix.]

Chairwoman WATERS. Thank you very much.

Ms. Coffin.

STATEMENT OF MARY COFFIN, EXECUTIVE VICE PRESIDENT, WELLS FARGO HOME MORTGAGE SERVICING

Ms. COFFIN. Chairwoman Waters, Ranking Member Capito, and members of the subcommittee, I am Mary Coffin, head of Wells Fargo Home Servicing.

Thank you for the opportunity to come before this subcommittee today to discuss our continued commitment to doing everything we can to prevent avoidable foreclosures and to help stabilize the housing market. Wells Fargo may be a big corporation, but we operate with the conscience of a company determined to do what is right for our customers, our investors, and the American taxpayers.

Since we last came before this subcommittee, much has changed and evolved in our economy and our efforts to assist struggling borrowers.

First, we worked hard to implement the very detailed and evolving home affordable modification programs, which include different guidelines and requirements for Fannie, Freddie, nonGSEs, and most recently FHA borrowers.

To handle the greater than 200 percent increase in borrowers requesting assistance, including the 35 to 40 percent who are current on their mortgages, we have hired and trained an additional 4,600 U.S.-based home retention staff for a total of more than 12,000.

As of September 3rd, we have qualified more than 304,000 customers for trial and completed modifications this year alone. As it pertains specifically to HAMP, we have offered 78,000 customers a trial modification and we have received at least the first payment for approximately 44,000 of these trial starts.

We have further enhanced our support systems, our training, and our retraining to aid our service representatives in appropriately communicating modification programs and guidelines as they continue to change and expand to help more borrowers.

In addition, we have improved the ways we obtain from borrowers the extensive documentation the government requires for its programs, and we continue to work to ensure all documents are processed in a timely manner.

To this point, we have asked the Treasury to meet with us tomorrow to discuss challenges with the Home Affordable Modification Programs and opportunities to make them even more effective.

And most importantly, in this dynamic environment we continue to conduct final reviews to ensure every option is exhausted before a property moves to foreclosure sale. Because when a foreclosure happens, everyone loses.

Wells Fargo has long adhered to responsible lending and servicing principles that guide our business practices. We did not make negative amortizing, pay option, adjustable rate mortgages, or subprime stated income loans, despite their popularity; and, as a result, we can directly attest to the fact that the home loans our company originated perform better than those loans we service but had no involvement in originating and/or underwriting.

Despite widespread decreases in home values, more than 92 percent of our customers in our entire servicing portfolio remain current on their mortgage payments. This is the direct result of our customers' efforts and our commitment to responsibly service all the loans in our portfolio, including those formerly owned by Wachovia and loans we service but did not originate.

In addition, our delinquency and foreclosure rates continue to be significantly lower than the industry average and the lowest of the Nation's largest mortgage lenders. And for all of 2008 and 2009 year to date, less than 2 percent of the owner-occupied properties in our servicing portfolio have actually proceeded to foreclosure sale.

These results would not have been achievable without the continued collaborative public and private sector efforts to inform customers of their options and the introduction of the new Home Affordable Modification Programs.

While we are proud to be a part of HAMP's development—it is an important option—but it needs to be acknowledged that HAMP will not help all borrowers in need of payment relief. For the customers who are ineligible for HAMP and where we can reach affordability, we offer customized solutions. During June, July, and August—the same time we fully executed HAMP—more than 83 percent of our customized modifications reduced payments.

Wells Fargo is a company committed to doing what is right for our customers; and, to that end, I have personally spoken to many of our borrowers to better understand their situations and the experiences they are having with Wells Fargo. These discussions have reinforced for me how many Americans are struggling with changes in their personal and financial services including unemployment and underemployment.

I have also learned how much they are struggling with the various program requirements and documentation. And in the past 6 months, some customers have been challenged with getting clear, timely communication from us as the guidelines and the requirements for the various programs have continued to change.

We hold ourselves to a high level of accountability for improving communication and returning all of our customers to the level of service they deserve. As servicers, we sit between the customer and investor, and we are responsible for doing modifications the right way. We also have a responsibility to execute these programs well for all American taxpayers by ensuring that customers given modifications are truly facing hardships and that they can afford and sustain their home payments after the modification is completed.

In closing, as we have from the very beginning of this crisis, Wells Fargo will continue to seek innovative ways to address the evolving challenges facing our Nation.

Thank you, and I look forward to your questions.

[The prepared statement of Ms. Coffin can be found on page 69 of the appendix.]

Chairwoman WATERS. Thank you very much.

Ms. Cohen.

STATEMENT OF ALYS COHEN, STAFF ATTORNEY, NATIONAL CONSUMER LAW CENTER

Ms. COHEN. Chairwoman Waters, Ranking Member Capito, and members of the subcommittee, thank you for inviting me to testify today regarding the Making Home Affordable Program and its effect on foreclosures.

I am a staff attorney at the National Consumer Law Center. In my work at NCLC, I provide training and technical assistance to attorneys across the country representing homeowners facing foreclosure. I testify here today on behalf of NCLC's low-income clients and on behalf of the National Association of Consumer Advocates.

For the last few months, I have been working with colleagues at NCLC and other organizations to promote large-scale solutions to the foreclosure crisis. During that time, the pleas for help from advocates on the field on the front lines of saving homes have escalated both in number and in urgency.

When the HAMP program was announced by the Administration on March 4th, hopes were high that homeowners would finally have the means to prevent foreclosures. Unfortunately, that reality has not materialized. In fact, what we increasingly hear is HAMP is not the core tool it should be for saving homes. In general, advocates find that HAMP loan modifications are hard to get at all and when obtained often are not compliant with program rules.

Reports from the field indicate that the three servicers testifying today, among others, have serious HAMP compliance problems. Moreover, even if HAMP operated at its full capacity as envisioned by Treasury officials, HAMP's loan modifications lack the mandated principal reductions that many believe are necessary to stem the foreclosure tide.

With cure rates at historic lows, more and better loan modifications are needed to turn around the crisis. HAMP will at best reduce foreclosures by one-third. It is unlikely to shrink the foreclosure numbers to pre-crisis levels.

Problems with HAMP fall into two main categories: implementation; and design. Participating servicers violate HAMP guidelines by requiring borrowers to waive legal rights, requiring downpayments or other prerequisites to HAMP review, and by steering borrowers away from HAMP into other loan modifications that are less advantageous. Moreover, servicers are routinely placing homeowners in foreclosure or proceeding to a sale without reviewing the homeowner for HAMP.

The design of the program hampers homeowners' ability to hold servicers accountable and to obtain sustainable modifications. The net present value test, which is the primary basis upon which a modification is granted or denied, is not available to the public. Homeowners have no ability to question whether a servicer's analysis is based on accurate information.

While homeowners are seeking modifications, servicers often continue the foreclosure process, and pursuing both tracks means that servicers have little incentive to prioritize modifications and homeowners face increased fees that are then capitalized into any eventual loan modification.

While homeowners in bankruptcy technically are eligible for the program, the fact that servicers have discretion about whether to offer modifications to these homeowners has resulted in almost total removal of this option.

The lack of mandated principal reductions under HAMP raises questions about the long-term sustainability of the modifications. Homeowners who could normally refinance their way out of a lost job or sell their home in the face of foreclosure are denied both options when they owe more on their home than it is worth. Without principal reduction, homeowners who lose their jobs, have a death in the family, or otherwise experience a drop in income are more likely to experience redefault and foreclosure.

Creating affordable and sustainable loan modifications for distressed homeowners is labor intensive. It is no surprise, then, that servicers continue to push homeowners away from HAMP modifications or delay the process substantially.

In addition, servicers' profit is directly linked to the principal of mortgages they service and the timing for writing down loans. Both motivate servicers away from offering principal reductions. Moreover, advances paid by servicers are more easily recovered after a foreclosure rather than a loan modification, tipping the scales away from modification.

While initial loan modification numbers are up, compliance with HAMP by all reports is still quite spotty, and many people who appear to be qualified are not getting a chance to receive the only type of help that may save their homes.

Congress should pass legislation requiring loan modification offers to qualified homeowners where such modifications are more profitable to investors than foreclosure. It also should consider further reforms to the servicing industry. Loss mitigation in general should be preferred over foreclosure; and, as the chairman noted, that is needed for homeowners with loans they never could afford and for those facing job loss.

H.R. 3451, recently introduced by Chairwoman Waters, reflects these basic goals of prioritizing loss mitigation, saving homes through loan modifications, and reforming how servicers do business.

Congress also should adopt court-supervised mortgage loan modifications which would sidestep many of the structural barriers in the servicing industry that today are preventing mass loan modifications from occurring.

Congress also should support mediation through funding and the establishment of standards. Congress soon should recognize that voluntary measures on their own by entities that profit from homeowner default even with incentives will not lead us out of this crisis.

Thank you for the opportunity to testify before the subcommittee today. We look forward to working with you to address the challenges that face our Nation's communities.

[The prepared statement of Ms. Cohen can be found on page 79 of the appendix.]

Chairwoman WATERS. Thank you very much.
Mr. Schakett.

STATEMENT OF JACK SCHAKETT, MORTGAGE EXECUTIVE, CREDIT LOSS MITIGATION STRATEGIES, BANK OF AMERICA

Mr. SCHAKETT. Madam Chairwoman, Ranking Member Capito, and members of the subcommittee, thank you for the opportunity to update you on Bank of America's efforts to help responsible homeowners stay in their homes.

I am Jack Schakett, credit loss mitigation strategies executive. I report to home loans president, Barbara Desoer, and have responsibility for foreclosure prevention programs for our mortgage servicing portfolio of nearly 14 million loans.

As the country's largest servicer, we are a major partner in the Administration's Home Affordable Modification Program and understand the responsibilities that come with that. We are committed to helping the Administration achieve its goal of 500,000 trial modifications by November 1st. Bank of America is working to transition 125,000 at-risk loans into trial modifications as a part of that goal. As a demonstration of our growing momentum, in August, we doubled the number of trial modifications that have been started.

Throughout this historic downturn, Bank of America has extended credit to drive economic growth and worked to develop financial solutions for our customers. For example, we are one of the first lenders to leverage the Administration's refinance program; and, to date, we have completed refinancing of the program to more than 74,000 homeowners. Before HAMP, we were one of the first to implement a national homeownership retention program.

Through our national program and through other efforts, Bank of America completed loan modifications for approximately 170,000 customers from January to July of 2009, compared with 230,000 modifications for all of 2008. We are now working hard to help ensure HAMP's success and have established a sizable infrastructure to handle customer demand and program details. Significant resources have been devoted to this effort, including expanding our default staff to more than 11,000, a 55 percent increase since the beginning of the year.

The HAMP program is now the first loan modification solution we consider in our home retention efforts. For our customers who do not qualify for HAMP, they still benefit from the availability of multiple programs that Bank of America continues to offer.

Our recent results reflect our conversion to HAMP as the centerpiece of our home retention efforts. As previously noted, we have doubled the number of customers with the trial modification in 1 month from approximately 28,000 in July to more than 68,000 through the end of August. In that same period, we have also increased the number of offers extended under HAMP to more than 135,000.

Importantly, as we ramped up, we placed on hold any foreclosure sale for borrowers who may be eligible for HAMP. Those holds remain in place during the time that it takes us to both contact and evaluate the borrower and throughout the trial modification period.

With that said, we continue to critically look at our own loan modification process. Three areas of particular focus: One, how can we make the process more customer friendly and responsive? Two, how can we more efficiently handle customer documentation? And, three, how can we keep customers better informed throughout the process?

In addition, there are other challenges we continue to confront in our efforts to help as many homeowners as possible realize the benefits of HAMP. Two of the most significant hurdles are our customers not providing required information and a lack of a borrowers' responsiveness to our outreach efforts.

In an effort to improve our outreach and close this gap, we have ramped up activity through traditional avenues such as mail, telephone, and participation in community events. Since January, we have participated in more than 167 community events.

We have also partnered with three national nonprofits in the creation of the Alliance for Stabilizing Communities. We have provided $2.5 million in support for this national coalition and their work to hold 40 housing rescue fairs over the next 2 years in 24 communities hardest hit by the foreclosure crisis.

Regrettably, there are limits to what the current programs can achieve. Unemployment, lack of interest in remaining in the property, and other eligibility issues are current impediments for qualifying for HAMP modification. With unemployment still near 10 percent, even the most ambitious long-term modification program will not be able to assist borrowers who have no ability to make a reasonable mortgage payment. To address this, we began exploring with the Administration methods for allowing us to responsibly offer current unemployed borrowers a temporary solution to stay in their homes, followed with a long-term solution after they obtain a job.

My written statement provides further details on the opportunities we still have to improve the effectiveness of the program.

The entire mortgage servicing industry is racing against the clock to stem the tide of foreclosures and home loss. We fully understand the urgency and will never be satisfied that we have done enough until the country is through this difficult cycle. I am certain my colleagues agree with this statement.

Strong focus from the Administration has added substantially to our collective abilities to assist homeowners. Yet we understand we have a long way to go under these very challenging circumstances. We look forward to continuing to work with Congress and the Administration on these important issues.

I would be happy to answer any questions you have.

[The prepared statement of Mr. Schakett can be found on page 148 of the appendix.]

Chairwoman WATERS. Thank you very much.

Ms. Sheehan.

STATEMENT OF MOLLY SHEEHAN, SENIOR VICE PRESIDENT, CHASE HOME LENDING, JPMORGAN CHASE

Ms. SHEEHAN. Chairwoman Waters, Ranking Member Capito, and members of the Subcommittee on Housing and Community Opportunity, we appreciate the opportunity to appear before you today on this most important topic of helping homeowners. We recognize that no one benefits in a foreclosure.

My name is Molly Sheehan. I work for the Home Lending Division of JPMorgan Chase as the executive responsible for housing policy. Chase is one of the largest residential mortgage servicers in the United States, serving more than 10 million customers located in every State of the country with mortgage and home equity loans totaling about $1.4 trillion that we service. We are proud to be part of one of this country's preeminent financial institutions with a heritage of over 200 years.

At Chase, we are investing in new business initiatives, people, and technology to help families meet their mortgage obligations. Since 2007, we have developed and expanded our comprehensive program to keep families in their homes, which has helped prevent over 730,000 foreclosures.

We have also been working hard to help borrowers through the Federal Government's loan modification program. From April 6th, when Chase began processing trial modifications through the MHA program, through August 31, 2009, Chase has approved over 144,000 MHA trial mortgage modifications. Of these trial plans offered, 113,000 are currently active as of August 31st and borrowers are making their trial plan payments.

Together with over 88,000 additional Chase loan modifications, over 230,000 struggling Chase, WaMu, and EMC customers have received approved trial modifications through August 31, 2009. Another 125,000 applications are currently being reviewed to see if they can be modified consistent with these program terms.

We have been able to reach this large number of borrowers by creating many avenues of communication. This year alone, we have opened 27 Chase homeownership centers in 11 States. To date, more than 42,000 borrowers have met with trained counselors at the centers. These centers have also mailed over 538,000 invitations to Chase customers to come discuss their situation with our counselors.

We have hosted more than 120 homeowner events to educate and inform homeowners about the loan modification process in just the past 6 months.

We have created a dedicated Web site with information about our programs where borrowers and counselors can download the documents needed to apply for a modification. In the last 6 months, there have been more than 2.7 million visits to Chase's Web site.

We rolled out a dedicated customer hotline for modification inquiries that has handled almost 1.3 million calls as of August 31, 2009.

In addition to reaching out to borrowers, we have made a number of investments in our systems and personnel to improve the loan modification process. We have added 1,700 loan counselors and 3,700 mortgage operations employees as well as created additional training for our staff, nonprofit counseling partners, and borrowers attending HOPE NOW outreach events, reaching hundreds of internal and external loan counselors and borrowers.

We estimate that, as of August 31st, Chase is servicing approximately 417,000 loans that are potentially eligible for modification under the MHA program guidelines. Of this eligible population, 33 percent to date have been offered a trial plan as of the end of this month.

However, much of the responsibility to complete the loan modification process does rest with borrowers. After being granted relief through a trial modification, borrowers must document income, hardship, debts, and other important information to enable underwriters to complete final loan modification offers that conform to MHA guidelines.

Chase's policy is to stop foreclosure sales while reviewing a mortgage for loan modification and other foreclosure prevention steps. If a loan does not qualify for an MHA loan modification, we next look to a Chase modification. If these alternatives do not produce a sustainable modification, the loan is referred to loss mitigation for other types of foreclosure prevention techniques that are more traditional such as short sale and deed in lieu.

I would be happy to discuss these alternatives as well as Chase's own loan modification programs with the subcommittee in more detail during the question and answer period.

We are pleased to have this opportunity to be with you today. Thank you for your attention. I will be happy to answer any questions you may have.

[The prepared statement of Ms. Sheehan can be found on page 152 of the appendix.]

Chairwoman WATERS. Thank you.

Mr. Willen.

STATEMENT OF PAUL S. WILLEN, SENIOR ECONOMIST AND POLICY ADVISOR, FEDERAL RESERVE BANK OF BOSTON

Mr. WILLEN. Chairwoman Waters, Ranking Member Capito, and members of the committee, thank you for your invitation to testify.

My name is Paul Willen, and I am a senior economist and policy advisor at the Federal Reserve Bank of Boston. I come to you today, however, as a researcher and as a concerned citizen and not as a representative of the Boston Fed, the other Reserve Banks, or of the Board of Governors.

Over the last 2 years, we have searched for policies to help troubled borrowers avoid foreclosure. In New England, we at the Boston Fed have worked with banks to set up a lending facility to help subprime borrowers refinance into prime mortgages. We brought borrowers and servicers together in large-scale foreclosure prevention events that have served as a national model. In the research department, we have gathered and analyzed detailed loan level data to help us evaluate policies to ameliorate the effects of the crisis on our communities and on the country.

In my remarks today I would like to focus on three aspects of the foreclosure crisis relevant to foreclosure prevention plans.

The first is that an effective plan must address the problem of unemployed borrowers. Long-term loan modifications that yield affordable payments for borrowers but also provide attractive payment streams to lenders will help some but cannot help unemployed borrowers. Thirty-one percent of an unemployed person's income is often 31 percent of nothing, and a payment of zero will never be attractive to a lender.

This is important because our research shows that, contrary to popular belief, unemployment and other life events such as illness and divorce, much more than problematic mortgages, have been at the heart of this crisis all along, even before the collapse of the labor market in the fall of 2008. This may seem counterintuitive. Life events could not explain the surge in defaults in 2007 because there was no underlying surge in unemployment or illness that year, but that view reflects a misunderstanding of the interaction of house price depreciation and life events in causing default.

When prices are rising and borrowers have positive equity, detrimental life events lead to profitable sales. But when prices are falling and borrowers cannot pay off their mortgages with the proceeds of a sale, those life events lead to foreclosures. Thus, we did not need to see a surge in life events to get a surge in foreclosures but, rather, a fall in house prices, which is exactly what we saw.

The second policy related finding from our research is that it is unlikely that a modest financial nudge to servicers will lead to millions of modifications that will help millions of worthy borrowers. In a recent paper, we showed that in the period 2005 to 2008, lenders gave payment-reducing modifications to only 3 percent of seriously delinquent borrowers. In addition, we show that this did not result from contractual issues related to securitization. Lenders were just as reluctant to modify loans when they owned them as when they serviced them for securitization trusts.

We argued that the main reason we see so few modifications is that it simply isn't profitable for lenders. Modification benefits lenders because it helps to avoid the high costs associated with foreclosure, but redefault risk, the possibility that the borrower who receives the modification will default again, and self-cure risk, the possibility the borrower would have repaid the loan without any assistance from the lender, can wipe out these benefits.

The role of self-cure here is key. About a third of the borrowers in our large sample are current on their mortgages or prepay a year after they become 60 days delinquent. An investor would view assistance given to such a borrower as wasted money.

A third result from our research is that policymakers need to exercise care in designing foreclosure prevention policies that provide the right incentives for borrowers and servicers. A program that offers a monetary incentive to do as many modifications as possible and to minimize the probability that modified loans redefault may not in fact prevent many foreclosures. To see why, one must realize that the easiest way to ensure that a borrower doesn't redefault is to choose a borrower who was unlikely to default in the first place. Thus, a servicer could make minor modifications to millions of loans to perfectly credit-worthy borrowers, collect large sums from the government, and then collect even more as the borrowers continue to repay the loan.

Taking these research results into account, we believe that the most effective use of government money for foreclosure prevention would involve direct assistance to borrowers rather than to servicers. Two recent proposals, one authored by a group of Federal Reserve economists, including me, and the other by researchers at the University Wisconsin, target the unemployed to help them cover their housing expenses until they get their feet back on the ground. Either plan would prevent large numbers of foreclosures and would be a good starting point for an effective foreclosure relief plan.

We hope that these findings add perhaps unexpected insights to your work as policymakers and thank you again for the opportunity to appear before you today. I would, of course, be happy to address any questions you have.

[The prepared statement of Mr. Willen can be found on page 165 of the appendix.]

Chairwoman WATERS. Thank you all very much for being here today.

I will recognize myself for 5 minutes for questions.

Let me just precede my questions with a statement about the concern that all the members basically have about what appears to be a lack of substantial loan modifications and a lot of unrest by homeowners who are desperately seeking loan modifications.

Now, we all recognize that many of these homeowners have been laid off, they may have lost their jobs, and they don't have the kind of income that could assist in getting a loan modification. What I have found is, if the income appears to be too low, that there is just no way for them to get help. I am told—and it was basically stated earlier by the Assistant Secretary—that some servicers are finding ways or have found ways to help homeowners who have lost their jobs, have been laid off and have regular debt and have some income through unemployment, very little, but that income does not appear to be adequate to service a mortgage. Which of you have programs to help those who are unemployed?

Ms. COFFIN. We do.

Chairwoman WATERS. Wells Fargo. Ms.—

Ms. COFFIN. Coffin. I am with Wells.

Chairwoman WATERS. Wells Fargo, Ms. Coffin, what do you do with someone who is unemployed, has been in a home for 10 or 15 years, they want to keep their home and maybe need a few months before they can find another job? How do you help them?

Ms. COFFIN. We help them with the forbearance plan that was referred to earlier.

Chairwoman WATERS. How does it work?

Ms. COFFIN. What happens is the borrower tells us I am about to be unemployed. They come to us sometimes when they are current and want to protect their credit, also.

Chairwoman WATERS. I am sorry?

Ms. COFFIN. Sometimes it is borrowers who are still current and know that they have lost their job and can you help me? You put them on a forbearance plan, and you may set it up for 6 months. Say we will give you a period of time where you don't have to make your payments while you are looking for and establishing income again. And then at the end of that period and throughout that we will communicate and work with them; and if they do establish income, then we have to work with them to provide help with those payments that were missed during that period. And we can do that by capitalizing them onto the loan, spreading them over a longer period of time.

I would suggest that all of us here and probably other servicers, one of the things that we will speak to the Treasury about tomorrow when we meet with them is actually an enhancement to the HAMP which is a short-term modification. Because what we believe borrowers do need once they reestablish a job, they need longer-term help in getting past that period where they could not make their payments; and by a short-term mod, we could actually provide a 12-to-24-month period of a modification to a loan that then would step back up.

Chairwoman WATERS. That's admirable. In helping my constituents, I have not found that to be true. I can't sit here and say that I have not found it to be true of Wells Fargo, because I have worked on so many different ones, but we have a long list in our office mostly fitting that description of people who have lost their jobs.

One of the things we did find with loan modifications in general was the late fees and lawyer fees that are attached to loan modifications for those who find themselves 6 months behind, some of them behind many months, and when they finally get in touch and they finally get to work then they are confronted with late fees and lawyer fees and some other fees that are attached onto the loan, which increases the amount of the modified loan. How do you handle that?

How do you handle that? Let me just ask Mr. Schakett from Bank of America.

Mr. SCHAKETT. Yes. On the temporary forbearance plan, I just want to maybe follow up on that also, because I do think the industry—everybody has in their tool kit a temporary forbearance for the unemployed. But as far as how it is employed and how formalized it is and how consistently it is used, I think there is much need of improvement in that area.

Just like we were before MHA came out for modifications, there were a lot of inconsistencies on what person qualified, and I think we ourselves at Bank of America are reassessing exactly how to formalize that program to make it easier for our counselors to know whom to offer it to. And we would target the customers who had a good pay history in the past, had a reasonable debt-to-income ratio before the hardship and for customers who actually showed they could handle their back-end debt.

So, again, a conservative program that knows exactly who we could offer it to and who we couldn't I think will improve the situation where, for the unemployed borrowers; and as well, as Mary mentioned, we are going to work with the Administration to try to develop a program where they may be able to assist in the process also.

So I can understand your concerns, that you probably hear a lot of times we aren't helping those customers enough; and I think it is because we really haven't formalized the process enough to actually make sure we offer it consistently from customer to customer. So that is an improvement needed.

The question that you asked about late fees and other—lawyer fees, etc., I think everybody's, at this table, policy is to waive all late fees, and there is no charge associated with the actual modification itself.

Chairwoman WATERS. I have not found that to be the case. Does everyone at the table waive late fees?

Ms. SHEEHAN. Yes. And that is a requirement of the MHA program.

Chairwoman WATERS. Well, let me say—since you answered, Ms. Sheehan, from Chase—I have here a statement, a waiver, and it basically says, "JPMorgan Chase Bank, National Association Successor enters to Washington Mutual Bank, has offered to try to qualify you for a modification—an MHA modification under the Making Home Affordable plan announced by the Obama Administration March 4th.

"You have declined to be considered for an MHA modification, opting instead to go forward with the modification offer made by lender to you prior to the March 4th announcement, the prior modification. Had you qualified for MHA modification, you may have been entitled to the following."

And you go on and talk about what they may have qualified for.

"By signing below, you acknowledge that you have been advised and understand the above features."

What is this all about?

Ms. SHEEHAN. That was a form that was developed at the time. Prior to the implementation or announcement even of MHA, Chase had rolled out a significant enhancement to its own loan modification efforts. We were in the process of communicating and qualifying many, many borrowers for the Chase modification program at the time of the MHA announcement on March 4th.

At that point in time, we had numerous borrowers who had actually been approved to close on a Chase modification, but we wanted to make sure before they made that decision that they were informed that the government program had been announced, but the details were not yet out.

So that was really a disclosure form that was designed to advise them that they had the option to wait for MHA to become available and to go through a trial process, but if they chose to go forward with the Chase mod, they could do that.

So it really was a form of disclosure. It does not mean that anyone who received a Chase modification waived any right in the future to a HAMP modification. I have heard that statement made; it is incorrect. If they found their Chase modification was not sustainable, they would still be eligible then to come back to us for a HAMP modification.

Chairwoman WATERS. Thank you very much.

Mrs. Capito.

Mrs. CAPITO. Thank you. I would like to clear up—I am hearing two different things here. From Ms. Coffin, I heard that—excuse me, Ms. Cohen—that while the modifications are going on, the foreclosure clock is ticking at the same time, simultaneously.

Is that part of what your testimony was?

Ms. COHEN. Yes.

Mrs. CAPITO. But then I thought I heard from some of the other servicers that is not the case. Could you clarify that for me?

Mr. Schakett, could we start with you?

Mr. SCHAKETT. I think you heard in my testimony that we have customers on foreclosure hold. I think the difference is a distinction of the process versus the sale.

Every customer that we are working—any kind of workout process we put on foreclosure hold. So that means that we will not have a foreclosure sale until we complete the process. It does not mean that we don't actually continue to go through a process of foreclosure.

For instance, we could have a customer that part of the process of foreclosure is to file a notice of default. We would still file that notice of default. So the customer starts seeing activity toward a foreclosure at the same time they are working on modifications, but we assure that no customer actually gets foreclosed on.

So you kind of see a process of foreclosure going, you can, simultaneously with the modification, but then no customer actually gets foreclosed on. That is the absolute hold to make sure that we have a chance to complete the modification first.

Mrs. CAPITO. So could there be a scenario where you are turned down for the loan modification, and within a short period of time, your property is up for sale in the foreclosure?

Mr. SCHAKETT. Yes. By giving them all the normal required notices in the foreclosure process, they would realize kind of what the dates are coming up, what the date of eviction is, what the date of the actual foreclosure sale is. So they would be aware of those dates and they would be aware, if the modification didn't complete, that they would live by those dates unless there was a reason to extend those dates.

Mrs. CAPITO. So I guess, better said would be, rather than you are holding on foreclosure, you are actually holding on foreclosure sale; you are not really holding on the process.

Mr. SCHAKETT. That is right. We are holding on foreclosure sale.

Ms. COHEN. May I respond to that?

Mrs. CAPITO. Sure.

Ms. COHEN. So there are two issues. One issue is whether the sales are proceeding and the other issue is whether the foreclosure process is moving forward.

The HAMP program is very clear that sales should not proceed, and we are getting calls from all over the country that the sales are proceeding anyway from all kinds of servicers around the country. So that is one compliance problem.

In addition, to the extent that foreclosure processes are going forward, what happens, especially in a judicial foreclosure State, is, the homeowner is incurring greater costs to litigate the foreclosure or to defend the foreclosure in court while they are trying to negotiate a loan modification.

There are two problems there. One is, it is easier for the servicer to just go to foreclosure because they are so close to the sale at that point. For the homeowner, because they have incurred greater costs, those fees are capitalized—and I think Chairwoman Waters was asking about this before—the lawyer fees, the valuation fees, are capitalized into the principal, and the homeowner is less likely to be MPV positive, less likely to qualify for a modification because of those costs.

So both of those are issues.

Mrs. CAPITO. Does anybody have another comment in response? Because what I think you just told me was, if I heard this correctly, the foreclosure lawyer fees and other things are rolled into the loan modification even though the property is not foreclosed on.

Is that what you are saying?

Ms. COHEN. So if you are figuring out how much the person owes and essentially what the outstanding principal balance is, that amount is also owed; and so, if the foreclosure—

Mrs. CAPITO. "That amount" being the foreclosure fees? Is that what you are talking about?

Ms. COHEN. Right. So any amount that the servicer pays the lawyer to pursue the foreclosure is billed to the homeowner and becomes part of the principal that the person has to pay back.

I also have to tell you that attorneys around the country tell me, while they are negotiating loan modifications, their clients routinely receive foreclosure sale notices.

Mrs. CAPITO. I would imagine that is something in the previous panel, when they set up their protocols for transparency and accountability, should be something that would come forth with a report on that.

So that is something we need to look at.

Ms. COFFIN. And let's make sure this is really clear. In the Making Home Affordable program, as you saw today, there are many customers who have been offered the HAMP that have not yet made the first trial payment. As soon as that first trial mod payment is made, that foreclosure proceeding stops. There are no foreclosure proceedings while they are making their trial mods and turning their docs in to us.

Mrs. CAPITO. That is another question I had.

On the trial modification, during that 3-month—it is a 3-month trial period. If you make your payments for 3 months, then you go to, I guess, a confirmed loan modification. During that period, is that when you are still bringing all your documentations? Or are you not documenting all of this pre-, temporary loan modification?

Ms. COFFIN. It depends on which program, because Freddie, Fannie, the government programs all have different guidelines; so you have to pick the particular one.

But in general, yes, you can verbally verify a customer over the phone and get them started to give payment relief to that home immediately through verbal verification of income. So they can start their trial month period. And they have three payments they have to make under that.

During that period, you are collecting documentation and then assessing that the verification of the income matches what you actually receive on the documents that are presented to you. And the completion of the modification at the end is the timely payment of the three payments and also the receipt and the—of the verification of income through the process.

Mrs. CAPITO. Well, it seems to me that one of the reasons we got into this problem is because we didn't have any verification of income or documentation as to debts or any of this if you look at the different loans that were put forward—one of the reasons. Unemployment understandably is probably the major reason right now.

I guess I didn't realize this, and I am kind of—I am not shocked, but I am kind of surprised that financial institutions would enter into a temporary situation without having this documentation. It seems to me that is just as risky.

So it goes back to the question I asked the previous panel: What are we going to find after we get through the trials? How many people actually pass the trials and move on to a major loan modification?

I don't know. That seems uncertain business to me, especially if you look in hindsight as to how some folks were able to purchase a home that maybe was way beyond their reach when they really weren't asked for the documentation.

Now they are back maybe asking for a loan modification. The price has plummeted or at least is less than what they initially purchased it for. And this is going to assume in this economy that they haven't, unless they have been lucky or worked really hard and gotten all the things that are due them, that their income is not going to increase that much over the last 2 or 3 years to be able to sustain this.

I mean, that is just a comment. Obviously, this was designed this way, but I find that rather surprising.

If you are doing your own loan modification within the bank, your other options, are you getting all this documentation before you do this instead of when you are Making Home Affordable modification? Is there a different standard?

Mr. SCHAKETT. I think historically most of the servicers did not have a trial modification built into it and, thus, they required—whatever they required, they required it before the modification was complete. That is a true statement. Clearly, the MHA program does actually have a much higher documentation than traditionally people used for modification.

Obviously, we have taxpayers' money at risk here, so I think the higher documentation standard does make sense. And obviously the trial modification period was a compromise to say, if we want to get them started sooner, you know, that you wanted to trust the customer to go ahead and tell you what they make and start the trial mod period.

So there is some risk. It actually puts the investors in a situation where they could end up having a 2- or 3-month period where the documentation doesn't work, and you have to start the trial mod period over again; or they fall out of the trial mod completely. But it does allow more customers to be helped sooner by the end of the trial modification period and, thus, you do that work during that 3-month period versus doing it before.

Mrs. CAPITO. Thank you.

Chairwoman WATERS. Thank you very much.

Mr. Green.

Mr. GREEN. Thank you, Madam Chairwoman.

Ms. Cohen—let me make sure I am addressing the proper person. Yes, Ms. Cohen.

Ms. Cohen, you were giving us some intelligence on legal fees and perhaps some other fees. Would you restate that again, please? Because I think a point was missed, and I would like to, if I may, underscore it.

Ms. COHEN. Sure. Thank you for your question.

During the foreclosure process, the servicer incurs fees to pursue the foreclosure on behalf of the investor trust, and that includes hiring an attorney generally to pursue the foreclosure, doing valuations of the property periodically. Those fees are paid by the homeowner; they are essentially billed to the homeowner.

If a loan modification happens sometime after those fees have been incurred, the principal of the loan that the homeowner is paying back includes those fees; and it is harder to afford a loan modification if you have racked up a lot of fees. So I have received a lot of concerned inquiries from folks in judicial foreclosure States saying that their homeowners are having a harder time getting modifications because of the amounts that are owed extra because of this process.

Mr. GREEN. Will you kindly give a number? And I know that you may not have empirical evidence to support a number that would be as pervasive and taken as much as we might want, but some indication as to how much these fees can be, please.

Ms. COHEN. I would say thousands of dollars. Maybe not $10,000, but—it might be that the servicers can tell you more about what they charge. But our experience is that it is maybe $5,000.

Mr. GREEN. This is a good segue to the servicers.

First, servicers, do you agree that the fees—for our purposes, let's just call them fees rather than many of the other things that we may. Do you agree that these fees are added on as principal to the buyer?

If you disagree, raise your hand. That will be the person that I will talk to. Let the record reflect that we have no hands. So I will assume that all agree with Ms. Cohen.

Now, if this is true, if we have these additional fees tacked on and if we are now proceeding to restructuring, Ms. Cohen, do we end up restructuring and having payments that are near or about the same as they were before we restructured?

Ms. COHEN. I think it really depends on a lot of factors for any particular individual. One of our concerns is that it makes it harder to afford the modification. If your balance is small, you are a low-income person, you live in a low-income area—

Mr. GREEN. Do this for me. Explain, what does it mean when you say it is harder to afford? What does that mean, harder to afford the loan modification?

Ms. COHEN. The loan modification payments are based on whatever total amount you owe, and so if you—if you are poor and you own your house, and your house is only worth $45,000 and you incur $7,000 extra, and you sort of add that on to the $45,000, your monthly payment has to cover the $45,000 plus the $7,000. And so the monthly payment is greater because the $7,000 was added to the $45,000.

So if you are low income, you don't have a lot of money coming in the door to begin with, and so even $7,000 on a small balance makes a huge difference.

Mr. GREEN. I understand.

Let me—before I come to you, sir, I know that you want to give a comment on this, but I have to go to the doctor from the Cato Institute, and I will come back to you, if I can.

Is it "Calabria?"

Mr. CALABRIA. “Calabria.”

Mr. GREEN. All right. Sir, I have read your paper, and I must tell you that while I may not agree with all that you have contained therein, I think it is well thought through and there is a line of logic that is consistent. I have great appreciation for consistency and logic, and I appreciate the way you dealt with the ARMs and other aspects of what are ostensible causes of the crisis.

But your conclusion is that negative equity and income shock, these are the causes of the current inability to restructure. Is that a fair statement?

Mr. CALABRIA. I would say they are the predominant causes.

Mr. GREEN. Predominant causes. I can read your exact words if you would like me to. You indicate after—well, let me just start with the sentence:

“It is not exploding ARMs or predatory lending that drives the current wave of foreclosures, but negative equity driven by house price declines coupled with adverse income shocks.”

You didn’t use those qualifiers in your statement, but I respect the right that you have to use them now.

So you would now qualify these statements?

Mr. CALABRIA. I would stick predominantly, and I would also add, my emphasis there is on the foreclosures that aren’t being addressed. Most of the things—

Mr. GREEN. Quickly, let me ask you this. You indicate that these two things must be addressed before we can be successful with these various plans.

Is that correct? Do you also make that statement?

Mr. CALABRIA. If you want to see more than just small numbers of marginal success, then I would say yes.

Mr. GREEN. Great.

Now tell me this quickly. How do you address the negative equity?

Mr. CALABRIA. I think that is the—I want to be clear. A diagnosis does not always lead you to very clear treatment.

Mr. GREEN. I understand. But you are with the Cato Institute. You are a brilliant man, and I would respect having you give me an opinion, even though I may not agree with it.

Mr. CALABRIA. Sure.

One of the things that I think is positive in regard to the housing market is I believe we are through most of the depreciation.

Mr. GREEN. My time is already up, so I have to ask you to go straight to negative equity. How would you address negative equity?

Mr. CALABRIA. First of all, my point about the housing market is that I believe we are turning up in the housing market, which gives homeowners some incentives to stay in it.

To deal with negative equity directly in terms of whether you do a payment modification on the part of the owner, I mean, I am not sure necessarily how you deal with negative equity without basically giving the owner equity.

Mr. GREEN. And is it your opinion that what we are attempting to do with this program addresses negative equity?

Mr. CALABRIA. I don't think it does. You are not necessarily putting the owner in a position where they have equity because even most of—

Mr. GREEN. Now I am going to put you in an uncomfortable position, but you can handle it. Do you agree then that if a loan is modified such that negative equity is addressed that there is a greater likelihood that the borrower can pay the loan?

Mr. CALABRIA. Actually, I don't think the negative equity situation has anything to do with the ability of the borrower to pay the loan. It has to do with the incentive of the borrower to stay in the home.

Mr. GREEN. Then the borrower will have a greater incentive to stay in the home. Do you agree?

Mr. CALABRIA. Yes.

Mr. GREEN. But your position is that this program is not getting us there. So now, whether you like it or not, if a person goes into a bankruptcy court and receives a stay which will deal with all these other concerns that have been addressed, you get an automatic stay, any additional efforts to foreclose are stalled and then the loan is modified structurally through the bankruptcy court, wouldn't that give a person a greater incentive to stay in the home?

Mr. CALABRIA. Well, let me start with an observation that if we are talking about, say, a cramdown, to qualify under Chapter 13 you need to come up with a repayment plan, which means you need income, and unemployment insurance doesn't count for that. So it is important to remember that a cramdown would not work for people whose primary problem is unemployment.

Mr. GREEN. Exactly. That is off the table.

Mr. CALABRIA. But even as the cramdown is structured—

Mr. GREEN. Let's not talk about it as structured. Let's talk about a cramdown. I don't like the term "cramdown."

Mr. CALABRIA. A modification.

Mr. GREEN. Okay. A bankruptcy, a bankruptcy that allows restructuring such that a person who can pay—and that is what we are talking about, so that people won't get confused and say that everybody is just going to run in and get bankruptcy and they are going to benefit from it notwithstanding their inability to pay. You made a good point.

Now, given that they can pay, would this give them a greater incentive to make their payments?

Mr. CALABRIA. It all depends on whether—

Mr. GREEN. Well, now, you just said if a person—if the negative equity is dealt with, that would give a person greater incentive to pay.

Mr. CALABRIA. I appreciate that.

My point is that modifications up until now, whether you look at second homes or you look at investment properties, they do not leave the person with equity, they leave them with zero equity, because they cram down the amount of the mortgage to the value of the house, which means you have zero equity. Even under the previous proposals for modification, there is no equity that is given. So I am only basing this off of the other examples that we talked about, modification—

Mr. GREEN. I understand. But if they modify such that there is equity, such that the person can now make the payment, does the person have greater incentives? This is pursuant to what you have in your paper.

Mr. CALABRIA. For the small number of people—

Mr. GREEN. Okay. Any number, is that true?

Mr. CALABRIA. For that—for any number of people who would fall into that category, that would provide them greater incentives, yes.

Mr. GREEN. And my final question to the other folks, if I may—

Chairwoman WATERS. Yes, you may.

Mr. GREEN. My final question to those of you in the modification business, tell me if you agree that allowing bankruptcy will provide a means by which persons—let's assume that they have tried everything that is available without success and they do file for bankruptcy. Would this knowledge that the bankruptcy is an option—would the knowledge of the bankruptcy as an option, not you, but would it help some servicers to realize that maybe I can do a little bit more than I have been doing? And I am trying to be as kind as I can in saying this, because I don't want to create problems for people who are trying to do a job. And you all are.

But let's start with the Bank of America representatives. Would this help some servicers and some investors to see that maybe we do have a little more latitude than we think we have in trying to modify some of these loans? Bank of America?

Mr. SCHAKETT. Well, I really can't speak for kind of all the other servicers. I can only speak for Bank of America. A threat of bankruptcy would not change our policies on modifications to keep companies, people in their homes.

We want—it is in our best interest, our shareholders' best interest, the public's best interest—to do everything we can to make the modifications for the people who are reasonably able and willing. So I don't think the threat of bankruptcy would change our posture at all as far as working out a modification.

Mr. GREEN. My suspicion is that your colleagues would say a similar thing. If anyone would differ in terms of the banks—JP, Austin, if you would differ, raise your hand. If you don't differ, I won't bother to ask you the question.

So nobody differs, no hands up, let the record reflect, which gets to the point I would like to make.

The bank, the servicers, are not going to change. They are going to continue to do what they are doing. And if we know they are going to continue to do what they are doing and we have about 8 million homes that may go into foreclosure within the next 4 years, then we have to do something different. We cannot allow all that we have done to try to revive the economy, to stabilize the economy, to become the sole province of servicers who are not going to change their method of operation.

I respect what you want to do and what you are trying to do, but at some point those of us who are in the arena who have to make these tough calls, we are going to have to make another call and give people another option, just as you have with your second home, your third home, your fourth home, just as you have with your auto payment, just as you have with your farm loan. All of these options are available to people, except the lowly person who can't afford a second home, third home, fourth home, who can't afford a farm, who may not have a fine car to drive, but has something called a primary residence that he or she or they, they are trying to protect. These people need help, too. That is what we have to look at.

I appreciate where you are and I thank each of you. My time has expired.

Thank you, Madam Chairwoman.

Chairwoman WATERS. Thank you very much. Before I dismiss the panel, I would like to just recognize myself to share with you some of the lessons I have learned as I have worked very closely with my staff in learning how to contact servicers, how to work with servicers. I get waivers from my constituents who are trying to seek some help and I get on the telephone with servicers and my constituents and I walk through the process, so I know a lot about it.

I have not yet encountered a situation where the documentation for income and debt was not required on a loan modification, and I am going to take a look at the ones that were not handled that way, and I will be in contact directly with you about them since you have testified a bit differently here today about how you are doing some of that.

The other thing that I have encountered is this: Some of the big servicers, big banks, have bought up these loans from other small mortgage companies along the way, and clearly there is fraud.

You hire lawyers to do foreclosures. How many of you hire lawyers to deal with fraud when you see it?

Wells Fargo, let me just ask, have you, your servicers, encountered some of the mortgages that are clearly fraudulent where the signatures have been falsified? A lot of income falsification that clearly was not true, what do you do with that kind of information when you encounter it?

Ms. COFFIN. Well, if we do encounter loans that definitely come to our attention that have fraudulent behavior, yes, we do bring that to the attention. Unfortunately, many of the companies who originated those loans are out of business.

And, number two, I will tell you that—

Chairwoman WATERS. But the homeowner—you bought the loan. When you bought the loan from this mortgage company, you had to vet it. You had to look at it to see what you were buying, right? Well, maybe you didn't.

Ms. COFFIN. Not loan by loan.

Chairwoman WATERS. Not loan by loan. You bought packages, okay.

So if you see fraudulent loans where the homeowner has been basically defrauded, what do you do? How can you help that homeowner?

Ms. COFFIN. I think one of the things that is toughest to do is determine where the fraud came from.

Chairwoman WATERS. Well, I know where it came from. It is very clear. It came from the person you bought them from.

Ms. COFFIN. But stated income, stated assets, which is where some of those loans that we acquired, determining the fraud—

Chairwoman WATERS. Well, but I have some where someone said, "That is not my signature; I didn't sign that."

Ms. COFFIN. That would be hard to determine.

Chairwoman WATERS. No, it wouldn't.

All right. So—okay. Well, let's look at another kind of fraud that I have run into. Well, it is not fraud really. Let me look at another case.

I have constituents who need a loan modification and they are earning the same amount of money at the time that they requested a loan modification as they were earning when they got into the loan, when you accepted them into the loan. It is no different.

You accepted them into the loan with what appears to be a lack of adequate income to service that mortgage. They discover along the way that they cannot service that mortgage. It may be a reset, what have you. But then they are asking for a loan modification, and they are told, "You don't have enough income."

But they had enough income when they got the mortgage. What do you do about that?

Bank of America, have you encountered that? Have any of you done loan modifications? How many people have actually done a loan modification?

So what do you do when you encounter someone whose income is exactly the same, when they request a loan modification, as it was when they signed on the dotted line for the mortgage; and now you are saying to them, "You don't qualify; you don't make enough money?"

How do you make that decision?

Mr. SCHAKETT. Well, first of all, we don't compare really what they were making at origination. And the comment about them not having enough money—

Chairwoman WATERS. I beg your pardon?

Mr. SCHAKETT. I am saying, we don't make a comparison back to say what they did at the origination time. The MHA program is set up to say how much income they have, use a 31 percent debt-to-income ratio.

Chairwoman WATERS. Let's forget about the 31 percent.

Ms. Jones had an income of $3,000 a month. She got a home that cost $500,000. She couldn't afford the loan then and she certainly can't afford it now. It has reset. She has the same income. What do you do?

Mr. SCHAKETT. Well, could she not afford the same modified payment if we actually reduced the payment down to her level of income to make it affordable? Could she not afford that payment?

Chairwoman WATERS. No. What you are telling her is, she can't modify because she doesn't make enough money to even get a modification.

Mr. SCHAKETT. Well, since the MHA program allows interest rates as low as 2 percent, 40-year terms with forbearance up to 30 percent—

Chairwoman WATERS. You think you can work something out for her?

Mr. SCHAKETT. For the vast, vast majority of the customers, we certainly could be able to have an offer for her. We would have to understand the particular circumstances. But definitely the program has very nice low floors for interest rates and forbearance amounts that should make the payment affordable for the vast majority of people.

Chairwoman WATERS. Well, I am going to call you about some that we have worked on that fit into that category.

The other thing that I wanted to ask you about is, I think you did refer to what Mrs. Capito alluded to when you said you do forbearance in order to provide assistance to homeowners who have no income or little income, or maybe just unemployment and they need some time.

Wells Fargo, you and Bank of America and Chase, you guys all say that you help these people with forbearance. Is that right?

All right. I am going to call you directly on the ones that we have that have been turned down.

Now, one last question I want to ask. It has been said that it is more profitable to not do a foreclosure in some cases than to do a foreclosure.

I think, Ms. Cohen, you were the one that tried the explain to us how servicers rush to foreclosure rather than modification because it is not in their best interest to do it. Would you explain that one more time?

Ms. COHEN. Sure. Thank you.

When a homeowner stops making payments on the loan, the servicer is still required to advance those payments to the investors. And so one of the challenges for the servicers is to figure out how to finance those advances, because they are generally financed, and how to get the money back to pay back the financing. And when you result in a foreclosure, in general, the pooling and servicing agreements allow the servicer to get paid back first from the foreclosure before the investors get any money. So the servicer gets paid back faster and in a more sure way from the foreclosure.

When is a loan modification, the investors still have priority. In general, they don't get paid first, the servicer doesn't get paid first. And the servicer has a way of recovering the money, but it is not as sure and it's not as fast.

Chairwoman WATERS. So let me just ask—Ms. Sheehan, Chase Home Lending, JPMorgan Chase, are you, as servicers, advancing payments to the investor?

Ms. SHEEHAN. Yes, we do. But I will say for JPMorgan Chase, we do not need financing for our advances. We have a strong capital base, and it is not in our interest to rush to foreclosure. It is not economic if the loan is positive from a net present value perspective, whether we own the loan or whether we service the loan, because for our investors we have an obligation to do the thing that is best for the investor.

Chairwoman WATERS. Wells Fargo, are you advancing the payments, the mortgage payments, to the investors also?

Ms. COFFIN. Yes, we are. And I would concur with all of Ms. Sheehan's comments. We also have a very strong balance sheet. We are not looking for refinancing, and foreclosure is never a better option.

Chairwoman WATERS. Is this strong balance sheet because of the citizens' investment in your banks, in your bailouts?

Ms. COFFIN. No. Wells Fargo has been a AAA bank and we have a strong balance sheet.

Chairwoman WATERS. You did get money from the bailout, didn't you?

Ms. COFFIN. Yes. And we are—

Chairwoman WATERS. How much did you receive?

Ms. COFFIN. $25 billion.

Chairwoman WATERS. You didn't need it?

Ms. COFFIN. We are working to return those funds.

Chairwoman WATERS. But you didn't need it when you got it?

Ms. COFFIN. No.

Chairwoman WATERS. You just took it? They made you take it?

Ms. COFFIN. Yes.

Chairwoman WATERS. Okay. Have any of you found that it is in your best interest to foreclose rather than to hold that and do a modification? Is there ever a time?

Yes, sir?

Mr. SCHAKETT. Yes and no. Ms. Sheehan addressed this.

As you know, part of the Making Home Affordable program itself, it has a calculation called a "net present value" that actually tries to determine is it better to foreclose on the property or actually do the modification.

Now, with the vast majority of the customers it is better to do the modification; but there are cases, if the customer has a lot of equity in the property and if the person can afford a very small payment, where the cost of the interest, cost to give up, is greater than the cost of foreclosure. So it actually makes more sense for the investor to foreclose on the property.

And the Administration has built in the program a protection for the investors to make sure that it is something that both aligns the kind of consumers' interests and the investors' interests. So, yes, there are cases where it makes more sense to foreclose.

But I would like to come back to the point that Ms. Cohen made earlier, which I think is just simply inaccurate, as far as we were talking about capitalizing third-party fees and the foreclosure process. And the statement was made, if you capitalize third-party fees, it will actually increase the payment amount that the customer has to make upon modification.

It just doesn't work that way. For the—yes, indeed, you can have capitalized third-party fees, but as you all are probably aware, the MHA program itself forces you to calculate 31 percent of the person's income, and that becomes the payment amount. So the payment is the same whether you have capitalized $2,000 of the fees or you haven't. And the difference is, the interest rate will go down.

So if you have capitalized fees, then the investor will receive the lower interest rate and the borrower will be in the exact same situation as far as the payment amount under the MHA program whether the fees have been capitalized or not.

Ms. COHEN. Can I respond to that?

So there are a couple of issues. One is—what I said was, if the fees are capitalized and the principal is higher, when the computer crunches the numbers, some homeowners are less likely to get sort of an outcome from the computer that says that the modification is more profitable to the investor than the foreclosure—I mean, it is all related to the net present value calculation. So that is sort of one issue.

I also want to say that every time I am in a meeting in Washington, the representatives of the servicers tell us what their policies are, they tell us that foreclosures are never profitable. But I have example after example of these servicers and others saying, Wells Fargo and Bank of America, you have to give us a payment before we will give you a modification. Bank of America, you need to be in default.

Chase, a person called 5 times in the last week and could not find one person to give them a HAMP loan modification. And an Attorney General attorney called our office and said that Chase is the biggest noncompliant HAMP servicer when it comes to actual responsiveness.

Wells Fargo will give you a 6-month forbearance with a balloon, and then will consider whether to give you a HAMP loan modification.

Over and over again what is happening on the ground does not comport with what these people are saying. And until they are pushed in a mandatory fashion, nothing is going to change.

Ms. COFFIN. Can I make a couple of comments?

In the forbearance—and, yes, there is a balloon at the end of it, and what we are looking for at the end of that 6- to 12-month period is, they still have to obtain a job. As was stated earlier, you cannot do a modification on someone who does not have a job. So there is—and that is communicated and it is made clear.

I think there is also a point to your constituents that I think is most important, and I will come back to the positive. We call early enough in to these borrowers who go delinquent immediately, because we know that the sooner we work with them, we can avoid all these fees—

Chairwoman WATERS. Hold it. Hold it right there, because I think Ms. Cohen said something that had been true in the past. And that was, some of you had policies, you have to be delinquent—before you will even talk to them about a modification—for 2 months. Is that still something that you practice?

Ms. COFFIN. No.

Chairwoman WATERS. Nobody practices that anymore? When did you stop?

Ms. COFFIN. I don't know that we ever did—

Chairwoman WATERS. Oh, yes, you did.

Ms. COFFIN. There are people who might have stated that. But it is in our polices and procedures to tell someone that you must go delinquent.

Chairwoman WATERS. Let me just stop right here.

Bank of America, are you saying that you never had a policy where you had to be in default at least by 2 months before a loan modification could be considered?

Mr. SCHAKETT. No, I am not saying that. I said, with MHA we now have a default standard that it makes it clear, if you actually cannot afford your payment and you are current, you can still qualify for the mortgage, you have to go through the process.

There was not a standard default standard prior to MHA. It was very uneven treatment of people that were current before, absolutely acknowledge that, and it was much easier to get a modification if you were 6 days delinquent than if you were current. And, of course, we did have a policy of not telling customers they need to go delinquent; that was certainly our policy. But it certainly is possible that somebody would have—

Chairwoman WATERS. Well, I found it to be consistent with Bank of America when I work on these loan modifications.

Since I am talking with you, why is it Bank of America does so few loan modifications? Why is your percentage of loan modifications so much lower than everybody else's?

Mr. SCHAKETT. I think if you are talking about—

Chairwoman WATERS. I am just talking about modifications.

Mr. SCHAKETT. Well, if we are talking about modifications in general, I would say that our numbers are not lower than everybody else. And that is the reason why I am referring—the numbers you are probably looking at are the MHA modifications.

One thing I think everybody would agree with, at least the servicers at this table, is that a better view of the kind of modification activity would include all the modifications the banks are doing today. If you look at some of the written testimony coming out from just Chase and Bank of America and Wells, all of us reference other modifications we are doing.

Chase referenced 89,000 additional modifications they did that weren't MHA; those are not in the numbers. Wells referenced 226,000 loans either qualified for or modified that are not MHA numbers. And Bank of America has 225,000, either modification or people qualified, that are not in the MHA numbers.

So we appreciate the committee's focus on the MHA numbers because they—obviously that is where the taxpayer money is being spent at. That is what the oversight is about.

But if you want to have a full appreciation for really how we are helping people stay in the homes, we do believe that you should look at the overall modification efforts. And our numbers will look much better if you look at the overall modifications versus simply what we have done so far in the MHA ramp-up.

Chairwoman WATERS. Well, I recognize this is a voluntary program, and you can do as few or as many as you would like. Why are you doing so few MHAs?

Mr. SCHAKETT. Well, again, as I just tried to explain, it is really a ramp-up period. We have doubled our efforts just the last month. We have set a target goal of 125,000 by November 1st, which I think we will make.

We got a little bit of a—we had a national retention program which I referenced earlier. We were doing lots of modifications prior to MHA, and we made a decision to continue with that program and kind of ramp over with the MHA program versus holding back customers and putting everything directly in MHA. So that kind of hurt our numbers a little bit, because we didn't have the ability of—kind of a lift of a new program; we already had an existing program.

But I think if you look out 6 months from now you will find, as we fully ramp up, our numbers will be, on MHA, comparable to industry standards or better.

Chairwoman WATERS. And how many will support H.R. 3451, our loss mitigation program that helps to direct servicers a bit more than they are directed now?

Are you familiar with that legislation that I have introduced? No? Not yet? Okay.

Well, I would like to thank you all for being here. We just have to do better with loan modifications. There are several reasons: Number one, people just need help, and they want to stay in their homes; and number two, the American citizens have been very generous with the banks.

And most of you represent banks, and your servicers also. Not only have you gotten bailout money, but the complaints are just overwhelming about the credit crunch, the decrease in credit card limits. The complaints are just ongoing, and we want to do everything that we possibly can to help you to do a better job. We think that you are missing the mark.

I don't have the information here to compare what you are doing with the President's program as opposed to what you may be doing. That may be better or worse; I don't know. But I would hope that you would take care to tell us what we can do to help you to do more to help more people—to help unemployed people, to help people who are the victims of fraud, to make your servicers even more accessible and more available.

It would be great to see particularly, the big banks who have locations in so many places, to put some of your servicers on the ground. The menus are still difficult to negotiate when you are on the telephone.

People would like to see some of you, your servicers, face-to-face. You could put some right next to your banking operations so that servicers can talk to individuals. I would like you to think about some of these things, think about and take seriously what we are saying about our concerns.

You heard a lot of discussion about bankruptcy here today. You heard our chairman, who is getting very, very concerned. And I am hopeful that we will be able to do a lot better than we have been doing.

Again, without objection, your written statements will be made a part of the record. And the Chair notes that some members may have additional questions for this panel which they may wish to submit in writing. Without objection, the hearing record will remain open for 30 days for members to submit written questions to these witnesses and to place their responses in the record.

We do have something to enter into the record that we must do. Without objection, this is a letter from NID Housing Counseling Agency.

Thank you so very much for your patience. We went a little bit beyond our normal time, and I thank you for engaging us.

This panel is now dismissed.

[Whereupon, at 1:32 p.m., the hearing was adjourned.]

APPENDIX

September 9, 2009

September 9, 2009

Assistant Secretary for Financial Institutions Michael S. Barr Written Testimony on Stabilizing the Housing Market before the House Financial Services Committee, Subcommittee on Housing and Community Opportunity

Written Testimony

Stabilizing the Housing Market

Chairwoman Waters, Ranking Member Moore and members of the Committee, thank you for the opportunity to testify today about the Treasury Department's comprehensive initiatives to stabilize the US housing market and support homeowners.

Introduction

A strong housing market is crucial to a sustained economic recovery. It is a driver of stability in our financial markets and a fundamental source of wealth for individual families and communities. The recent crisis in the housing sector has devastated families and communities across the country and is at the center of our financial crisis and economic downturn.

Today, I want to outline the steps that Treasury and the Administration have taken to strengthen the housing sector, help millions of homeowners and lay the foundation for economic recovery and financial stability.

Weakness in the US housing market developed over many years. In advance of the downturn, inadequate regulation of lending and securitization practices, including lax underwriting standards, helped cause widespread over-leveraging in the residential mortgage sector that has contributed to millions of borrowers having mortgage payments they are unable to afford.

The rapid decline in home prices over the past two years has had devastating consequences for homeowners, communities and financial institutions throughout the country. Moreover, rising unemployment and other recessionary pressures have impaired the ability of many otherwise responsible families to stay current on their mortgage payments.

The result is that responsible homeowners across America are grappling with the possibility of foreclosure and displacement. Analysts project that more than 6 million families could face foreclosure over the next three years.

The Administration's Efforts to Stabilize the Housing Market

This Administration has acted quickly and aggressively to confront the economic challenges facing our economy and our housing market.

Within weeks of assuming office, President Obama worked with Congress to enact the largest economic recovery plan since World War II.

The Administration is addressing the housing crisis across multiple fronts. First, we boosted demand by implementing a new homebuyer's tax credit in the Recovery Act. Within a month of taking office, on February 18, we announced the Making Home Affordable (MHA) Program, a critical element of Treasury's Financial Stability Plan. This program was broadly designed to stabilize the U.S. housing market and offer assistance to millions of homeowners by reducing mortgage payments and preventing avoidable foreclosures.

A key part of the broad housing plan is the Home Affordable Modification Plan – a comprehensive $75 billion program to lower monthly mortgage payments for at risk borrowers, providing modifications on a scale never previously attempted.

The Home Affordable Modification Program supports loan modifications that will provide sustainable, affordable mortgage payments for up to 3 to 4 million borrowers. HAMP offers "pay-for success" incentives to investors, lenders, servicers, and homeowners for successful mortgage modifications.

There are clear signs that the incentives offered under the Home Affordable Modification Program are having a substantial effect.

- Over forty-five servicers have signed up for the Home Affordable Modification Program, including the five largest. Between loans covered by these servicers and loans owned or guaranteed by the GSEs, more than 85% of loans in the country are now covered by the program.
- These participating servicers have extended offers on over 570,000 trial modifications.
- Over 360,000 trial modifications are already underway.

On March 4, just two weeks after the Feb. 18 announcement of MHA, the Administration, worked with the banking regulators, HUD, and the Federal Housing Finance Agency to publish detailed program guidelines for HAMP. These guidelines outlined a standard for the industry to follow in modifying mortgages to make them affordable and sustainable.

On April 28, the Administration announced additional details related to the Second Lien Program which will help to provide a more comprehensive affordability solution for borrowers by addressing their total mortgage debt. In addition, this announcement included provisions to strengthen the HOPE for Homeowners Program, administered by HUD, which provides additional relief for borrowers with mortgage balances greater than the current value of their homes. In August, we released the supplemental directive providing specific implementation guidelines for the Second Lien Program. Second lien servicers covering the majority of second liens in the country have committed to participate in the second lien program.

On May 14, we announced additional details related to the Foreclosure Alternatives Program, which will provide incentives for short sales and deeds-in lieu of foreclosure where borrowers are unable to complete the HAMP modification process. We also announced additional details on Home Price Decline Protection Incentives, designed to provide incentive payments for modifications to partially compensate lenders and investors for home price declines. As of September 1, Home Price Decline Incentive payments will become operational, and begin to be included in NPV calculations, allowing more borrowers in the geographic areas hardest hit by home price declines to obtain modifications.

The Administration's broad housing plan, the Making Home Affordable Plan, also includes broad support for the GSEs to support mortgage refinancing and affordability across the market.

On March 4, the Administration increased its funding commitment to Fannie Mae and Freddie Mac to support the strength and security of the mortgage market and to help maintain mortgage affordability generally. To this end, Treasury expanded its commitment to the GSEs under the Preferred Stock Purchase Agreements by $200 billion. The Treasury Department also continues to purchase Fannie Mae and Freddie Mac mortgage-backed securities to promote stability and liquidity in the marketplace.

In addition, the Administration increased refinancing flexibilities for the GSEs, providing more homeowners with an opportunity to refinance to lower monthly payments. As a part of this increased refinancing flexibility, the Administration launched the Home Affordable Refinance Program which expands access to refinancing for families whose homes have lost value.

Many homeowners who made what seemed like conservative financial decisions three, four or five years ago find themselves unable to benefit from the low interest rates available today because the value of their homes has sunk below that of their existing mortgages.

Originally, the Home Affordable Refinancing Program was designed to help homeowners whose existing mortgages were up to 105 percent of their current house value, but it has since been expanded to help those with mortgages up to 125 percent of current value.

Overall, the GSEs have refinanced more than 2.7 million loans since the announcement of the Administration's comprehensive housing plan.

HAMP Program Design

Key Principles

The Home Affordable Modification Program is built around three core concepts.

First, the program focuses on affordability. Building on the insights of Chairwoman Bair of the FDIC, it is designed to reduce mortgage payments to an affordable level based on a borrowers' gross monthly income. Every modification under the program must lower the borrower's monthly mortgage payment to 31% of the borrower's monthly gross income.

Second, HAMP's pay-for-success structure aligns the interests of servicers, investors and borrowers in ways that encourage loan modifications that will be both affordable for borrowers over the long term and cost-effective for taxpayers.

Third, the HAMP program establishes detailed guidelines for the industry to use in making loan modifications with the goal of encouraging the mortgage industry to adopt a sustainably affordable standard, both within and outside of the HAMP program.

In the past, a lack of agreed-upon guidelines has limited the number of loan modifications that are completed, even in instances where modifications would have been beneficial to all involved. HAMP should help increase the number of modifications industry-wide by providing standardized modification guidance to servicers and lenders.

That will be good for borrowers, good for lenders, good for mortgage lending standards and good for improved stability of our overall financial system.

Eligibility Criteria

The eligibility criteria for the modification program were developed specifically to help responsible American homeowners with the greatest need for assistance and to provide that assistance at the lowest cost to taxpayers.

Modifications are potentially available to all borrowers regardless of loan-to-value ratio, so borrowers can qualify no matter how much the price of their home has fallen.

The modification plan was designed to be inclusive, with a loan limit of $729,750 for single-unit properties, and higher limits for multi-unit properties. At this level, over 97 percent of the mortgages in the country have a principal balance that might be eligible.

Finally, because it is more effective to reach borrowers before they have missed a payment, the modification program includes additional incentives for the modification of loans where borrowers are current on their payments, but can demonstrate financial hardship or imminent risk of default.

Modification Process

Under HAMP's loan modification guidelines, mortgage servicers are prevented from "cherry-picking" which loans to modify in a manner that might deny assistance to borrowers at greatest risk of foreclosure. Participating servicers are required to service all loans in their portfolio according to HAMP guidelines, unless explicitly prohibited by pooling and servicing agreements, and further must make reasonable efforts to obtain waivers of any limits on participation.

Participating servicers are also required to evaluate every eligible loan using a standard net present value (NPV) test. The NPV test compares the net present value of cash flows with modification and without modification. If the test is positive, the servicer must modify the loan.

Under the program, servicers must reduce the borrower's first lien mortgage to a 31 percent debt-to-income (DTI) ratio, meaning that the monthly mortgage payment can be no greater than 31 percent of gross monthly income. To reach this payment, the servicer must use a specified sequence of steps:

1. Reduce the interest rate, subject to a rate floor of 2 percent.
2. If the 31 percent DTI has not been reached, extend the term or amortization period of the loan up to a maximum of 40 years.
3. If the 31 percent DTI still has not been reached, forbear principal until the 31 percent ratio is achieved.

Principal forgiveness may be applied at any stage. Additionally, each loan must be considered for a HOPE for Homeowners refinancing.

The borrowers' modified monthly payment of 31 percent DTI will remain in place for five years, provided the borrower remains current, and following the modification the interest rate will step up each year to a specified cap that will be fixed for the life of the loan. We believe HAMP creates new fixed-rate loans that homeowners can afford and can understand.

"Pay for Success" Incentive Structure

HAMP offers "pay for success" incentives to servicers, investors and borrowers for successful modifications. This aligns the incentives of market participants and ensures efficient expenditure of taxpayer dollars.

Servicers receive an up-front payment of $1,000 for each successful modification after completion of the trial period, and "pay for success" fees of up to $1,000 per year, provided the borrower remains current. Homeowners may earn up to $1,000 towards principal reduction each year for five years if they remain current and pay on time.

HAMP also matches reductions in monthly payments dollar-for-dollar with the lender/investor from 38 percent to 31 percent DTI. This requires the lender/investor to take the first loss in reducing the borrower payment down to a 38 percent DTI, holding lenders/investors accountable for unaffordable loans they may have extended.

To encourage the modification of current loans expected to default, HAMP provides additional incentive to servicers and lender/investors when current loans are modified.

Signs of Progress

Our progress in implementing these programs to date has been substantial, but we recognize that much more has to be done to help homeowners. Today, I want to highlight some key points of success:

We have signed contracts with over 45 servicers, including the five largest. Between loans covered by these servicers and loans owned or guaranteed by the GSEs, more than 85 percent of all mortgage loans in the country are now covered by the program.

Over 570,000 trial modifications have been offered under the program. Over 360,000 trial modifications are underway.

At this early date, HAMP has already been more successful than any previous similar program in modifying mortgages for at risk borrowers to sustainably affordable levels, and helping to avoid preventable foreclosures.

Nonetheless, we recognize that challenges remain in implementing and scaling up the program, and are committed to working to overcome those challenges and reach as many borrowers as possible. In particular, we are focused on addressing challenges in three key areas: capacity, transparency and borrower outreach.

Expanding Servicer Capacity

We are taking a number of steps and working with servicers to expand nationwide capacity to accommodate the number of eligible borrowers who can receive assistance through HAMP. I highlight some key measures below:

One, we are asking that all servicers move rapidly to expand servicing capacity and improve the execution quality of loan modifications. This will require that servicers add more staff than previously planned, expand call center capacities, provide a process for borrowers to escalate servicer performance and decisions, bolster training of representatives, enhance on-line offerings, and send additional mailings to potentially eligible borrowers

On July 9, as a part of the Administration's efforts to expedite implementation of HAMP, Secretaries Geithner and Donovan wrote to the CEOs of all of the servicers currently participating in the program. In this joint letter, they noted that "there appears to be substantial variation among servicers in performance and borrower experience, as well as inconsistent results in converting trial modification offers into actual trial modifications." They called on the servicers "to devote substantially more resources" to the program in order for it to fully succeed.

The joint letter to participating servicers also requested that the CEOs designate a senior liaison, authorized to make decisions on behalf of the CEO, to work directly with us on all aspects of MHA and attend a program implementation meeting with senior HUD and Treasury officials on July 28, 2009.

At the meeting on July 28, servicers committed to reaching a cumulative target of 500,000 trial modifications started by November 1, 2009. We are on track to meet that goal.

Two, we have made significant progress in reaching implementation objectives outlined during our July 28 meeting.

We are establishing denial codes that will require servicers to report the reason for modification denials, both to Treasury and to borrowers. This will enhance Treasury's ability to evaluate the program and consider options for further program enhancement. We expect denial codes to become operational on Oct. 1.

We are working with servicers and Fannie Mae to streamline application documents and develop web tools, which can serve as a centralized point for modification applications, and for borrowers to check the status of their applications.

Three, we are taking additional steps to expedite implementation, including greater disclosure of the NPV evaluation.

Transparency and Accountability

As Secretary Geithner has noted, we are committed to transparency and better communication in all of Treasury's programs. Accordingly, Treasury is focused on continued transparency and servicer accountability to maximize the effectiveness of HAMP. Specifically, we have taken three additional concrete steps in conjunction with the July 28 servicer liaison meeting to enhance transparency in the program:

On August 4, we began publicly reporting servicer-specific results on a monthly basis. The second public report was published this morning, September 9. These reports provide a transparent and public accounting of individual servicer performance by detailing the number of trial modification offers extended, the number of trial modifications underway, the number of official modifications offered and the long terms success of modifications.

Two, we are working to establish specific operational metrics to measure the performance of each servicer. These performance metrics are likely to include such measures as average borrower wait time in response to inquiries, the quality of information provided to applicants, procedures for document processing and review, and response time for completed applications. We plan to include these metrics in our monthly public report.

Finally, on July 28 we asked Freddie Mac, in its role as compliance agent, to develop a "second look" process pursuant to which Freddie Mac will audit a sample of MHA modification applications that have been declined.

This “second look” process began on August 3, and is designed to minimize the likelihood that borrower applications are overlooked or that applicants are inadvertently denied a modification.

In addition, the “second look” program is examining servicer non-performing loan (NPL) portfolios to identify eligible borrowers that should have been solicited for a modification, but were not.

We have also expanded the efforts of the federal government to combat mortgage rescue fraud and put scammers on notice that we will not stand by while they prey on homeowners seeking help under our program.

Borrower Outreach

The third challenge we are tackling aggressively is borrower outreach. We recognize the importance of borrower outreach and education and are committing significant resources, in partnership with servicers, to reach as many borrowers as possible. Here, we have taken a number of steps:

We have launched a consumer focused website, www.MakingHomeAffordable.gov, with self-assessment tools for borrowers to evaluate potential eligibility in the MHA program. This website is in both English and Spanish and already has over 34 million page views.

We have worked with an interagency team to establish a call center for borrowers to reach HUD approved housing counselors, so that they are able to receive direct information and assistance in applying for the HAMP program.

Working closely with Fannie Mae, we have launched an effort to hold foreclosure prevention workshops and borrower outreach events in cities facing high foreclosure rates. These foreclosure prevention events include counselor training forums where representatives from Treasury, Fannie Mae, HUD and other agencies provide information and training to local housing counselors and non-profit groups, leveraging local resources to expand the reach of the HAMP program. We will have visited 10 hard hit markets by October 1, and will continue our outreach efforts throughout the fall and the year to come.

HAMP has made significant progress in reaching borrowers at risk of foreclosure. However, much more remains to be done and we will continue to work with other agencies, regulators and the private sector to reach as many families as possible.

Program Limitations

Finally, we recognize that any modification program seeking to avoid preventable foreclosures has limits, HAMP included. Even before the current crisis, when home prices were climbing, there were still many hundreds of thousands of foreclosures. Therefore, even if HAMP is a total success, we should still expect millions of foreclosures, as President Obama noted when he launched the program in February.

Some of these foreclosures will result from borrowers who, as investors, do not qualify for the program. Others will occur because borrowers do not respond to our outreach. Still others will be the product of borrowers who bought homes well beyond what they could afford and so would be unable to make the monthly payment even on a modified loan.

Nevertheless, for millions of homeowners, HAMP will provide a critical opportunity to stay in their homes. It will bring relief to the communities hardest hit by foreclosures. It will provide peace of mind to families who have barely managed to stay current on their mortgages or who only recently have fallen behind on payments. It will help stabilize home prices for all American homeowners and, in doing so, aid the recovery of the U.S. economy.

Conclusion

In less than six months, including the initial start-up phase, HAMP has accomplished a great deal and helped homeowners across the country. But we recognize the continued commitment needed to help American families during this crisis and will aggressively continue to build on our progress to date. For example, we are taking additional steps to expedite program implementation and increase take-up, including: implementing the Foreclosure Alternatives Program and strengthening the HOPE for Homeowners refinancing program. Each of these supplemental programs, along with the Second Lien Program and Home Price Decline Protection Incentives is designed to increase the effectiveness and take-up of the first lien modification plan.

Sustained recovery of our housing market is critical to lasting financial stability and promoting a broad economic recovery.

We look forward to working with you to help keep Americans in their homes, restore stability to the US housing market and growth to the U.S. economy.

Thank you. I look forward to your questions.

###

Testimony of Mark A. Calabria, Ph.D.
Director, Financial Regulation Studies, Cato Institute
Before the
House Committee on Financial Services
Subcommittee on Housing and Community Opportunity
On "Progress of the Making Home Affordable Program: What Are the Outcomes for Homeowners and What Are the Obstacles to Success?"
September 9, 2009

Mark A. Calabria, Ph.D. is Director of Financial Regulation Studies at the Cato Institute. Before joining Cato in 2009, he spent six years as a member of the senior professional staff of the U.S. Senate Committee on Banking, Housing and Urban Affairs. In that position, he handled issues related to housing, mortgage finance, economics, banking and insurance for Ranking Member Richard Shelby (R-AL). Prior to his service on Capitol Hill, Calabria served as Deputy Assistant Secretary for Regulatory Affairs at the U.S. Department of Housing and Urban Development, and also held a variety of positions at Harvard University's Joint Center for Housing Studies, the National Association of Home Builders and the National Association of Realtors. Calabria has also been a Research Associate with the U.S. Census Bureau's Center for Economic Studies. He has extensive experience evaluating the impacts of legislative and regulatory proposals on financial and real estate markets, with particular emphasis on how policy changes in Washington affect low and moderate income households. He holds a doctorate in economics from George Mason University. http://www.cato.org/people/mark-calabria

Testimony of Mark A. Calabria, Ph.D.
Director, Financial Regulation Studies, Cato Institute
Before the
House Committee on Financial Services
Subcommittee on Housing and Community Opportunity
On "Progress of the Making Home Affordable Program: What Are the Outcomes for Homeowners and What Are the Obstacles to Success?"
September 9, 2009

Subcommittee Chair Waters, Ranking Member Capito, and distinguished members of the Subcommittee, I thank you for the invitation to appear at today's important hearing. I am Mark Calabria, Director of Financial Regulation Studies at the Cato Institute, a nonprofit, non-partisan public policy research institute located here in Washington. Before I begin my testimony, I would like to make clear that my comments are solely my own and do not represent any official policy positions of the Cato Institute. In addition, outside of my interest as a citizen and a taxpayer, I have no direct financial interest in the subject matter before the subcommittee today, nor do I represent any entities that do.

My testimony today will address two specific questions. The first is: why have the Obama and Bush Administration efforts, along with those of the mortgage industry, to reduce foreclosures had so little impact on the overall foreclosure numbers?

The second question is: given what we know about why previous efforts have had such little impact, what are our policy options?

In answering both these questions, I rely on an extensive body of academic literature, the vast majority of which has been subjected to peer review, which has examined the determinates of mortgage delinquency and default. Foremost among this literature is a series of recent papers written by economists at the Federal Reserve Banks of Boston and Atlanta, in particular the work of Paul Willen, Christopher Foote and Kristopher Gerardi. My testimony owes a considerable intellectual debt to this research.

Why haven't previous efforts stemmed the foreclosure tide?

The short answer to why previous federal efforts to stem the current tide of foreclosures have largely failed is that such efforts have grossly misdiagnosed the causes of mortgage defaults. An implicit assumption behind former Treasury Secretary Paulson's HOPE NOW, FDIC Chair Sheila Bair's IndyMac model, and the Obama Administration's current foreclosure efforts is that the current wave of foreclosures is almost exclusively the result of predatory lending practices and "exploding" adjustable rate mortgages, where large payment shocks upon the rate re-set cause mortgage payment to become "unaffordable."

The simple truth is that the vast majority of mortgage defaults are being driven by the same factors that have always driven mortgage defaults: generally a negative equity position on the part of the homeowner coupled with a life event that results in a substantial shock to their income, most often a job loss or reduction in earnings. Until *both* of these components, negative equity and a negative income shock are addressed, foreclosures will remain at highly elevated levels.

Given that I am challenging the dominant narrative of the mortgage crisis, it is reasonable to ask for more than mere assertions. First, if payment shock alone were the dominate driver of defaults then we would observe most defaults occurring around the time of re-set, specifically just after the re-set. Yet this is not what has been observed. Analysis by several researchers has found that on loans with re-set features that have defaulted, the vast majority of defaults occurred long before the re-set. Of course some will argue that this is due to such loans being "unaffordable" from the time of origination. Yet according to statistical analysis done at the Boston Federal Reserve, the borrower's initial debt-to-income (DTI) had almost no predictive power in terms of forecasting subsequent default.

Additionally if payment shock was the driver of default, the fixed rate mortgages without any payment shocks would display default patterns significantly below that of adjustable rate mortgages. When one controls for owner equity and credit score, the differences in performance between these different mortgage products largely disappears. To further illustrate this point, consider that those mortgages generally considered among the "safest" – mortgages insured by the Federal Housing Administration (FHA), which are almost exclusively fixed rate with no-prepayment penalties and substantial borrower protections, perform, on an apples to apples basis, as badly as the subprime market in terms of delinquencies.

The important shared characteristic of FHA and most of the subprime market is the widespread presence of zero or very little equity in the mortgage at origination. The characteristics of zero or negative equity also explain the poor performance of most subprime adjustable rate mortgages. Many of these loans also had little or no equity upon origination, providing the borrower with little equity cushion when prices fell. Recognizing the critical role of negative equity of course raises the difficult question as to what exactly it is that homeowners are losing in the event of a foreclosure.

"Unnecessary" foreclosures

Central to the arguments calling for greater government invention in the mortgage market is that many, if not most, of the foreclosures being witnessed are "unnecessary" or avoidable. Generally it is argued that investors and loan servicers do not face the same incentives and that in many cases in would be better for the investor if the loan were modified, rather than taken to foreclosure, but still the servicer takes the loan to foreclosure.

The principal flaw in this argument is it ignores the costs to the lender of modifying loans that would have continued paying otherwise. Ex Ante, a lender has no way of separating the truly troubled borrowers, who would default, from those that would take advantage of the system, if they knew they could get a modification just by calling. As long as potentially defaulting borrowers remain a low percentage of all borrowers, as they are today, it is in the best interest of the investor to reject many modifications that might make sense ex post. In addition, lenders may institute various mechanisms to help distinguish troubled borrowers from those looking to game the system.

It is also claimed that the process of securization has driven a wedge between the interests of investors and servicers, with the implication that servicers would be happy to modify, and investors would prefer modifications, but that the pooling and servicing agreements preclude modifications or that servicers fear being sued by investors. The first fact that should question this assumption is the finding by Boston Fed researchers that there is little difference in modification rates between loans held in portfolio versus those held in securitized pools. There is also little evidence that pooling and servicing agreements preclude positive value modifications. According to recent Credit Suisse report, less than 10 percent of agreements disallowed any modifications. While the Congressional Oversight Panel for the TARP has been critical of industry efforts, even that Panel has found that among the sample of pools it examined with a 5-percent cap on the number of modifications, none of the pools examined had actually reached that cap. If few pools have reached the cap, it would seem obvious that the 5 percent cap is not a binding constraint on modifications. In many instances the pooling agreements also require the servicer to act as if the servicer held the whole loan in its portfolio, raising substantial doubts as the validity of the "tranche warfare" theory of modifications.

A careful review of the evidence provides little support for the notion that high transaction costs or a misalignment of incentives is driving lenders to make foreclosures that are not in their economic interest. Since lenders have no way to separate troubled borrowers from those gaming the system, some positive level of negative value foreclosures will be profit-maximizing in the aggregate.

What could reduce the level of foreclosures?

The high level of foreclosures has left many policymakers and much of the public understandably frustrated and searching for answers. To be effective, those answers must be grounded in solid and unbiased analysis. In order to gauge the success of any federal efforts, we must also establish a reasonable baseline. I strongly encourage both Congress and the Administration to present detailed estimates of how many foreclosures are driven by which primary causes and how many of those foreclosures can be reasonably avoided.

Before discussing specific policy proposals, Congress should bear in mind that as approximately 50 percent of foreclosures are currently driven by job loss, the most significant way to reduce foreclosures is to foster an environment that is conducive to private sector job creation. Accordingly, the worst thing Congress can do is to insert uncertainty into the job market, pushing employers to the sides-lines.

In addition to focusing on owners currently in foreclosure, efforts can also be made to reach families before they fall behind on their obligation. For instance, approximately 4 million jobs have been lost in "mass lay-offs" since the beginning of the current recession. Mass lay-offs represent a double shock to households: the loss of a job along with a shock to the local housing market as the result of a major employer downsizing. As damaging as mass lay-offs can be, they do have one advantage – we know about them ahead of time, as the Department of Labor (DoL) collects data on mass lay-offs and workers must be given notice of such. Despite the strong connection between mass lay-offs and foreclosures, there is almost no coordination between DoL and HUD (or the many non-profit organizations providing housing assistance). DoL and HUD should partner in an effort to provide currently appropriated housing counseling funds to workers when they receive a notice of mass lay-off.

Congress can also encourage bank regulators to give lenders more flexibility to lease out foreclosed homes to the current residents. Typically banks come under considerable pressure from their regulators not to engage in long term property leasing or management, as that activity is not considered a core function of banks. I believe we can avoid the larger debate of banks being property managers by giving banks greater flexibility in retaining properties with non-performing mortgages as rentals, preferably to current residents. In addition to many owners who may wish to stay in their homes as renters, approximately 20 percent of foreclosures occur on renter-occupied investment properties. If current renters can continue to make their rent, many banks may prefer to keep those renters rather than proceed to a foreclosure sale.

In order to separate out deserving borrowers, who are trying to get back on their feet, from those simply walking away from a bad investment, Federal lending entities, such as FHA and the GSEs, should engage in aggressive recourse against delinquent borrowers who have the ability to pay, but simply choose not too. All federal modification programs should also include strong recourse provisions. We should make every effort to turn away from becoming a society where legally incurred debts are no longer obligations to be honored but simply options to be exercised.

Lastly, Congress and the Administration should focus resources on those households most in need, who *but for* an intervention, would lose their home. Programs aimed at households who are not facing foreclosure, but simply cannot re-finance due to being "underwater" on their mortgage should be ended. These programs draw off limited lenders/servicer resources that should instead focus on at-need families.

Conclusions

In concluding my testimony, I again wish to strongly state: the current foreclosure relief efforts have largely been unsuccessful because they have misidentified the underlying causes of mortgage default. It is not exploding ARMs or predatory lending that drives the current wave of foreclosures, but negative equity driven by house prices declines coupled with adverse income shocks that are the main driver of defaults on primary residences. Defaults on speculative properties continue to represent a large share of foreclosures. Accordingly, for any plan to be successful it must address both negative equity and reductions in earnings. I thank you for your attention and welcome your questions.

Primary References:

Foote, Gerardi, Goette and Willen (2009) "Reducing Foreclosures: No Easy Answers," National Bureau of Economic Research working paper 15063.

Cordell, L., K. Dynan, A. Lehnert, N. Liang, and E. Mauskopf (2008). The Incentives of Mortgage Servicers: Myths and Realities. Finance and Economics Discussion Series, Federal Reserve Board 46.

Foote, C., K. Gerardi, L. Goette, and P. S. Willen (2008). Just the facts: An initial analysis of subprime's role in the housing crisis. *Journal of Housing Economics* 17 (4).

Foote, C., K. Gerardi, and P. Willen (2008). Negative equity and foreclosure: Theory and evidence. *Journal of Urban Economics* 6 (2), 234–245.

Gerardi, K., A. Shapiro, and P. Willen (2007). Subprime outcomes: Risky mortgages, homeownership experiences, and foreclosures. Federal Reserve Bank of Boston Working Paper 07-15.

Hunt, J. (2009). What do subprime securitization contracts actually say about loan modification. Berkeley Center for Law, Business and the Economy.

Kau, J. B., D. C. Keenan, and T. Kim (1994). Default probabilities for mortgages. *Journal of Urban Economics* 35 (3), 278–296.

Sherlund, S. (2008). The past, present, and future of subprime mortgages. Finance and Economics Discussion Series 2008-63, Federal Reserve Board.

Testimony of

Mary Coffin
Executive Vice President
Wells Fargo Home Mortgage Servicing

Before the

Subcommittee on Housing
Financial Services Committee
United States House of Representatives

September 9, 2009

Chairman Waters, Ranking Member Capito and Members of the Subcommittee, I'm Mary Coffin, head of Wells Fargo Home Mortgage Servicing.

Thank you for the opportunity to come before this Subcommittee today to discuss our continued commitment to doing everything we can to prevent avoidable foreclosures and to help stabilize the housing market. Wells Fargo may be a big corporation, but we operate with the conscience of a company determined to do what is right for our customers, our investors, and for all American taxpayers.

Since we last came before this Subcommittee in February, much has changed and evolved in our economy and in our efforts to assist struggling borrowers.

- First, we worked hard to implement the very detailed and evolving *Home Affordable Modification Programs* which include different guidelines and requirements for Fannie, Freddie, non-GSE, and most recently FHA borrowers.
- To handle the greater than 200 percent increase in borrowers requesting assistance – including the 35 to 40 percent who are current on their mortgages – we have hired and trained an additional 4,600 U.S.-based home retention staff for a total of more than 12,000.
- As of September 3, we have qualified more than 304,000 customers for trial and completed modifications this year alone. As it pertains specifically to HAMP, we have offered 78,000 customers a trial modification and we have received at least the first payment for about 44,000 of these trial modifications.
- We have further enhanced our support systems, our training and our re-training to aide our service representatives in appropriately communicating modification programs and guidelines as they continue to change and expand to help more borrowers.
- In addition, we have improved the ways we obtain from borrowers the extensive documentation the government requires for its programs, and we continue to work to ensure all documents are processed in a timely manner.
- To this point, we have asked the Treasury to meet with us tomorrow to discuss challenges with the *Home Affordable Modification Programs*, and opportunities to make them even more effective.
- And, most importantly, in this dynamic environment we continue to conduct final reviews to ensure every option is exhausted before a property moves to foreclosure sale – because when a foreclosure occurs everyone loses.

Wells Fargo has long adhered to responsible lending and servicing principles that guide our business practices. We did not make negative amortizing, pay option adjustable rate mortgages or subprime stated income loans, despite their popularity. And, as a result, we can directly attest to the fact that the home loans our company originated perform better than those loans we service but had no involvement in originating or underwriting.

Despite widespread decreases in home values, more than 92 percent of our customers in our entire servicing portfolio remain current on their mortgage payments. This is the direct result of our customers' efforts and our commitment to responsibly service all of the loans in our portfolio – including those formerly owned by Wachovia and loans we service but did not originate.

In addition, our delinquency and foreclosure rates continue to be significantly lower than industry average, and the lowest of the nation's largest mortgage lenders. And, for all of 2008 and 2009 year-to-date, less than 2 percent of the owner-occupied properties in our servicing portfolio have actually proceeded to foreclosure sale.

These results would not have been achievable without the continued collaborative public and private sector efforts to inform customers of their options and the introduction of the new *Home Affordable Modification Programs.*

While we are proud to have been part of HAMP's development – as it is an important option – it needs to be acknowledged that HAMP will not help all borrowers in need of payment relief. For the customers who are ineligible for HAMP and where we can reach affordability, we offer customized solutions. During June, July and August – the same time we fully executed HAMP – more than 83% of our customized modifications reduced payments. Where payments stayed the same or increased, the customer did not have a permanent hardship, could afford their monthly payments, and needed short-term assistance to take care of their delinquency – or there were investor restrictions.

Wells Fargo is a company committed to doing what is right for our customers. To that end, I have personally spoken with many of our borrowers to better understand their situations and experiences with Wells Fargo.

These discussions have reinforced for me how many Americans are struggling with changes in their personal and financial circumstances including unemployment and under-employment. I also learned how much they are struggling with the various program requirements and documentation. And, in the past six months some customers have been challenged with getting clear, timely communication from us as the guidelines and the requirements for the various programs have continued to change.

We hold ourselves to a high level of accountability for improving communication and returning all of our customers to the level of service they deserve.

As servicers, we sit between the customer and investor and we are responsible for doing modifications the right way. We also have a responsibility to execute these programs well for all American taxpayers, by ensuring that customers given modifications are truly facing hardships and that they can afford and sustain their home payments after a modification is completed.

In closing, as we have from the very beginning of this crisis, Wells Fargo will continue to seek innovative ways to address the evolving challenges facing our nation. We continue to have faith that together, we will help the nation turn the corner and return the housing market and our economy to a state of health.

Thank you, I look forward to your questions.

Home Affordable Modification Programs

Feb 18	President Obama announced HAMP
Mar 4	Treasury outlines program details
Mar 4	Fannie released guidelines
Mar 11	Freddie released guidelines
Apr 6	Treasury released non-GSE guidelines
Apr 13	Wells Fargo first authorized to participate in HAMP program for non-GSEs
Apr 21	Fannie HAMP guidelines revised
Jul 6	Treasury further refined program details, including trial requirements
Jul 30	Released FHA guidelines
Jul 31	Further revisions to non-GSE guidelines, including home price depreciation incentives
Aug 19	Treasury further refined the guidelines with FAQs
Future	Possible option ARM & short-term mod programs

Customers' Expectations Set

Customers' Expectations Managed

Improvements Needed to Help More At-risk Borrowers

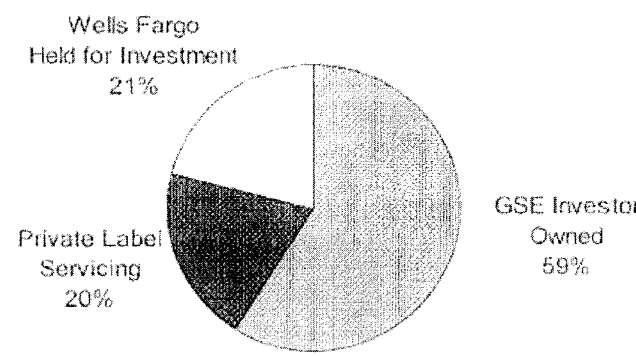
- Finalize HAMP program for second liens
- Provide a tailored HAMP for Pay Option ARMs
- Provide a tailored HAMP for short-term modifications
- Streamline HAMP documentation requirements
- Provide Short-sale incentives
- Revise Hope For Homeowners (H4H)

Wells Fargo Services Loans It Originates and Loans Originated by Others

Mortgage Servicing Rights

- Seventy-nine percent of servicing portfolio is held by other investors. We do not own the loan, but retain the servicing rights.
- We also acquire servicing rights for loans we do not originate.
- Acquired nonprime servicing is handled under the name *America's Servicing Company* (ASC) to allow for private label servicing.
- In our "Held for Investment" portfolio, Wells Fargo owns both the loan and the servicing rights.

Wells Fargo Servicing Portfolio by Investor Type, as of 2Q2009



Large Mortgage Servicer Delinquency Rates

(Dollars in billions, as of June 30, 2009)

Lender	Servicing Volume	Mortgage Delinquency Rate 30-60 Day	60-90 Day	90+ Day	Forcl	Total	Change 1Q09-2Q09
Bank of America Mtg. & Affiliates, NC	$2,111.9	2.93%	1.49%	5.23%	2.74%	12.39%	1.67%
Wells Fargo & Company, IA	$1,752.1	2.31%	1.01%	2.25%	1.92%	7.49%	0.67%
Chase, NJ	$1,443.1	3.36%	1.75%	5.30%	4.19%	14.61%	1.49%
Citi, MO	$769.0	2.49%	1.20%	3.12%	1.48%	8.30%	1.12%
Residential Capital LLC, NY	$297.7	3.89%	1.84%	2.31%	4.77%	12.81%	1.25%
National City Mortgage Co., OH (PNC)	$179.6	3.10%	1.10%	2.21%	2.30%	8.71%	1.31%
SunTrust Mortgage Inc., VA	$170.9	2.45%	1.12%	1.95%	4.91%	10.43%	0.87%
PHH Mortgage, NJ	$149.2	2.22%	0.68%	0.93%	1.79%	5.62%	1.09%
American Home Mortgage Servicing, TX	$96.9	7.49%	4.08%	7.28%	15.29%	34.14%	0.99%
MetLife Home Loans, NY	$97.9	2.43%	0.72%	0.97%	1.48%	5.60%	1.77%
Taylor, Bean, & Whitaker Mortgage Corp., FL	$80.3	4.44%	2.06%	3.43%	3.31%	13.24%	1.94%
BB&T Mortgage, NC	$80.1	1.85%	0.81%	1.10%	1.12%	4.86%	0.29%
Flagstar Bank, MI	$70.1	3.99%	1.93%	2.73%	3.92%	12.57%	2.17%
Provident Funding, CA	$40.0	1.73%	0.27%	0.54%	1.02%	3.56%	0.39%
Ocwen Financial Corporation, FL	$38.4	9.70%	6.10%	11.90%	15.40%	43.10%	3.10%
Citizens Financial Group, Inc., RI	$25.4	1.43%	0.49%	1.20%	1.05%	4.17%	0.47%

Inside Mortgage Finance Large Servicer Delinquency Index

	Servicing Volume	Mortgage Delinquency Rate 30-60 Day	60-90 Day	90+ Day	Forcl	Total
First Quarter 2003	$4,011.3	2.68%	0.61%	0.92%	0.81%	5.02%
Second Quarter 2003	$3,984.1	2.72%	0.57%	0.95%	0.63%	4.88%
Third Quarter 2003	$4,123.4	2.84%	0.67%	1.06%	0.43%	5.00%
Fourth Quarter 2003	$4,259.5	2.45%	0.63%	0.94%	0.63%	4.64%
First Quarter 2004	$4,183.9	1.91%	0.48%	0.81%	0.67%	3.87%
Second Quarter 2004	$4,222.5	2.22%	0.53%	0.52%	0.59%	3.86%
Third Quarter 2004	$4,495.8	2.13%	0.54%	0.49%	0.50%	3.73%
Fourth Quarter 2004	$4,689.8	2.32%	0.58%	0.74%	0.61%	4.25%
First Quarter 2005	$4,879.6	1.71%	0.44%	0.68%	0.61%	3.44%
Second Quarter 2005	$5,258.1	1.91%	0.52%	0.67%	0.51%	3.61%
Third Quarter 2005	$5,446.0	1.96%	0.52%	0.77%	0.54%	3.80%
Fourth Quarter 2005	$5,039.7	2.07%	0.59%	0.88%	0.55%	4.09%
First Quarter 2006	$4,925.7	1.55%	0.45%	0.76%	0.61%	3.37%
Second Quarter 2006	$6,111.4	1.97%	0.59%	0.85%	0.96%	4.37%
Third Quarter 2006	$6,183.6	2.27%	0.67%	0.79%	0.53%	4.25%
Fourth Quarter 2006	$7,093.3	2.52%	0.74%	0.84%	0.67%	4.77%
First Quarter 2007	$7,117.0	2.03%	0.63%	0.84%	0.68%	4.18%
Second Quarter 2007	$7,237.1	2.31%	0.75%	0.90%	0.74%	4.70%
Third Quarter 2007	$7,322.5	2.61%	0.68%	1.02%	0.84%	5.32%
Fourth Quarter 2007	$7,551.1	2.87%	1.00%	1.35%	1.18%	6.19%
First Quarter 2008	$7,151.1	2.18%	0.86%	1.37%	1.34%	5.74%
Second Quarter 2008	$6,940.4	2.36%	0.91%	1.51%	1.32%	6.10%
Third Quarter 2008	$7,035.5	2.76%	1.16%	1.92%	1.58%	7.42%
Fourth Quarter 2008	$7,465.0	2.89%	1.39%	2.46%	1.65%	8.60%
First Quarter 2009	$7,471.5	2.57%	1.25%	3.04%	2.25%	9.11%
Second Quarter 2009	$7,432.0	2.93%	1.42%	3.84%	3.00%	11.18%

Notes: Servicing volume in billions. Lenders shown in italics report delinquencies based on loan count; others are based on dollar volume.

Source: Inside Mortgage Finance

HELPING YOU STAY IN YOUR HOME.

MAKING HOME AFFORDABLE

You may be able to make your payments more affordable.

Act now to get the help you need!

[Servicer logo]

Dear Borrower,

There is help available if you are having difficulty making your mortgage loan payments. You may be eligible for the Home Affordable Modification Program, part of the initiative announced by President Obama to help homeowners.

As your mortgage loan servicer, we will work with you in an effort to make your mortgage payment affordable. You will not pay any fees to take advantage of this opportunity to modify your mortgage loan payment and keep your home. Now is the time to act. We are ready to help you.

Here's how it works: We will first determine if you are eligible based on your situation. If you are eligible, we will look at your monthly income and housing costs, including any past due payments, and then determine an affordable mortgage payment.

At first, you will make new, affordable monthly payments on your mortgage loan during a trial period. If you make those payments successfully and fulfill all trial period conditions, we will permanently modify your mortgage loan.

The modification may involve some or all of the following changes to your mortgage loan: **1)** Bringing your account current; **2)** Reducing the interest rate on your loan; **3)** Extending the term of the loan, and/or **4)** delaying your repayment of a portion of the mortgage principal until the end of the loan term. ***[Servicer can also mention the possibility of principal forgiveness if permitted by the investor.]***

STEP 1 GATHER THE INFO WE NEED TO HELP YOU

To take advantage of this opportunity and the Home Affordable Modification Program, contact us as soon as possible. To help speed the process it will be helpful if you have the following information when you call:

- Loan number
- Monthly pre-tax income of each borrower
- Information about any financial hardship you are suffering

If you do not qualify for a loan modification under this program, or do not want to stay in your home, we will work with you to explore other options available to help you keep your home or ease your transition to a new home.

STEP 2 CONTACT US

We want to make modifying your mortgage loan as easy as possible. However, you must take the first step by contacting us at [phone number]. You may also write to us at the address at the [bottom/top] of this letter. Be sure to include the information listed above. [Servicer may insert any fax or e-mail contact alternatives.]

Sincerely,

The *Making Home Affordable* program was created to help millions of homeowners refinance or modify their mortgages. As part of this program, we – your mortgage servicer – and the Federal Government are working to offer you options to help you stay in your home.

GSL-309-01-08

IMPORTANT NOTICE We want to help you avoid foreclosure scams.

Beware of Foreclosure Rescue Scams. Help is free!

- There is never a fee to get assistance or information about the Making Home Affordable Program from your lender or a HUD-approved housing counselor.
    - For a HUD-approved counselor, visit: http://www.hud.gov/offices/hsg/sfh/hcc/fc/
- Beware of any person or organization that asks you to pay a fee in exchange for housing counseling services or modification of a delinquent loan.
- Beware of anyone who says they can "save" your home if you sign or transfer over the deed to your house. Do not sign over the deed to your property to any organization or individual unless you are working directly with your mortgage company to forgive your debt.
- Never make your mortgage payments to anyone other than your mortgage company without their approval.

Progress of the Making Home Affordable Program:
What Are the Outcomes for Homeowners and What are the Obstacles to Success

Written Testimony

of

Alys Cohen
National Consumer Law Center

also on behalf of
National Association of Consumer Advocates

Before the United States House of Representatives
Subcommittee on Housing and Community Opportunity
of the House Committee on Financial Services

September 9, 2009

I. Introduction

Chairwoman Waters, Ranking Member Capito, and members of the Subcommittee, thank you for inviting me to testify today regarding the Making Home Affordable Program and its effect on foreclosures.

I am a staff attorney at the National Consumer Law Center (NCLC).[1] In my work at NCLC, I provide training and technical assistance to attorneys across the country representing homeowners who are facing foreclosure, and I also lead the Center's Washington mortgage policy work. Prior to my work at the National Consumer Law Center, I focused on mortgage lending issues as an attorney at the Federal Trade Commission's consumer protection bureau, where I was involved in investigations and litigation regarding lending abuses (and where I drafted the Commission's first testimony regarding predatory mortgage lending in the late 1990s). I testify here today on behalf of the National Consumer Law Center's low-income clients. On a daily basis, NCLC provides legal and technical assistance on consumer law issues to legal services, government and private attorneys representing low-income consumers across the country. I also testify here today on behalf of the National Association of Consumer Advocates.[2]

---

[1] The **National Consumer Law Center, Inc.** (NCLC) is a non-profit Massachusetts Corporation, founded in 1969, specializing in low-income consumer issues, with an emphasis on consumer credit. On a daily basis, NCLC provides legal and technical consulting and assistance on consumer law issues to legal services, government, and private attorneys representing low-income consumers across the country. NCLC publishes a series of eighteen practice treatises and annual supplements on consumer credit laws, including *Truth In Lending* (6th ed. 2007) and *Cost of Credit: Regulation, Preemption, and Industry Abuses* (3d ed. 2005) and *Foreclosures* (2d ed. 2007), as well as bimonthly newsletters on a range of topics related to consumer credit issues and low-income consumers. NCLC attorneys have written and advocated extensively on all aspects of consumer law affecting low-income people, conducted training for thousands of legal services and private attorneys on the law and litigation strategies to deal predatory lending and other consumer law problems, and provided extensive oral and written testimony to numerous Congressional committees on these topics. This testimony was written by Alys Cohen, Staff Attorney, and Diane E. Thompson, Of Counsel, NCLC.

[2] The **National Association of Consumer Advocates** (NACA) is a non-profit corporation whose members are private and public sector attorneys, legal services attorneys, law professors, and law students, whose primary focus involves the protection and representation of consumers. NACA's mission is to promote justice for all consumers.

We are facing in this country a foreclosure tsunami, which threatens to destabilize our entire economy, devastate entire communities, and destroy millions of families. Large-scale, sustainable modifications are widely recognized as an essential component of restoring economic health to our country—a goal that is not yet in sight.

The Home Affordable Modification Program (HAMP) announced by President Obama's administration on March 4, 2009, is a laudable attempt to overcome long standing reluctance by servicers to perform large numbers of sustainable loan modifications. HAMP seeks to change the dynamic that leads servicers to refuse even loan modifications that would be in the investors' best interests by providing both servicers and investors with payments to support successful loan modifications. Several months into the Home Affordable Modification Program (HAMP), however, homeowners and their advocates report that the program is not providing a sufficient number of loan modifications to homeowners, the modifications offered often do not meet the guidelines of the program, and the program itself still presents serious barriers to mass loan modifications. Moreover, even if HAMP operated at its full capacity as envisioned by Treasury officials, HAMP's loan modifications still would be substantially outpaced by foreclosures, and the modifications themselves lack the mandated principal reductions that many believe are necessary to stem the foreclosure tide.

To date, implementation of the program by servicers has been slow and sporadic. The Administration's efforts to hold servicers accountable[3] are a welcome and necessary step forward, however, further changes to the program's design are needed for the program to reach even its stated goals. A timeline should be set to evaluate whether HAMP, along with other existing

[3] Renae Merle, *White House Prods Banks: Letter Tells Chiefs To Start Backing Mortgage Relief*, Wash. Post, July 10, 2009, *available at* http://www.washingtonpost.com/wp-dyn/content/article/2009/07/09/AR2009070902928.html?nav=rss_business.

programs, can sufficiently address foreclosures.[4] If the data confirm the experience of advocates nationwide, which seems likely in light of structural barriers in the servicing industry that inhibit efficient loan modifications (even when they are in the interest of investors), more stringent measures should be adopted. With cure rates at a historic low, only a stronger approach to loan modifications will make a difference. Congress should mandate a loan modification process that guarantees that homeowners facing hardship will be offered a second chance when it is consistent with investor interests and also should allow bankruptcy judges to modify appropriate mortgage loans.

A. Problems with Servicers' Implementation of HAMP Plague Homeowners Seeking Loan Modifications.

- Participating servicers violate the HAMP guidelines:
  - Servicers still require waivers.
  - Some participating servicers offer non-compliant loan modifications.
  - Some participating servicers refuse to offer HAMP modifications.
  - Servicers charge fees to homeowners for the modification.
  - Servicers are continuing to initiate foreclosures and sell homes at foreclosure sales while the HAMP review is pending.
- Servicer staffing and training still lag behind what is needed.

[4] As GAO has noted, the Treasury Department may be overstating its assumptions on participation and success, and there is an important outstanding question regarding success of permanent modifications that go beyond the trial modification period. United States Government Accountability Office, *Troubled Asset Relief Program: Treasury Actions Needed to Make the Home Affordable Modification Program More Transparent and Accountable* (July 2009).

  - Homeowners and counselors report waits of months to hear back on review for a trial modification, followed by very short time frames to return documents.
  - Staff of participating servicers continue to display alarming ignorance of HAMP.
  - Non-participating servicers continue to represent themselves as participating in HAMP.

- Lack of transparency and accountability is resulting in summary denials and other unreasonable acts by servicers.

B. Certain HAMP Policies Must Be Changed to Provide Sustainable Modifications and Save Communities.

- Transparency must be improved.
  - The Net Present Value model for qualifying homeowners must be available to the public.
  - The layers of documents governing HAMP, the guidelines, the Supplemental Directives, the various FAQ's, and the servicer contracts, should be consolidated, reconciled, and clarified.
  - Participating subsidiaries must be clearly identified.

- Mechanisms for enforcement and compliance should be adopted.
  - All foreclosure proceedings must be stopped upon the initiation of a HAMP review, not just at the point before sale.

- Homeowners should be provided with an independent review process when denied a loan modification.
- Homeowners should have access to an ombudsman to address complaints about the process.
- Denials based in part on a borrower's credit score should be accompanied by an adverse action notice under the Fair Credit Reporting Act.

❖ The HAMP guidelines should be adjusted to provide more meaningful relief to homeowners without reducing their existing rights.

- Homeowners need principal reductions, not forbearance.
- Homeowners suffering an involuntary drop in income should be eligible for a second HAMP loan modification.
- Homeowners in bankruptcy should be provided clear access to the HAMP program.
- Mortgages should remain assumable as between spouses, children, and other persons with a homestead interest in the property.
- Fair lending principles must be ensured throughout the HAMP process.
- HAMP application procedures should better recognize and lessen the impact of exigent circumstances.
- The trial modification program should be further formalized and clarified, such that homeowners receive assurances of the terms of the permanent modification and

homeowners are not put into default on their loans if they are current at the onset of the trial modification.

- The final modification agreement should make clear that the homeowners do not waive any rights nor are required to reaffirm the debt in order to enter into the modification.

- The second lien program should be further developed to promote coordination with first lien modifications; servicers should be required to participate in both programs.

❖ Data collection and reporting should provide broad, detailed information in order to support the best HAMP outcomes.

II. Foreclosures Far Outweigh Loan Modifications.

Goldman Sachs estimates that, starting at the end of the last quarter of 2008 through 2014, 13 million foreclosures will be started.[5] The Center for Responsible Lending, based on industry data, predicts 2.4 million foreclosures in 2009, and a total of 9 million foreclosures between 2009 and 2012.[6] At the end of the first quarter of 2009, more than 2 million houses were in foreclosure.[7] At the close of the second quarter of 2009, the percent of loans that were seriously delinquent was 7.97 percent, 73 basis points higher than the first quarter of 2009 and 347 basis points higher than the

[5] Goldman Sachs Global ECS Research, *Home Prices and Credit Losses: Projections and Policy Options* (Jan. 13, 2009), at 16; *see also* Rod Dubitsky, Larry Yang, Stevan Stevanovic & Thomas Suehr, Credit Suisse Fixed Income Research, *Foreclosure Update: Over 8 Million Foreclosures Expected* 1 (Dec. 4, 2008) (predicting 9 million foreclosures for the period 2009-2012).
[6] Center for Responsible Lending, Soaring Spillover 1 (May 2009), *available at* http://www.responsiblelending.org/mortgage-lending/research-analysis/soaring-spillover-3-09.pdf.
[7] Mortgage Bankers' Ass'n, Nat'l Delinquency Survey Q109 at 4 (2009) (reporting that 3.85% of 44,979,733, or 1.7 million, mortgages serviced were in foreclosure). Roughly half of these were serviced by national banks or federal thrifts. *See* Office of the Comptroller of the Currency & Office of Thrift Supervision, OCC and OTS Mortgage Metrics Report: Disclosure of National Bank and Federal Thrift Mortgage Loan Data, First Quarter 2009, at 8 (June 2009), *available at* http://files.ots.treas.gov/482047.pdf (reporting that 884,389 foreclosures were in process by national banks and federal thrifts at the end of the first quarter of 2009). The estimate of more than 2 million homes in foreclosure is achieved by extrapolating from the MBA numbers. The MBA survey only covers approximately 80% of the mortgage market. Thus, (44979733*3.85%)/0.8=2.16 million.

second quarter of 2008.[8] Realtytrac recently reported that an additional 300,000 homes go into foreclosure every month.[9] At the same time, cure rates have declined from an average of 45% during 2000-2006 to 6.6%. In addition to prime cure rates dropping to 6.6%, Alt-A cure rates have decreased 4.3%, from an average of 30.2%, and subprime has dropped to 5.3% from an average of 19.4%.[10] These spiraling foreclosures weaken the entire economy and devastate the communities in which they are concentrated.[11] Neighbors lose equity;[12] crime increases;[13] tax revenue shrinks.[14]

---

8 Mortgage Bankers' Ass'n, Nat'l Delinquency Survey Q209 at 2 (2009).

9 Realtytrac, 1.9 Million Foreclosure Filings Reported On More Than 1.5 Million U.S. Properties in First Half of 2009, *available at* http://www.realtytrac.com/ContentManagement/PressRelease.aspx?channelid=9&ItemID=6802.

10 Press Release, Fitch Ratings (Aug. 24, 2009).

11 *See, e.g.,* Ben S. Bernanke, Chairman, Bd. of Governors, Fed. Reserve Sys., Address at the Federal Reserve System Conference on Housing and Mortgage Markets (Dec. 4, 2008), *available at* http://www.federalreserve.gov/newsevents/speech/bernanke20081204a.htm#f12; Ira J. Goldstein, The Reinvestment Fund, Lost Values: A Study of Predatory Lending in Philadelphia, at 62/-/63 (2007), *available at* www.trfund.com/resource/downloads/policypubs/Lost_Values.pdf (discussing disastrous community impact left behind by failed subprime lenders).

12 *See* John P. Harding, Eric Rosenblatt, & Yao Vincent, The Contagion Effect of Foreclosed Properties (July 15, 2008), *available at* http://ssrn.com/abstract=1160354; Letter, Senator Dodd to Senator Reid (Jan. 22, 2008) (describing cycle of disinvestment, crime, falling property values and property tax collections resulting from foreclosures), *available at* http://dodd.senate.gov/multimedia/2008/012308_ReidLetter.pdf; Staff of the J. Economic. Comm., 110th Cong., 1st Sess., The Subprime Lending Crisis: The Economic Impact on Wealth, Property Values and Tax Revenues, and How We Got Here (2007), *available at* http://jec.senate.gov/index.cfm?FuseAction=Reports.Reports&ContentRecord_id=c6627bb2-7e9c-9af9-7ac7-32b94d398d27&Region_id=&Issue_id= (projecting foreclosed home owners will lose $71 billion due to foreclosure crisis, neighbors will lose $32 billion, and state and local governments will lose $917 million in property tax revenue); Dan Immergluck & Geoff Smith, *The External Costs of Foreclosure: The Impact of Single-Family Mortgage Foreclosures on Property Values*, 17 Housing Pol'y Debate 57, 69, 75 (2006) ("for each additional conventional foreclosure within an eighth of a mile of a house, property value is expected to decrease by 1.136 percent"; estimating total impact in Chicago to be between $598 million and $1.39 billion); William C. Apgar, Mark Duda, & Rochelle Nawrocki Gorey, The Municipal Cost of Foreclosures: A Chicago Case Study (Hous. Fin. Policy Research Paper 2005), at 1, *available at* www.995hope.org/content/pdf/Apgar_Duda_Study_Full_Version.pdf; John P. Harding, Eric Rosenblatt, & Yao Vincent, The Contagion Effect of Foreclosed Properties (July 15, 2008), *available at* http://ssrn.com/abstract=1160354 ; Letter, Senator Dodd to Senator Reid (Jan. 22, 2008) (describing cycle of disinvestment, crime, falling property values and property tax collections resulting from foreclosures), *available at* http://dodd.senate.gov/multimedia/2008/012308_ReidLetter.pdf.

13 *See, e.g.,* J.W. Elphinstone, *After Foreclosure, Crime Moves In*, Boston Globe, Nov. 18, 2007 (describing Atlanta neighborhood now plagued by house fires, prostitution, vandalism and burglaries); Dan Immergluck & Geoff Smith, *The Impact of Single-Family Mortgage Foreclosures on Neighborhood Crime*, 21 Housing Stud. 851 (2006), *available at* www.prism.gatech.edu/~di17/housingstudies.doc (calculating that for every 1% increase in the foreclosure rate in a census tract there is a corresponding 2% increase in the violent crime rate).

14 *See, e.g.,* ., Staff of the J. Economic Comm., 110th Cong., 1st Sess., The Subprime Lending Crisis: The Economic Impact on Wealth, Property Values and Tax Revenues, and How We Got Here (2007), *available at* http://jec.senate.gov/index.cfm?FuseAction=Reports.Reports&ContentRecord_id=c6627bb2-7e9c-9af9-7ac7-32b94d398d27&Region_id=&Issue_id= (projecting foreclosed home owners will lose $71 billion due to foreclosure crisis, neighbors will lose $32 billion, and state and local governments will lose $917 million in property tax revenue); William C. Apgar, Mark Duda, & Rochelle Nawrocki Gorey, The Municipal Cost of Foreclosures: A Chicago Case

Communities of color remain at the epicenter of the crisis; targeted for subprime, abusive lending, they now suffer doubly from extraordinarily high rates of foreclosure and the assorted ills that come with foreclosure.[15]

Modifications have not made a dent in the burgeoning foreclosures. A recent paper in the Boston Federal Reserve Bank's Public Policy series found that less than eight percent of all the loans 60 days or more delinquent were modified during 2007-2008.[16] Professor Alan White, in examining pools of securitized mortgages, found that the number of modifications varied dramatically by servicer, ranging from servicers who modified as many as 35 percent of the loans in foreclosure to as few as 0.28 percent of the loans in foreclosure in November 2008.[17] Even at the high end of 35 percent of all mortgages in foreclosure, the modification rate is not enough to reduce the foreclosure rate to pre-crisis levels.[18]

Worse, the modifications offered pre-HAMP (and presumably still by servicers not offering HAMP modifications) were overwhelmingly ones that increased the borrower's payment and principal balance. Only about three percent of the delinquent loans studied in Boston Federal Reserve Bank

---

Study (Hous. Fin. Policy Research Paper), 2005, at 1, *available at* www.995hope.org/content/pdf/Apgar_Duda_Study_Full_Version.pdf.

[15] *See, e.g.*, Michael Powell & Janet Roberts, *Minorities Affected Most as New York Foreclosures Rise*, N.Y. Times, May 15, 2009; Mortgage Foreclosure Filings in Pennsylvania: A Study by the Reinvestment Fund for the Pennsylvania Department of Banking 36 (Mar. 2005), *available at* www.trfund.com/policy/pa_foreclosures.htm; Paul Calem, Kevin Gillen & Susan Wachter, *The Neighborhood Distribution of Subprime Mortgage Lending*, 29 J. Real Estate Fin. & Econ. 393 (2004); Ira Goldstein, The Reinvestment Fund, Predatory Lending: An Approach to Identify and Understand Predatory Lending (2002) (showing that areas within the City of Philadelphia that are predominately African American or Latino also tended to have higher concentrations of foreclosure sales and were more vulnerable to predatory lending); *cf.* AARP Pub. Pol'y Inst., A First Look at Older Americans and the Mortgage Crisis 5 (2008), http://assets.aarp.org/rgcenter/econ/i9_mortgage.pdf (African Americans and Hispanics are foreclosed on at roughly three times the rate of white Americans).

[16] Manuel Adelino, Kristopher Gerardi & Paul S. Willen, *Why Don't Lenders Renegotiate More Home Mortgages? Redefaults, Self-Cures, and Securitization* 35 (Fed. Reserve Bank of Boston Pub. Pol'y Paper No. 09-4, July 6, 2009), *available at* http://www.bos.frb.org/economic/ppdp/2009/ppdp0904.pdf.

[17] Alan M. White, *Deleveraging the American Homeowner: The Failure of 2008 Voluntary Mortgage Modification Contracts,* Conn. L. Rev. 12-13 (forthcoming 2009), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1325534.

[18] *See* Ben S. Bernanke, Chairman, Bd. of Governors, Fed. Reserve Sys., Address at the Federal Reserve System Conference on Housing and Mortgage Markets (Dec. 4, 2008), *available at* http://www.federalreserve.gov/newsevents/speech/bernanke20081204a.htm#f12 (noting that the number of foreclosures has more than doubled from pre-crisis levels).

paper received modifications that reduced the payment.[19] Professor White's data shows that, in the aggregate, modifications increase the principal balance.[20] While the first quarter 2009 data from the OCC and OTS shows that a majority of the modifications (excluding short term payment plans or forbearance agreements) decreased the payment, most of those modifications also increased the principal balance by capitalizing arrears.[21] Unsurprisingly, redefault rates on loan modifications remain high.[22]

HAMP's redefault rate will depend on the quality of the modifications offered. While in theory, HAMP modifications should have a lower rate of redefault because payments are reduced, there remain serious questions about the quality of HAMP modifications. Extensive reports from advocates around the country show that the quality of loan modifications offered too often does not comport with HAMP guidelines. Advocates for homeowners continue to report problems with implementation of the program.[23] Servicers are all too often refusing to do HAMP modifications, soliciting a waiver of homeowners' rights to a HAMP review, and structuring offered modifications in ways that violate HAMP. These violations may be harder to detect than the gross failure of servicers to date to process a meaningful number of modifications, but they will vitiate HAMP just as surely. While not every homeowner can and should receive a modification, more will need to be done.

---

[19] Manuel Adelino, Kristopher Gerardi & Paul S. Willen, *Why Don't Lenders Renegotiate More Home Mortgages? Redefaults, Self-Cures, and Securitization* (Fed. Reserve Bank of Boston Pub. Pol'y Paper No. 09-4, July 6, 2009), *available at* http://www.bos.frb.org/economic/ppdp/2009/ppdp0904.pdf.

[20] Alan White, *Rewriting Contracts, Wholesale: Data on Voluntary Mortgage Modifications from 2007 and 2008 Remittance Reports,* Fordham Urb. L. J. 20 (forthcoming 2009), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1259538#

[21] Office of the Comptroller of the Currency & Office of Thrift Supervision, OCC and OTS Mortgage Metrics Report: Disclosure of National Bank and Federal Thrift Mortgage Loan Data, First Quarter 2009, at 5 (June 2009), *available at* http://files.ots.treas.gov/482047.pdf.

[22] Office of the Comptroller of the Currency & Office of Thrift Supervision, OCC and OTS Mortgage Metrics Report: Disclosure of National Bank and Federal Thrift Mortgage Loan Data, First Quarter 2009, at 6 (June 2009), *available at* http://files.ots.treas.gov/482047.pdf.

[23] *See, e.g.,* California Reinvestment Coalition, *The Ongoing Chasm Between Words and Deeds: Abusive Practices Continue to Harm Families and Communities in California* (2009); Peter S. Goodman, *Paper Avalanche Buries Plan to Stem Foreclosures,* N.Y. Times, June 29, 2009.

Moreover, the lack of mandated principal reductions under HAMP raises questions about the long-term sustainability of the modifications. Absent a mandate of principal reduction, almost all borrowers are likely denied the possibility of principal reductions, which undermines the long-term success of their modifications, and thus their homeownership. The double-whammy of declining home values and job losses helps fuel the current foreclosure crisis.[24] Homeowners who could normally refinance their way out of a lost job or sell their home in the face of foreclosure are denied both options when they owe more on their home than it is worth. Without principal reductions, homeowners who lose their jobs, have a death in the family, or otherwise experience a drop in income are more likely to experience redefault and foreclosure.[25] The threat of high rates of redefault looms without a meaningful way to reduce the principal balance of mortgages.

HAMP will, at best, reduce foreclosures by one-third; it is unlikely to shrink the foreclosure numbers to pre-crisis levels. Even if the Administration reaches its goal of providing 3 to 4 million loan modifications through HAMP, that will address no more than one-third of all foreclosures.[26] This leaves a majority of all foreclosures still unaddressed, and the foreclosure rate still significantly elevated compared to more normal times.[27]

---

[24] *Preserving Homeownership: Progress Needed to Prevent Foreclosures: Hearing Before the Senate Commi. on Banking, Housing & Urban Affairs*, 111th Cong. (July 16, 2009), at 4-5 (testimony of Paul Willen).

[25] This is especially so since the HAMP modification program does not permit a second HAMP modification for any reason, even if there is a subsequent, unavoidable drop in income.

[26] If we compare the Center for Responsible Lending's predictions of 9 million foreclosures for the period 2009-2012, Center for Responsible Lending, Soaring Spillover 1 (May 2009), *available at* http://www.responsiblelending.org/mortgage-lending/research-analysis/soaring-spillover-3-09.pdf., with Treasury's prediction that HAMP will provide 3-4 million modifications over the same period, and then recognize that not every modified loan would have resulted in a foreclosure absent modification, one-third seems a generous estimate for the amount of reduction in the foreclosure rate afforded by HAMP.

[27] *See* Ben S. Bernanke, Chairman, Bd. of Governors, Fed. Reserve Sys., Address at the Federal Reserve System Conference on Housing and Mortgage Markets (Dec. 4, 2008), *available at* http://www.federalreserve.gov/newsevents/speech/bernanke20081204a.htm#f12 (noting that the number of foreclosures has more than doubled from pre-crisis levels). While a substantial portion of the homeowner whose loans will not be modified by HAMP may be unemployed or have reduced paychecks, some portion of these homeowners will be able to support a loan modification or qualify for other temporary assistance.

In part, this slow start reflects problems with staffing at the servicers. Servicers are still staffing up to deal with homeowners in distress.[28] Administration officials have admitted that the industry is not yet up to the task.[29] The progress servicers have made in hiring loan modification staff, although real, is not keeping up with the numbers of foreclosures filed by those same servicers.

III. Servicers' Lack of Alignment with the Interests of Investors or Homeowners Contributes to the Failure to Do Loan Modifications.

As discussed above, despite widespread calls for more modifications, the number of modifications remains paltry compared to the number of foreclosures. And investors are losing mind-boggling large sums of money on foreclosures.[30] The available data suggests that investors lose ten times more on foreclosures than they do on modifications.[31] In particular, leading investor groups have advocated broader use of principal reductions as part of the anti-foreclosure arsenal, but only a handful of servicers have obliged.[32]

A. Servicers Have Different Interests Than Investors.

In attempting to make sense of this puzzle, we should remember that servicers are not investors. Investors hold the note, or a beneficial interest in it, and are, in general, entitled to repayment of the interest and principal. Servicers collect the payments from the homeowners on behalf of the investors. The bulk of their income comes from a percentage payment on the outstanding principal

---

[28] *See, e.g.,* Peter S. Goodman, *Promised Help Is Elusive for Some Homeowners*, N.Y. Times, June 3, 2009.
[29] Peter S. Goodman, *Paper Avalanche Buries Plan to Stem Foreclosures*, N.Y. Times, June 29, 2009) (quoting Michael Barr, Assistant Secretary for Financial Institutions at the Treasury Department: "They need to do a much better job on the basic management and operational side of their firms . . . .What we've been pushing the servicers to do is improve their infrastructure to make sure their call centers are doing a better job. The level of training is not there yet.").
[30] *Home Foreclosures: Will Voluntary Mortgage Modification Help Families Save Their Homes? Hearing Before the Subcomm. on Commercial and Administrative Law of the H. Comm. on the Judiciary,* 111th Cong. (2009) (testimony of Alan M. White) (65% loss severity rates on foreclosures in June 2009).
[31] *Home Foreclosures: Will Voluntary Mortgage Modification Help Families Save Their Homes? Hearing Before the Subcomm. on Commercial and Administrative Law of the H. Comm. on the Judiciary,* 111th Cong. (2009) (testimony of Alan M. White).
[32] *Preserving Homeownership: Progress Needed to Prevent Foreclosures: Hearing Before the Senate Commi. on Banking, Housing & Urban Affairs,* 111th Cong. (July 16, 2009) (testimony of Curtis Glovier, on behalf of the Mortgage Investors Coalition).

balance in the pool; the bulk of their net worth is tied to the value of the mortgage servicing rights they purchased. A servicer may or may not lose money—or lose it in the same amounts or on the same scale—when an investor loses money. And it is servicers, not investors, who are making the day-to-day, on the ground, decisions as to whether or not to modify any given loan.

Servicers continue to receive most of their income from acting as largely automated pass-through accounting entities, whose mechanical actions are performed offshore or by personified computer systems.[33] Their entire business model is predicated on making money by skimming profits from what they are collecting: through a fixed percentage of the total loan pool, fees charged homeowners for default, interest income on the payments during the time the servicer holds them before they are turned over to the owners, and affiliated business arrangements. Servicers make their money largely through lucky or strategic investment decisions: purchases of the right pool of mortgage servicing rights and the correct interest hedging decisions. Performing large numbers of loan modifications would cost servicers upfront money in fixed overhead costs, including staffing and physical infrastructure.

B. Servicers' Business Model Involves As Little Service As Possible.

As with all businesses, servicers add more to their bottom line to the extent that they can cut costs.[34] Servicers have cut costs by relying more on voicemail systems and less on people to assist homeowners, by refusing to respond to homeowners' inquires and by failing to resolve borrower disputes. Servicers sometimes actively discourage homeowners from attempting to resolve matters.

---

[33] *See, e.g., In re* Taylor, 2009 WL 1885888 (Bankr.E.D.Pa. Apr 15, 2009).
[34] *See* Joseph R. Mason, Servicer Reporting Can Do More for Modification than Government Subsidies 17 (Mar. 16, 2009), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1361331(noting that "servicers' contribution to corporate profits is often . . . tied to their ability to keep operating costs low").

As one attorney in Michigan attempting to arrange a short sale with Litton reports, the voice mail warns "If you leave more than one message, you will be put at the end of the list of people we call back." Recent industry efforts to "staff-up" loss mitigation departments have been woefully inadequate.[35] As a result, servicers remain unable to provide affordable and sustainable loan modifications on the scale needed to address the current foreclosure crisis. Instead homeowners are being pushed into short-term modifications and unaffordable repayment plans.

Creating affordable and sustainable loan modifications for distressed homeowners on a loan-by-loan basis is labor intensive.[36] Under many current pooling and servicing agreements, additional labor costs incurred by servicers engaged this process are not compensated by the loan owner. By contrast, servicers' costs in pursuing a foreclosure are compensated. In a foreclosure, a servicer gets paid before an investor; in a loan modification, the investor will usually continue to get paid first. Under this cost and incentive structure, it is no surprise that servicers continue to push homeowners into less labor-intensive repayment plans, non-HAMP loan modifications, or foreclosure.

Post hoc reimbursement for individual loan modifications is not enough to induce servicers to change their existing business model. This business model—of fee-collecting and fee-skimming—has been extremely profitable. A change in the basic structure of the business model to active engagement with homeowners is unlikely to come by piecemeal tinkering with the incentive structure. Indeed, some of the attempts to adjust the incentive structure of servicers have resulted in

[35]Larry Cordell, Karen Dynan, Andreas Lehnert, Nellie Liang, & Eileen Mauskopf, *The Incentives of Mortgage Servicers: Myths and Realities* 9-10 (Fed. Reserve Bd. Fin. & Econ. Discussion Series Div. Research & Statistical Affairs Working Paper No. 2008-46); State Foreclosure Prevention Working Group, Analysis of Subprime Mortgage Servicing Performance, Data Report No. 3 at 8 (2008), http://www.csbs.org/Content/NavigationMenu/Home/SFPWGReport3.pdf; Preston DuFauchard, California Department of Corporations, Loss Mitigation Survey Results 4 (Dec. 11, 2007); *cf.* Aashish Marfatia, Moody's, U.S. Subprime Market Update November 2007 at 3 (2008) (expressing concern as to servicers' abilities to meet staffing needs).
[36] Joseph R. Mason, Mortgage Loan Modification: Promises and Pitfalls 7(Oct. 3, 2007), *available at* papers.ssrn.com/sol3/papers.cfm?abstract_id=1027470.

confused and conflicting incentives, with servicers rewarded for some kinds of modifications, but not others,[37] or told both to proceed with a foreclosure and with a modification. Until recently, servicers received little if any explicit guidance on which modifications were appropriate and were largely left to their own devices in determining what modifications to make.[38] In the face of an entrenched and successful business model, fragmented oversight, and weak, inconsistent, and post hoc incentives, servicers need powerful motivation to perform significant numbers of loan modifications. Servicers clearly have not yet received such powerful motivation.

Servicers may make a little money by making a loan modification, but it will definitely cost them something. On the other hand, failing to make a loan modification will not cost the servicer any significant amount out-of-pocket, whether the loan ends in foreclosure or cures on its own. Until servicers face large and significant costs for failing to make loan modifications, until servicers are actually at risk of losing money if they fail to make modifications, no incentive to make modifications will work. What is lacking in the system is not a carrot; what is lacking is a stick.[39] Servicers must be required to make modifications, where appropriate, and the penalties for failing to do so must be certain and substantial.

C. Servicers Maximize Income in Ways that Hurt Both Homeowners and Investors.

---

[37] *See, e.g.,* Ben S. Bernanke, Chairman, Bd. of Governors of the Federal Reserve System, Speech at the Federal Reserve System Conference on Housing and Mortgage Markets: Housing, Mortgage Markets, and Foreclosures (Dec. 4, 2008), *available at* http://www.federalreserve.gov/newsevents/speech/bernanke20081204a.htm ("The rules under which servicers operate do not always provide them with clear guidance or the appropriate incentives to undertake economically sensible modifications.").

[38] American Securitization Forum, Discussion Paper on the Impact of Forborne Principal on RMBS Transactions 1 (June 18, 2009), *available at* http://www.americansecuritization.com/uploadedFiles/ASF_Principal_Forbearance_Paper.pdf.

[39] *See Helping Families Save Their Homes: The Role of Bankruptcy Law: Hearing Before the S. Comm. on the Judiciary,* 110th Cong., 2nd Sess. (Nov. 19, 2008), *available at* http://judiciary.senate.gov/hearings/testimony.cfm?renderforprint=1&id=3598&wit_id=4083 (statement of Russ Feingold, Member, Sen. Comm. on the Judiciary) ("One thing that I think is not well understood is that because of the complex structure of these securitized mortgages that are at the root of the financial calamity the nation finds itself in, voluntary programs to readjust mortgages may simply be doomed to failure.").

Servicers are designed to serve investors, not borrowers. Despite the important functions of mortgage servicers, homeowners have few market mechanisms to employ to ensure that their needs are met. Rather, in the interest of maximizing profits, servicers have engaged in a laundry list of bad behaviors, which have considerably exacerbated foreclosure rates, to the detriment of both investors and homeowners.[40]

Most servicers derive the majority of their income based on a percentage of the outstanding loan principal balance.[41] For most pools, the servicer is entitled to take that compensation from the monthly collected payments, even before the highest-rated certificate holders are paid. The percentage is set in the PSA and can vary somewhat from pool to pool, but is generally 25 basis points for prime loans and 50 basis points for subprime loans.[42] This compensation may encourage servicers to refuse principal reductions and to seek capitalizations of arrears and other modifications that increase the principal balance.

Servicers also receive fees paid by homeowners and the "float"—the interest earned on funds they are holding prior to their disbursement to the trust.[43] For many subprime servicers, late fees alone constitute a significant fraction of their total income and profit.[44] Servicers thus have an incentive to push homeowners into late payments and keep them there: if the loan pays late, the servicer is more likely to profit than if the loan is brought and maintained current. Float income encourages servicers to delay turning over payments to investors for as long as possible.

---

[40] *See* National Consumer Law Center, Foreclosures, Ch. 6 (2d ed. 2007 & Supp.) (describing the most common mortgage servicing abuses).
[41] *See, e.g.,* Ocwen Fin. Corp., Annual Report (Form 10-K), at 3 (Mar. 17, 2008) (typically receive 50 basis points annually on the total outstanding principal balance of the pool).
[42] Anthony Pennington-Cross & Giang Ho, *Loan Servicer Heterogeneity & The Termination of Subprime Mortgages* 2 (Fed. Res. Bank of St. Louis Working Paper No. 2006-024A); 26 NCLC Reports, *Follow the Money: How Servicers get Paid* May/June 2008..
[43] *See generally In re* Stewart, 391 B.R. 327, 336 (Bankr.E.D.La. 2008) (overviewing servicer compensation).
[44] *See, e.g.,* Ocwen Fin. Corp., Annual Report (Form 10-K), at 3 (Mar. 17, 2008); Kurt Eggert, *Limiting Abuse and Opportunism by Mortgage Servicers,* 15 Housing Pol'y Debate 753, 758 (2004).

For servicers, their most important asset is the value of their mortgage servicing rights. Whether or not the servicer made the correct speculative investment decision when it bought the mortgage servicing rights to a pool of mortgages does more to shape its profitability than any other single factor. A servicer's performance has only a marginal impact on the performance of the loan pool; the way a servicer increases its net worth is not by doing a top-notch job of servicing distressed mortgages but by gambling on market trends. Servicers with thin margins may need to squeeze all they can out of increasing performance from delinquent loans; servicers with stronger pools are likely to be less invested in the performance of the loans they manage.[45] This dynamic leaves many servicers indifferent to the performance of the loans they service and unmotivated to hire and train the staff needed to improve performance.

D. Servicers Have Disincentives to Perform Principal Reductions, Even When Doing So Would Benefit the Trust

Some servicers, notably Ocwen, Litton, and, to a lesser extent, Carrington, have made significant numbers of principal reductions. But other servicers—including those who are also major lenders—have not. In part, this represents nothing more than experience: Ocwen has more experience modifying loans than many other servicers. In part, it reflects the varying incentives servicers have weighing against loan modifications.

Of key importance is whether or not the loss of a principal reduction is recognized immediately or if it is delayed. Most PSAs are silent on the treatment of principal reductions or forebearance.[46] If

[45] Vikas Bajaj & John Leland, *Modifying Mortgages Can Be Tricky*, N.Y. Times, Feb. 18, 2009 (reporting views of Credit Suisse analyst that "[s]maller companies . . . that are under more financial pressure and have more experience in dealing with higher-cost loans have been most aggressive in lowering payments" than larger companies, who offer weaker modifications).
[46] *See* American Securitzation Forum, Discussion Paper on the Impact of Forborne Principal on RMBS Transactions 1 (June 18, 2009), *available at* http://www.americansecuritization.com/uploadedFiles/ASF_Principal_Forbearance_Paper.pdf.

recognition of the loss is immediate, servicers face reduced income in two ways, their monthly servicing fee and income from any subordinate tranches. Only if recognition of the loss is delayed are servicers likely to be neutral or even positive towards principal reductions.[47] This accounting nicety accounts, in part, some industry analysts believe, for the high rate of loan modifications with principal reductions performed by Ocwen in 2007.[48]

As discussed above, servicers derive the bulk of their income from the monthly servicing fee. The monthly servicing fee is set as a percentage of the outstanding loan principal balance in the pool. Once a principal write down is recognized, the outstanding principal balance of the pool declines and so does the servicer's monthly fee.

Servicers will also take a hit against their residual income if the loss is recognized immediately. Commonly, servicers also derive some income from the lowest level investment interests in the pool, called residuals.[49] Residuals represent payment of the surplus income after the senior certificate holders have been paid. If the pool shrinks, through foreclosure, prepayment, or principal reduction, or the interest rate drops on the loans in the pool due to modifications, there will be less of a surplus, and the servicer will suffer a loss. Once a pool suffers a certain level of loss, further payments out of residual income are cut off. If the loss is recognized immediately, the subordinate

[47] *See generally* American Securitzation Forum, Discussion Paper on the Impact of Forborne Principal on RMBS Transactions (June 18, 2009), available at http://www.americansecuritization.com/uploadedFiles/ASF_Principal_Forbearance_Paper.pdf (discussing impact of accounting for principal forbearance).

[48] Ocwen was apparently not recognizing the loss immediately, and thus shifting more of the pain to senior bond holders and away from the subordinate tranches. Rod Dubitsky, Larry Yang, Stevan Stevanovic, Thomas Suer, Credit Suisse, Subprime Loan Modifications Update 7-8 (2008).

[49] *See, e.g.,* Ocwen Fin. Corp., Annual Report (Form 10-K), at 20 (Mar. 17, 2008); Joseph R. Mason, Mortgage Loan Modification: Promises and Pitfalls 8 (Oct. 2007) (servicers who own residual interests always lose money when loans are modified). In some cases, the servicer may even bet against itself, by purchasing a credit default swap on the pool, in which case it makes money if there is a foreclosure. *See* Patricia A. McCoy & Elizabeth Renuart, The Legal Infrastructure of Subprime and Nontraditional Home Mortgages 36 (2008), *available at* http://www.jchs.harvard.edu/publications/finance/understanding_consumer_credit

tranches in most cases bear the entire cost.[50] Since industry practice, despite the silence in the PSAs, has now moved towards recognizing the principal write down as an immediate loss, many servicers may be doubly reluctant to write down principal, regardless of the investors' druthers.[51]

E. The Possibility of Cure Does Not Explain Servicers' Failure to Make Loan Modifications in the Current Market.

A recent paper confirms that extremely few loan modifications are being done and, in an attempt to solve the puzzle, propounds an economic model to explain the dearth of loan modifications.[52] Under the terms of that economic model, investors recover more if a borrower brings the loan current or refinances than if the lender modifies the loan. This is a commonsense and unobjectionable observation. Both the FDIC Loan Mod-in-a-Box NPV test and the HAMP NPV test build in the likelihood of cure in determining whether a loan modification or foreclosure is the more profitable path for investors.

In more normal times, it is surely rational for a servicer to spare itself the time and expense of modifying a loan in favor of the possibility of cure. In normal times, when cure rates exceeded foreclosure rates, an investor would have little objection to the wait-and-see-approach.[53] However,

---

[50] *See* American Securitzation Forum, Discussion Paper on the Impact of Forborne Principal on RMBS Transactions 3-6 (June 18, 2009), *available at* http://www.americansecuritization.com/uploadedFiles/ASF_Principal_Forbearance_Paper.pdf.

[51] *See* Rod Dubitsky, Larry Yang, Stevan Stevanovic, Thomas Suer, Credit Suisse, Subprime Loan Modifications Update 7-8 (2008).

[52] Manuel Adelino, Kristopher Gerardi & Paul S. Willen, *Why Don't Lenders Renegotiate More Home Mortgages? Redefaults, Self-Cures, and Securitization* 35 (Fed. Reserve Bank of Boston Pub. Pol'y Paper No. 09-4, July 6, 2009), *available at* http://www.bos.frb.org/economic/ppdp/2009/ppdp0904.pdf. .

[53] Alan White, *Rewriting Contracts, Wholesale: Data on Voluntary Mortgage Modifications from 2007 and 2008 Remittance Reports,* Fordham Urb. L. J. 17-18 (forthcoming 2009), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1259538#; *see also* Aashish Marfatia, Moody's, U.S. Subprime Market Update November 2007 at 5 (2008) (reporting that half of all active loans facing reset in the first three-quarters of 2007 refinanced; more than one-quarter of all remaining loans refinanced after reset); State Foreclosure Prevention Working Group, Analysis of Subprime Mortgage Servicing Performance, Data Report No. 3 at 8 (2008), http://www.csbs.org/Content/NavigationMenu/Home/SFPWGReport3.pdf (reporting that 23% of closed loss mitigation efforts in May 2008 were either refinancings or reinstatements in full by the borrower).

this model cannot explain the failure to perform loan modifications when we observe real world conditions: dropping cure rates,[54] due in part to the restricted ability to refinance, even for homeowners with high credit scores;[55] homes so deeply underwater that investors lose 65 percent of the mortgage debt on average in foreclosure;[56] and a lack of other, more attractive places, to invest funds. The study does not run actual net present value analyses on actual loans: many loans that it would not make sense to modify in a market with rising home prices, easy refinancing, and plentiful alternative investment channels do make sense, purely from the standpoint of financial return to investors, to modify in today's economic market. The paper presents no hard data on whether or not servicers, in this climate, are serving the best interests of investors in refusing to modify loans. Servicers, moreover, may have different incentives than investors, and it is not clear that servicers do always make loan modification based upon the best interests of the trust as a whole.

What we know from this study is that servicers are not making modifications. We believe that more modifications could be made that would serve the interests of both investors and homeowners, as well as the national economy. As Professor Alan White noted in his recent testimony before a House subcommittee,[57] and as the authors acknowledge,[58] there may be compelling public policy reasons to increase the number of modifications. Foreclosures impose high costs on families,

[54] Press Release, Fitch Ratings (Aug. 24, 2009).
[55] David Streitfeld, *Tight Mortgage Rules Exclude Even Good Risks,* N.Y. Times, July 10, 2009.
[56] *Home Foreclosures: Will Voluntary Mortgage Modification Help Families Save Their Homes? Hearing Before the Subcomm. on Commercial and Administrative Law of the H. Comm. on the Judiciary,* 111th Cong. (2009) (testimony of Alan M. White).
[57] *Home Foreclosures: Will Voluntary Mortgage Modification Help Families Save Their Homes? Hearing Before the Subcomm. on Commercial and Administrative Law of the H. Comm. on the Judiciary,* 111th Cong. (2009) (testimony of Alan M. White).
[58] Manuel Adelino, Kristopher Gerardi & Paul S. Willen, *Why Don't Lenders Renegotiate More Home Mortgages? Redefaults, Self-Cures, and Securitization* 8 (Fed. Reserve Bank of Boston Pub. Pol'y Paper No. 09-4, July 6, 2009), *available at* http://www.bos.frb.org/economic/ppdp/2009/ppdp0904.pdf.

neighbors, extended communities, and ultimately our economy at large.[59] It would be short-sighted indeed to fail to act.

IV. HAMP Design and Implementation Present Substantial Barriers to High Volume, High Quality Loan Modifications

HAMP has the potential to increase both the quantity and the quality of loan modifications made. By mandating a take-one, take-all policy, requiring servicers of GSE loans to modify loans, and standardizing the loan modification process, HAMP should increase the total number of modifications. By mandating affordable payments, limiting the fees charged, and permitting principal reductions, HAMP will increase the quality of the loan modifications offered. Yet the program has significant limitations both in design and implementation. HAMP's ability to guarantee an increase in sustainable modifications is dependent on voluntary servicer participation in the program. Several large servicers are still not participating, and the patchwork coverage is confusing to homeowners and their advocates alike.

More seriously, homeowners have no leverage to obtain a HAMP loan modification from even a participating servicer. It is unclear if the Administration's compliance efforts will be able to detect and remedy servicer noncompliance. Whether or not HAMP's equalization of the incentives for principal or interest rate reductions will be enough to boost the number of modifications that reduce principal also remains to be seen. Since loan modifications with principal reductions appear to have the lowest redefault rates,[60] HAMP's long-term success may be contingent on increasing the number of loan modifications with principal reductions and its great weakness in ensuring

[59] Ben S. Bernanke, Chairman, Bd. of Governors, Fed. Reserve Sys., Address at the Federal Reserve System Conference on Housing and Mortgage Markets (Dec. 4, 2008), *available at* http://www.federalreserve.gov/newsevents/speech/bernanke20081204a.htm#f12

[60] *See, e.g.,* Roberto G. Quercia, Lei Ding, Janneke Ratcliffe, *Loan Modifications and Redefault Risk: An Examination of Short-Term Impact* (Center for Community Capital, March 2009), *available at* http://www.ccc.unc.edu/documents/LM_March3_%202009_final.pdf.

sustainable modifications may be its failure to mandate principal reductions. Moreover, it is not clear that even a best case HAMP scenario is sufficient to keep up with the foreclosure crisis. The leverage missing from HAMP is directly addressed by other proposals, including judicial modifications of distressed mortgages.

A. Problems with Servicers' Implementation of HAMP Plague Homeowners Seeking Loan Modifications.

Servicers' compliance with HAMP is, at best, erratic. There is widespread violation of the HAMP guidelines across many servicers. The lack of compliance arises in part from obvious and persistent short falls in staffing and training. Yet some of the violations of HAMP are embodied in form documents, perhaps reflecting a more conscious attempt to evade the HAMP requirements. Lack of transparency prevents homeowners from identifying violations. Lack of accountability prevents homeowners from obtaining any redress when violations are identified.

1. Participating servicers violate existing HAMP guidelines.

Waivers of claims and defenses are still being required by servicers.

The HAMP rollout language prohibits waivers of legal rights. Yet servicers still are seeking waivers from homeowners or an admission of default.[61] We have learned of many instances in which servicers require homeowners to waive all claims and defenses in order to obtain a loan modification or even a loan modification review. Servicers also have asked homeowners to waive their right to a HAMP loan modification review in favor of a non-HAMP loan modification.[62] Not only does this

[61] *See* Attachment A, Ocwen Loan Servicing Loan Modification Agreement dated June 1, 2009 (seeking waiver of all legal rights by homeowner) Attachment B, Aurora Loan Services "workout agreement" dated May 20, 2009 (seeking homeowner admission of default and stating that the trial payments will not remove the homeowner from delinquency).
[62] *See, e.g.,* Attachment C (Chase Agreement seeking to obtain waiver of homeowner's right to a HAMP loan modification in favor of a non-HAMP loan modification offered prior to March 4, 2009).

violate HAMP rules but it demonstrates bad faith. Some servicers also are requiring homeowners to sign a waiver that states that any HAMP loan modification will be suspended if the homeowner subsequently files for bankruptcy.[63] These are form documents and thus unlikely to represent a random mistake by a line-level employee.

Some participating servicers offer non-compliant loan modifications.

All homeowners who request a HAMP review are entitled to one. Homeowners may elect a non-HAMP modification, but that should be the borrower's choice, informed by disclosure of all modification options.

Nonetheless, some servicers have told homeowners that they are providing a HAMP modification, only to provide documents that do not comport with the HAMP guidelines. These loan modifications are usually significantly less sustainable than a HAMP modification would be and often have higher costs. In addition to the waiver issue discussed above, advocates have been told that homeowners must pay large advance fees before a modification will be considered, homeowners have been required to complete hefty repayment plans before a review is conducted, and homeowners have been offered, as HAMP modifications, modifications limited to five years, with no limitation on interest rate increases after that time. Aurora, for example, represented to one advocate that it does not have the "right documents," although they have been publicly available for months, and so instead offered the borrowers old forms that contain waivers and are otherwise not HAMP compliant. Select Portfolio Servicing has insisted that a New York borrower make payments at a 44 percent debt-to-income ratio instead of the 31 percent mandated by HAMP.

Some participating servicers refuse to offer HAMP modifications.

[63] *See, e.g.,* Attachment D (WaMu HAMP trial plan agreement requiring waiver of HAMP loan modification if homeowner later enters bankruptcy).

The HAMP servicer contracts require that participating servicers review all homeowners in default for HAMP eligibility and that any borrower who requests a HAMP review be granted one, even if the borrower is not yet in default. Homeowners not yet in default but who are at imminent risk of default are eligible for a HAMP modification. Servicers may only refuse to perform a HAMP review if the pooling and servicing agreement (PSA) forbids modification. In that case, servicers are still expected to use all reasonable efforts to obtain an exception to the PSA.

Staff at some participating servicers routinely refuse to do HAMP loan modifications.[64] For example, in a New York case, the employee stated that the investor did not permit loan modifications, yet refused to produce a copy of the PSA or even identify the investor, much less attempt to obtain a release from the restrictions as required by HAMP. One California advocate pursuing a HAMP modification for a loan serviced by Wells Fargo was told repeatedly that the holder did not do modifications. After protracted discovery, the servicer identified the holder as Wells Fargo Home Mortgage. Wells Fargo Home Mortgage, of course, is owned by Wells Fargo Bank, a participating servicer under HAMP. In another case, a Select Portfolio Servicing representative said that the PSA prevented a HAMP modification, but could not provide the PSA due to "system errors." Other times servicers tell homeowners that they are not participating or that they are only participating for GSE loans. Bank of America has told homeowners in both Pennsylvania and Florida that it is only modifying loans that are owned by the GSEs.[65] Bank of America is a participating servicer under HAMP and therefore required to evaluate all loans for modification under HAMP. Some servicers have asserted that loans held by the GSEs require a higher debt-to-income ratio than HAMP, despite the implementation of nearly identical programs

[64] *See, e.g., Home Foreclosures: Will Voluntary Mortgage Modification Help Families Save Their Homes? Hearing Before the Subcomm. on Commercial and Administrative Law of the H. Comm. on the Judiciary*, 111th Cong. (2009) (testimony of Irwin Trauss) (Saxon Mortgage "simply reject[s] homeowners for consideration under HAMP, for no reason that is in any way connected with the program requirements, with no notice of any kind to the homeowner or to her counsel.").

[65] *See, e.g., Home Foreclosures: Will Voluntary Mortgage Modification Help Families Save Their Homes? Hearing Before the Subcomm. on Commercial and Administrative Law of the H. Comm. on the Judiciary*, 111th Cong. (2009) (testimony of Irwin Trauss).

by both Fannie Mae and Freddie Mac. Advocates in both Ohio and Florida have been driven to file court documents to compel Wells Fargo to do a HAMP review and stay foreclosure proceedings, after Wells Fargo failed to complete a HAMP review.[66]

HAMP may even be causing a drop off in loan modifications. Loan modifications rose through the first quarter of the year, but fell after HAMP's roll out in March.[67] Bank of America informed an advocate that future HAMP modifications are put on hold while Treasury reviews Bank of America's version of the Net Present Value calculation. Other advocates and homeowners have been told more generally that their servicer is participating but that the servicer does not yet have a program to evaluate homeowners for HAMP. Ocwen, for example, told an advocate on July 1 that it did not know when it would be rolling out its HAMP modifications. Ocwen signed a contract as a participating servicer on April 16, two and a half months earlier. One Brooklyn, New York advocate was told that the investor was not allowing any modifications because they were waiting for the federal government to act. In the meantime, of course, foreclosures continue.

Servicers charge fees to homeowners for the modification.

HAMP forbids any upfront payments as a precondition to review or trial modification. Several homeowners have reported being told by various servicers that they must make payments before being considered for HAMP.[68] Sometimes these payments take the form of a special forbearance agreement or lump-sum payment of arrearages; other times it is less clear what the payment is for. A Bank of America loss mitigation representative informed a Pennsylvania homeowner's counsel that if the homeowners paid $2,200.00 to Bank of America, then Bank of America would "consider"

---

66 Motion to Set Aside the Judgment, Modify the Loan, and Dismiss the Foreclosure, U.S. Bank National Ass'n as Trustee HEAT 2006-1 v. Pitman, No. 2008-CV-337 (Greene County, Ohio, 2009); Motion to Stay/Abate, Deutsche Bank Nat'l Trust Company, as Trustee for HIS Asset Securitization Trust 2007-HE1 v. Hoyne, No. 42-2009-CA-002178 (Marion County, Fla., 2009).
67 Gretchen Morgenson, *Fair Game—So Many Foreclosures, So Little Logic,* N.Y. Times, July 4, 2009
68 *See, e.g.,* Attachment A, Ocwen Loan Servicing Loan Modification Agreement dated June 1, 2009.

a loan modification. America's Servicing Company, a division of Wells Fargo Home Mortgage, told a New York borrower that only upon completion of a three month repayment plan, followed by a balloon payment of $18,000, could the borrower be considered for HAMP. Select Portfolio Servicing representatives demanded a payment in the amount of the original mortgage payment in order to enter the trial period agreement in order to demonstrate the borrower's "good faith."

Servicers are continuing to initiate foreclosures and sell homes at foreclosure sales while the HAMP review is pending.

HAMP requires that no foreclosures be initiated and no foreclosure sales be completed during a HAMP review, although existing foreclosure actions may be pursued to the point of sale. Reports from around the country indicate that servicers are routinely placing homeowners into foreclosure during a HAMP review and, far worse, selling the home at foreclosure while the homeowner is waiting on the outcome of the HAMP review.

Servicers often negotiate loan modifications on a separate track from the personnel pursuing foreclosure. This structure results in homeowners being placed in foreclosure, and being subject to a foreclosure sale, while HAMP review is occurring.

2. Servicer staffing and training still lag behind what is needed.

Homeowners encounter numerous bureaucratic barriers in attempting to negotiate a loan modification.

Homeowners' loan files are routinely lost.[69] Counselors report waits of months to hear back on review for a trial modification. In one case, Select Portfolio Services advised counsel for a New York borrower on three separate occasions over six weeks that the necessary broker price opinion had been cancelled due to "system errors" and a new request would have to be submitted. A Florida

[69] Peter S. Goodman, *Paper Avalanche Buries Plan to Stem Foreclosures,* N.Y. Times, June 28, 2009.

homeowner had his HAMP trial modification cancelled by Citimortgage for non-compliance, despite having submitted all required documents and payments as required, only to receive a HAMP solicitation letter the same day. His lawyer, in describing the situation to us, wrote, "It is driving the poor guy bananas."

To add insult to injury, homeowners are expected to return the documents within days of receipt. Homeowners in both New York and Florida have reported receiving the trial modification agreements the same day the servicer required their return. One Illinois homeowner received her trial modification agreement three days after she was required to return the agreement.

Staff of participating servicers continue to display alarming ignorance of HAMP.

Staff of participating servicers have told homeowners that HAMP does not exist. Several homeowners have reported being told to contact HUD since HAMP is a government program. HUD, of course, does not administer HAMP; participating servicers do. Bank of America apparently told the homeowners in one case that they were not eligible for HAMP because they were not in default.[70] This misinformation was given to the homeowner despite the fact that servicers are given an additional $500 incentive payment for modifying a loan prior to default. In another case, Bank of America refused to modify a first lien position home equity line of credit, apparently under the belief that modifications of home equity lines of credit were banned as second liens, whether or not they actually were junior liens.

In one case, Select Portfolio Servicing (SPS) claimed that it could only take 80% of the applicants' gross income into consideration, regardless of HAMP guidelines and that the clients would have to reduce their debt obligations by $300 to be considered for a modification. The representatives

[70] Freda R. Savana, *Some Banks Not With the Program,* Bucks County Courier Intelligencer, July 14, 2009.

appeared to be operating under SPS's standard screening process for non-HAMP modifications and were not familiar with the HAMP standards. In the same case, another SPS representative claimed that the investor on the loan would only allow for payment modifications at 44 percent debt-to-income ratio, not the 31 percent mandated by HAMP. In many cases, it is not clear if staff are applying the net present value test or if they are applying it correctly.[71]

A recent blurb from *Mortgage Servicing News Bulletin* captures the problem: "Confused About the Rescue Plan?"[72] Apparently many servicers are.

Non-participating servicers continue to represent themselves as participating in HAMP.

Some servicers give conflicting information on whether or not they participate in HAMP. American Home Mortgage Servicing, for example, conveyed on its web site, automated answering service, and through its loan modification staff that it was a participating servicer under HAMP. Yet at least some of the loan modifications it offered were not HAMP-compliant, nor is it, as of July 13, 2009, listed as a participating servicer.

3. Lack of transparency is resulting in summary denials and other unreasonable acts by servicers.

Even when servicers do a HAMP review, they sometimes use the wrong numbers, which advocates are only able to uncover after a protracted battle. In one case involving a New York borrower, Select Portfolio Servicing representatives initially advised that the clients were ineligible for a HAMP loan modification, based on their budget. When asked for clarification about the grounds for this determination, SPS representatives claimed that the clients' expenses

---

[71] *See, e.g., Home Foreclosures: Will Voluntary Mortgage Modification Help Families Save Their Homes? Hearing Before the Subcomm. on Commercial and Administrative Law of the H. Comm. on the Judiciary*, 111th Cong. (2009) (testimony of Irwin Trauss) (discussing a case involving Wells Fargo).
[72] Mortgage Servicing News Bull., July 14, 2009.

exceeded their income, making it impossible for them to afford their mortgage. Upon further discussion, it was revealed that SPS was using the clients' original mortgage payment as an input value for these calculations, rather than the proposed modified payment amount that would have made their mortgage affordable.

Some servicers are scrutinizing homeowner expenses and using back-end ratios as a basis for denying HAMP loan modifications. Back-end ratios, the ratio between all of the borrowers' fixed monthly obligations and income, should not disqualify a borrower under HAMP unless the reduced payment will cause the borrower severe financial hardship; instead, homeowners with back-end ratios above 55 percent are to be referred to HUD-certified housing counselors. In other cases, homeowners are turned down for loan modifications without any explanation.

Servicers refuse to provide the final payment amounts even when the borrower provides all verified information before the beginning of the trial modification period. In one case, three days after the servicer had supplied the borrower with the first set of trial modification documents and nearly two months after the borrower had submitted verified income information, the servicer increased the monthly payment amount, without any apparent justification.

The permanent modifications offered often include arrears that are undocumented and apparently overestimated. While HAMP permits arrearages and some fees to be capitalized, HAMP does not permit unpaid late fees to be capitalized. Given the widespread practice by servicers of padding fees in foreclosure or bankruptcy,[73] homeowners and their advocates have good reason to seek review of the legitimacy of the fees.

[73] *See, e.g., In re* Stewart, 391 B.R. 327 (Bankr. E.D. La. 2008); *In re* Sacko, 394 B.R. 90 (Bankr. E.D. Pa. 2008); *In re* Prevo, 394 B.R. 847 (Bankr. S.D. Tex. 2008); *In re* Porter, 399 B.R. 113 (Bankr. D. N.H. 2008); Katherine Porter, *Misbehavior and Mistake in Bankruptcy Mortgage Claims,* 87 Tex. L. Rev 121 (2009).

Some servicers claim they are doing a large volume of modifications for homeowners not eligible for HAMP, as well as many HAMP loan modifications. Whether or not the homeowners with the non-HAMP modifications were in fact eligible for HAMP is uncertain. As discussed above and exemplified in Attachment C, some servicers are requiring homeowners to waive their eligibility for a HAMP review in order to obtain any modification. The lack of public accountability makes it impossible to know how many of those reported as ineligible for HAMP were, in fact, ineligible, and how many were simply steered away from HAMP modifications.

In addition, determining whether or not any individual servicer is or is not participating is not trivial. As discussed above, some servicers represent themselves on their websites as participating, but fail to provide any HAMP review. As discussed below, confusion as to coverage of affiliated servicers is widespread.

B. Certain HAMP Policies Must Be Changed to Provide Sustainable Modifications and Save Communities.

1. Transparency must be improved.

The NPV model for qualifying homeowners must be available to the public.

A homeowner's qualification for a loan modification under HAMP is determined primarily through an analysis of the Net Present Value ("NPV") of a loan modification as compared to a foreclosure. The test measures whether the investor profits more from a loan modification or a foreclosure. Most investors require that servicers perform some variant of this test prior to foreclosure.[74] The outcome of this analysis depends on inputs including the homeowner's income, FICO score, current

[74] American Securitization Forum, *Statement of Principles, Recommendations and Guidelines for the Modification of Securitized Subprime Residential Mortgage Loans* (June 2007), *available at* http://www.americansecuritization.com/uploadedFiles/ASF%20Subprime%20Loan%20Modification%20Principles_060107.pdf.

default status, debt-to-income ratio, and property valuation, plus factors relating to future value of the property and likely price at resale. Participating servicers are required to apply this analysis to all homeowners who are 60 days delinquent and those at imminent risk of default. Homeowners and their advocates need access to the program to determine whether servicers have actually and accurately used the program in evaluating the homeowner's qualifications for a HAMP modification. Without access to the NPV analysis, homeowners are entirely reliant on the servicer's good faith.

The lack of NPV transparency makes servicer turndowns hard to counteract. NPV turndowns must be detailed and in writing, and based on a transparent process that conforms to HAMP guidelines.

The layers of documents governing HAMP, the guidelines, the Supplemental Directives, the various FAQ's, and the servicer contracts, should be consolidated, reconciled, and clarified.

Homeowners, their advocates, and servicers have no one source of guidance on HAMP. The initial guidelines differ slightly from the Supplemental Directives, and the FAQs provide different interpretations. All of this complicates compliance.

Participating subsidiaries must be clearly identified

Participating servicers may, but need not, require their subsidiaries to participate, so long as the subsidiary is a distinct legal entity. However, if the subsidiary is not a distinct legal entity, then the subsidiary must participate. The public list of participating servicers still does not make these distinctions clear. One example of the confusion is Wells Fargo. On financialstability.gov, Wells Fargo Bank is listed as a participating servicer. Wells Fargo Bank, N.A., is, according to the National Information Center maintained by the Federal Reserve, the parent company of Wells Fargo Home Mortgage. The contract posted on financialstability.gov variously represents the covered servicer as Wells Fargo Bank, N.A. (when giving the address for notices) and Wells Fargo Home Mortgage, a division of Wells Fargo Bank, N.A. (above the signature lines). Does this contract mean that both Wells Fargo Bank, N.A., and Wells Fargo Home Mortgage are covered? And is America's Servicing Company, a division of Wells Fargo Home Mortgage also covered? The answer to both questions appears to be yes but has not been uncontested. Asking homeowners and counselors to wade through these legal relationships invites confusion and frustration.[75]

2. Mechanisms for enforcement and compliance should be adopted.

All foreclosure proceedings must be stopped upon the initiation of a HAMP review, not just at the point before sale.

While many servicers are placing homeowners in foreclosure and proceeding to sale in violation of HAMP guidelines (as described above), even compliance with the current rule is pushing homeowners into costlier loan modifications and tilting the scales toward foreclosure. In judicial foreclosure states, servicers are aggressively pursuing foreclosures while reviewing homeowners for loan modifications. As a result, homeowners are incurring thousands of dollars in foreclosure costs. Servicers either demand these payments upfront (an apparent violation of HAMP) or capitalize the costs without permitting any review by the homeowner. In either event, these costs make it harder to provide an affordable loan modification and the continuation of the foreclosure causes homeowners great stress. All foreclosure proceedings should be stayed while HAMP reviews occur. Staying the foreclosures during the pendency of a HAMP review would encourage servicers to expedite their HAMP reviews, rather than delaying them.

Homeowners should be provided with an independent review process when denied a loan modification.

---

[75] We understand and appreciate that the Treasury Department is working on this issue. As is apparent, providing full information to the public on participating servicers is essential.

It seems unlikely that all servicers will always accurately evaluate the qualifications of every homeowner who is eligible for HAMP. Homeowners who are wrongly denied must be afforded an independent review process to review and challenge the servicer's determination that the borrower does not qualify for HAMP.

Homeowners should have access to an ombudsman to address complaints about the process.

Homeowners currently have no resource for addressing complaints, whether with a servicer's failure to return phone calls or offer of a non-compliant modification. Any forum for addressing homeowners' complaints must adhere to time lines for addressing complaints and provide public accounting as to the nature of the disputes and their resolution.

Denials based in part on a borrower's credit score should be accompanied by an adverse action notice under the Fair Credit Reporting Act.

The Fair Credit Reporting Act requires that if an adverse action in the provision of credit is taken based in part on the borrower's credit score that the borrower be advised of that adverse action and of the credit score upon which the decision was based.[76] The reason for that requirement is that credit scores often have errors, which a borrower may correct—but only if the borrower is aware of the error.

The Net Present Value test relies on credit scores to determine default and redefault rates. It is at least possible that those credit scores could result in the failure of the NPV test and the denial of a loan modification. Absent full transparency regarding the NPV calculation, homeowners are unlikely to know of the program's reliance on their FICO score or, if they do, whether or not their FICO score was the cause of their denial for a HAMP modification. An adverse action notice alerts

[76] 15 U.S.C. §1681m.

homeowners to the possibility that an incorrect FICO score—which could be corrected—might be the reason their servicer denied a HAMP modification. Without an adverse action notice homeowners have little opportunity to address any potential problems.

3. The HAMP guidelines should be adjusted to provide more meaningful relief to homeowners without reducing their existing rights.

Homeowners need principal reductions, not forbearance.

Principal forgiveness is necessary to make loan modifications affordable for some homeowners. A significant fraction of homeowners owe more than their homes are worth.[77] The need for principal reductions is especially acute – and justified – for those whose loans were not adequately underwritten and either 1) received Payment Option Adjustable Rate Mortgage loans that negatively amortize until as much as 125 percent of the original balance is owed; or 2) obtained loans that were based on inflated appraisals. As a matter of equity and commonsense, homeowners should not be trapped in debt peonage, unable to refinance or sell.

Practically, principal reductions may be key to the success of HAMP. Being "underwater" increases the risk of default, particularly when coupled with unaffordable payments.[78] Built into the HAMP NPV calculations is an assumption that default increases as a function of how far underwater the homeowner is. Existing data on loan modifications shows that loan modifications with principal

[77] *See* Renae Merle & Dina ElBoghdady, *Administration Fills in Mortgage Rescue Details,* Wash. Post, Mar. 5, 2009 (reporting that one in five homeowners with a mortgage owe more on their mortgages than their home is worth).
[78] *See, e.g.,* Kristopher Gerardi, Christopher L. Foote, & Paul S. Willen, *Negative Equity and Foreclosure: Theory and Evidence* (Fed. Reserve Bank of Boston Pub. Pol'y Paper No. 08-3 , June 2008); Andrey Pavlov & Susan Wachter, *Aggressive Lending and Real Estate Markets* (Dec. 20, 2006), *available at* http://realestate.wharton.upenn.edu/newsletter/pdf/feb07.pdf.

reductions tend to perform better.[79] In order to bring down the redefault rate and make loan modifications financially viable for investors, principal reductions must be part of the package.[80]

The Federal Reserve Board's loan modification program directly requires principal reductions for those homeowners most underwater. Under that program, principal reductions are mandated when the outstanding loan balance exceeds 125 percent of the home's current market value. Not incidentally, under the most recent revisions to the Making Home Affordable refinance program, once the mark-to-market loan-to-value ratio is 125 percent, a homeowner may refinance. Thus, once the loan value is reduced to 125 percent of current market valuation, there is, at least for some homeowners, the possibility of refinancing. While a loan-to-value ratio of 125 percent still leaves homeowners underwater and restricts their options, it gives them some hope, as it permits the possibility of refinancing or even sale, after several years of payments or subsequent to a market rebound. A reduction only to 125 percent is still sufficiently harsh that it is likely to contain any moral hazard problems, yet it puts a finite bound on the homeowner's debt peonage.

HAMP permits principal reductions, but does not mandate them, not even in the most extreme cases. HAMP does require forbearance, but only as a method for reducing payments. While forbearance provides affordable payments, it prevents a homeowner from selling or refinancing to meet a needed expense, such as roof repair or college tuition, and sets both the homeowner and the loan modification up for future failure. For all of these reasons, the HAMP guidelines should be revised so that they at least conform to the Federal Reserve Board's loan modification program by reducing loan balances to 125 percent of the home's current market value.

---

[79] Roberto G. Quercia, Lei Ding, Janneke Ratcliffe, *Loan Modifications and Redefault Risk: An Examination of Short-Term Impact* (Center for Community Capital, March 2009), *available at* http://www.ccc.unc.edu/documents/LM_March3_%202009_final.pdf.
[80] *See* Ben S. Bernanke, Chairman, Bd. of Governors, Fed. Reserve Sys., Address at the Federal Reserve System Conference on Housing and Mortgage Markets (Dec. 4, 2008), available at http://www.federalreserve.gov/newsevents/speech/bernanke20081204a.htm#f12 ("[P]rincipal write-downs may need to be part of the toolkit that servicers use to achieve sustainable mortgage modifications.").

Homeowners suffering an involuntary drop in income should be eligible for a second HAMP loan modification.

Even after a loan modification is done successfully and is performing, homeowners may still become disabled, lose their jobs, or suffer the death of a spouse. These subsequent, unpredictable events, outside the control of the homeowner, should not result in foreclosure if a further loan modification would save investors money and preserve homeownership. Foreclosing on homes where homeowners have suffered an involuntary drop in income without evaluating the feasibility of a further HAMP modification is punitive to homeowners already suffering a loss and does not serve the interests of investors.

The failure to offer a second chance modification intensifies the problems with the failure to mandate principal reductions. Homeowners who experience adverse life events often refinance or sell their homes in order to avoid a foreclosure. But both of those options are foreclosed if homeowners owe more than their homes are worth. Without a second chance at a loan modification, homeowners who are underwater at the beginning of the modification are likely to be unable to avoid foreclosure should they suffer an involuntary drop in income.

Some servicers provide modifications upon re-default as part of their loss mitigation program. This approach should be standard and mandated, and should include continued eligibility for HAMP modifications rather than only specific servicer or investor programs.

Homeowners in bankruptcy should be provided clear access to the HAMP program.

As a result of the HAMP guidelines providing servicer discretion on whether to provide homeowners in bankruptcy access to HAMP modifications, homeowners generally are being denied such modifications. In at least one instance, a servicer is reported to have refused a modification on the basis of a former bankruptcy, a clear violation of the HAMP guidance. The HAMP guidelines should provide clear guidance on instances where a loan modification should be provided to homeowners in bankruptcy. The HAMP guidelines should explicitly provide that servicers must consider a homeowner seeking a modification for HAMP even if the homeowner is a debtor in a pending bankruptcy proceeding.

Some servicers have explained their reluctance to do loan modifications in bankruptcy by citing a fear of violating the automatic stay in bankruptcy. Neither the automatic stay nor the discharge order should be a bar to offering an otherwise eligible homeowner a loan modification. HUD, in recent guidance to FHA servicers, has explicitly recognized that offering a loan modification does not violate the automatic stay or a discharge order.[81]

Servicers should be required, upon receipt of notice of a bankruptcy filing, to send information to the homeowner's counsel indicating that a loan modification under HAMP may be available. Upon request by the homeowner and working through homeowner's counsel, servicers should offer appropriate loan modifications in accordance with the HAMP guidelines prior to discharge or dismissal, or at any time during the pendency of a chapter 13 bankruptcy, without requiring relief from the automatic stay, and, in the case of a chapter 7 bankruptcy, without requiring reaffirmation of the debt. The bankruptcy trustee should be copied on all such communications. All loan modifications offered in pending chapter 13 cases should be approved by the Bankruptcy Court prior to final execution, unless the Court determines that such approval is not needed. If the homeowner is not represented by counsel, information relating to the availability of a loan modification under HAMP should be provided to the homeowner with a copy to the bankruptcy trustee. The communication should not imply that it is in any way an attempt to collect a debt.

[81] HUD Mortgagee Letter 2008-32, October 17, 2008.

Two changes to the modification rules should also be made to facilitate access for homeowners in bankruptcy. First, the payment rules should take into account the fact that payments may be passed through the bankruptcy trustee, rather than directly from homeowner to servicer. Supplemental Directive 09-03 requires that the servicer receive a payment by the end of the first month that the trial plan is in effect. If the servicer does not receive the payment, the trial modification is terminated and the homeowner is disqualified from a permanent modification under HAMP. There is often an initial lag between passing the payments from the bankruptcy trustee to the servicer; homeowners should not be penalized for a delay over which they have no control and which is occasioned solely by their exercise of their right to file bankruptcy.

Second, the modification documents should explicitly prohibit servicers from requiring homeowners to reaffirm mortgage debts. Although the guidance and supplemental directive appear to allow homeowners not to reaffirm in bankruptcy, the form modification agreement requires reaffirmation by its terms in paragraph 4E. The modification agreement should be amended to restate explicitly that the borrower does not waive any claims by entering into the modification and that no reaffirmation of the debt is required. Because reaffirmations of home mortgages have the potential to deny homeowners a fresh start, many bankruptcy judges refuse to approve them. Congress recognized this concern with an amendment to the Bankruptcy Code in 2005 that permits mortgages to be serviced in the normal course after bankruptcy even if the mortgage has not been reaffirmed. These purported reaffirmation agreements made outside the mandatory notice and review procedures of section 523(c) and (d) of the Bankruptcy Code have no effect, are not enforceable, and the government should not be involved in encouraging the practice.

Mortgages should remain assumable as between spouses, children, and other persons with a homestead interest in the property.

Federal law, the Garn-St Germain Depository Act of 1982, specifically forbids acceleration when the property is transferred from one spouse to another and permits a spouse or child to assume the mortgage obligations.[82] Such transfers are most likely to occur upon death or divorce. They may also occur in the context of domestic violence. Freddie Mac has long allowed mortgage assumptions by relatives as one method of working out delinquent mortgages.

Following these policies, the HAMP program should allow mortgages for certain homeowners to be assumable. Homeowners who have recently suffered the death of a loved one should not find themselves immediately faced with foreclosure or suddenly elevated mortgage payments.

Fair lending principles must be ensured throughout the HAMP process.

Incentive payments for pre-default homeowners are aimed at the necessary policy of ensuring that homeowners already facing hardship obtain sustainable loans, yet the additional funds for such reviews may implicate fair lending issues. The home price decline protection program may result in payments focused more on non-minority areas and should be reviewed for fair lending concerns. Servicer incentive payments based on reductions in the dollar amount of a payment also may raise fair lending considerations. Moreover, hardship affidavits and paperwork must be made available in appropriate languages to ensure wide access to the program. Data on loan modifications and applications are essential to ensuring equitable access to the program; these data must all be available as of fall 2009. Any further delay will limit transparency and delay accountability.

HAMP application procedures should better recognize and lessen the impact of exigent circumstances.

[82] 12 U.S.C. § 1701j-3(d)(6) (2008) (transfer from borrower to spouse or children); 12 U.S.C. § 1701j-3(d)(7) (2008) (transfer to spouse pursuant to divorce decree or legal separation agreement).

Aspects of the loan modification procedures, or gaps in current guidance, create hurdles for certain homeowners. For example, victims of domestic violence are unlikely to be able to obtain and should not be required to obtain their abuser's signature on loan modification documents. While predatory lending and predatory servicing can create default and an imminent risk of default, as recognized by the HAMP plan, the hardship affidavit does not contain an explicit reference to either category. Thus, at present, a loan modification would be available only to a homeowner who realizes that the fraud and predatory behavior that resulted in unreasonable levels of debt are legitimate grounds for seeking a modification and who is able to articulate and defend that categorization to a line-level employee of the servicer who may be relying in a formulaic way on the categories contained in the hardship affidavit or may be outright hostile to claims of predatory behavior.

The trial modification program should be further formalized and clarified, such that homeowners receive assurances of the terms of the permanent modification and homeowners are not put into default on their loans if they are current at the onset of the trial modification.

The trial modification program currently complicates matters for participating homeowners by increasing costs and failing to maximize the chances for long-term success. Moreover, by binding homeowners but not servicers, it may further discourage some homeowners from participating.

Payments received during the trial modification period should be applied to principal and interest, not held in suspense until the end of the trial period. Trial modification payments should be applied as if the modification, and any capitalization, occurred at the outset of the trial period, with payments allocated accordingly between principal and interest. The policy of capitalizing arrears at the end of the modification period, including any difference between scheduled and modified payments, penalizes homeowners (including those not in default at the time of the trial modification) by raising the cost of the modification and increasing the chances that some homeowners will not pass the NPV test. The use of suspense accounts and capitalizing arrears after the trial period render meaningless the term "modification" in "trial modification."

In addition, homeowners who are not delinquent at the start of the trial period and who are making payments as agreed under the trial plan currently are reported to credit bureaus as making payments under a payment plan; this may register as a black mark against their credit. Homeowners should not face decreased credit scores simply because they are seeking to attain a responsible debt load. For homeowners in bankruptcy, the new rules defining when trial payments are "current" fail to take into account the delay in initial disbursement that may occur when payments are made through the chapter 13 trustee.

Finally, homeowners need some assurance at the time of the trial modification that, if their income is as represented upon approval of the trial modification, the servicer will provide a final modification on substantially similar terms. Homeowners are bound by the trial modification; it is not clear that servicers are.

The borrower is required to sign the trial modification documents, but the servicer is not. This one-sided contract discourages some homeowners and advocates. Homeowners may decide that the costs of a trial modification—the capitalized interest, the sunk payments, the potential adverse credit reporting—are not worth the uncertain benefit of a permanent modification. Some servicers compound this problem by telling homeowners seeking modifications that they are under no obligation to offer a permanent modification. Indeed, the trial modification agreement itself, in paragraph 2F, appears to allow servicers to choose not to complete a permanent modification.

According to paragraph 2F, homeowners are not entitled to a permanent modification if the servicer fails to provide the borrower with "a fully executed copy of this Plan and the Modification Agreement." Should a servicer fail to provide the borrower with a fully executed copy, the borrower is left without a permanent modification and without any recourse, while the servicer may then retain the payments made and proceed to a foreclosure. Faced with this uneven exchange, many homeowners will rationally refuse to complete a trial modification, even if they would qualify for and benefit from a permanent modification.

The final modification agreement should make clear that the homeowners do not waive any rights nor are required to reaffirm the debt in order to enter into the modification.

Although the HAMP guidelines prohibit waiver of claims and defenses,[83] the language in paragraph 4E of the modification agreement, "[t]hat the Loan Documents are composed of duly valid, binding agreements, enforceable in accordance with their terms and are hereby reaffirmed," could be construed as a waiver of some claims, particularly claims involving fraud in the origination or execution of the documents. In addition to the problems posed by reaffirmation of the debt in bankruptcy, reaffirmation of the debt and loan documents outside of bankruptcy could be construed as a waiver of defenses to the debt. Servicers, as discussed above and demonstrated by the attachments, are seeking even stronger waivers of legal rights; the form documents should give such unauthorized behavior no shelter. The modification agreement should clearly state that the borrower does not waive any claims and defenses by entering into the agreement and that the borrower is not required to reaffirm the debt.

The second lien program should be further developed to promote coordination with first lien modifications; servicers should be required to participate in both programs.

[83] Supplemental Directive, 09-01, at 2, *available at* hmpadmin.com.

Servicers continue to express ignorance of the second lien program and widely refuse to modify second liens. For example, Bank of America told a Pennsylvania borrower that a home equity line of credit could not be modified because it was "written" as a second lien, even though it was the primary, and only, lien against the property.

Servicers will often service both the first and second liens. Frequently, servicers themselves hold the second lien. Yet often servicers refuse to address the second lien, despite the incentives in HAMP to do so. Servicers who hold second liens may prefer to gamble on a market recovery rather than accept the incentive payments under HAMP and recognize their losses now. Many servicers will choose not to participate in the second lien program absent a federal mandate.

The second lien program should work in concert with the primary lien modification program to the greatest extent possible. Only such coordination will result in maximizing the potential of the program to save homes and communities.

4. Data collection and reporting should support the best HAMP outcomes possible.

The maximum amount of data should be made available to the public, including data on a loan-by-loan basis. The data should be made available in user-friendly formats that are easy to obtain and that allow for additional and varied processing and analysis. The data should be made available on a basis as close to real time as possible. Data collected by the government and disclosed to the public, including HAMP monitoring data and other data, should enable the government and the public to compare the performance of HAMP against specific benchmarks. The data should enable the government and the public to assess the extent to which HAMP is serving equitably those most heavily targeted for high risk loans (especially African-American, Latino and older borrowers).

V. Congress Should Pass Legislation Mandating Loan Modification Offers to Qualified Homeowners Where The Modification Is Consistent with Net Present Value, as well as other measures.

Creating affordable and sustainable loan modifications for distressed homeowners is labor intensive. It is no surprise, then, that servicers continue to push homeowners away from HAMP loan modifications or delay the process substantially.

Initial data collection will make a more exact review of the HAMP program possible within the next few months. Freddie Mac already is engaged in substantial oversight. Our work nationwide on behalf of homeowners facing foreclosure and unaffordable loans tells us that many qualified homeowners are being unnecessarily turned away from HAMP, those receiving loan modifications often obtain terms quite different from HAMP, and even the HAMP-compliant modifications are limited in what they can do for homeowners with high loan principal balances.

Accordingly, Congress should mandate loan modifications where they are more profitable to investors than foreclosure. Loss mitigation, in general, should be preferred over foreclosure. H.R. 3451, recently introduced by Chairwoman Waters, reflects these basic goals by setting up standards for equitable loss mitigation and otherwise seeking to revise how servicers interact with homeowners. Congress also should enact legislation to allow bankruptcy judges to modify appropriate mortgages in distress.

VI. Conclusion

Thank you for the opportunity to testify before the Subcommittee today. The foreclosure crisis is continuing to swell. We are drowning in the detritus of the lending boom of the last decade. The need to act is great. It is clear that HAMP can not do the job on its own and thus additional steps that do not rely on voluntary measures by the mortgage industry are in order. Unless HAMP both increases its reach and mandates principal reductions, Congress should pass legislation to mandate loan modification offers to qualified homeowners prior to foreclosure where the modification is consistent with net present value, and also should allow bankruptcy judges to modify home loans in bankruptcy and consider further reforms to the servicing industry. We look forward to working with you to address the challenges that face our nation's communities.

Attachment A—Ocwen Loan Modification Agreement

Ocwen Loan Servicing, LLC
P.O.Box 785052
Orlando, Florida 32878

WWW.OCWEN.COM

June 1, 2009

[redacted]

Loan Number: [redacted]
Property Address: [redacted]

PROPOSED MODIFICATION AGREEMENT

Dear Borrower(s):

Enclosed please find a proposed modification agreement (the "Agreement") on your loan referenced above for your review and consideration.

In order to accept this modification on your loan, you must complete ALL of the following steps on or before June 12, 2009, ("Due Date"):

1. **SIGN** the bottom of the Agreement on the line(s) for the Borrower(s);.	
2. **FAX** the fully executed Agreement to:	Attention: Home Retention Department (407) 737-5693
3. **PAY** the full down payment in the amount of:	$1,281.00 *[See Payment Instructions Attached]*
4. **NEW MONTHLY PAYMENT:**	$737.82 (**which may or may not include escrow**) starting on July 1, 2009.
5. **SEND** proof of insurance coverage* (Send proof of insurance ONLY to Escrow Dept. DO NOT include the Agreement.)	Attention: Escrow Department Fax: 1-888-882-1816 E-mail:dateinsuranceinfo@ocwen.com

* Proof of insurance and the Agreement must be sent separately to the correct departments using the fax numbers provided above. Failure to send proof of insurance coverage before the Due Date will constitute acceptance of a force placed policy and agreement to pay the costs of such force placed policy, so long as all other items are complete.

Time is of the essence on this offer. If ALL of the items above are not completed by the Due Date, the Agreement shall have no force or effect and any down payment received will be returned to you. Please be advised that Ocwen Loan Servicing, LLC will not delay, postpone or otherwise stop any collection efforts until ALL of the steps above have been completed.

If you have any questions or require additional information, please contact the Home Retention Department directly at (877) 596-8580.

Sincerely,

Ocwen Loan Servicing, LLC

6348635

Ocwen Loan Servicing, LLC
P.O.Box 785052
Orlando, Florida 32878

WWW.OCWEN.COM

PAYMENT REMITTANCE INFORMATION
PLEASE DON'T FORGET TO:

1. Make checks payable to Ocwen Loan Servicing, LLC.
2. Always include your loan number with your payment.
3. The down payment must be in the form of certified funds.

OVERNIGHT DELIVERY
(Money Order & Certified Checks Only)
OCWEN LOAN SERVICING, LLC
ATTN: CASHIERING DEPARTMENT
12650 INGENUITY DRIVE
ORLANDO, FL 32826

MONEY GRAM
RECEIVER CODE: 3237
PAYABLE TO: OCWEN LOAN SERVICING, LLC
CITY: ORLANDO
STATE: FLORIDA
REFERENCE: [redacted]
AGENT LOCATER: (800) 926-9400

BY WUQC
Code City: Ocwen
State: FL
Reference: Loan #[redacted]
Attn: Home Retention Department,
Home Retention Consultant

BANK WIRE
BANK: JPMorgan Chase Bank, NA
ABA: 021000021
ACCOUNT NAME: Ocwen Financial Corporation
ACCOUNT NUMBER: 00113339999
REFERENCE: Loan Number, Property Address, and Borrower Name

Email: Transferfunds@ocwen.com with the details of the wire.

LOAN MODIFICATION AGREEMENT

Ocwen Loan Servicing, LLC ("Ocwen") is offering you this Loan Modification Agreement ("Agreement"), dated June 1, 2009, which modifies the terms of your home loan obligations as described in detail below:

A. the Mortgage, Deed of Trust, or Security Deed (the "Mortgage"), dated and recorded in the public records of CLAY County, and

B. the Note, of the same date and secured by the Mortgage, which covers the real and personal property described in the Mortgage and defined therein as the "Property", located at [redacted]

Pursuant to our mutual agreement to modify your Note and Mortgage and in consideration of the promises, conditions, and terms set forth below, the parties agree as follows:

1. You agree that the new principal balance due under your modified Note and the Mortgage will be $125,056.60. Upon modification, your Note will become contractually current; however, fees and charges that were not included in this principal balance will be your responsibility.

2. You promise to make an initial down payment in the amount of $1,281.00 on or before June 12, 2009, after which you will commence payments of principal and interest in the amount of $555.87 beginning on July 1, 2009 and continuing on the same day of each succeeding month for a five (5) year period. At the end of this period, your payment is subject to change based on paragraph 4 below.

3. Any payments due for taxes and insurance will be your responsibility in addition to the payments of principal and interest required under the terms of this modification. If this loan is currently escrowed, Ocwen will continue to collect the escrow amounts with your monthly principal and interest payment.

4. Upon Modification, the annual rate of interest charged on the unpaid principal balance of your loan will be 4.42100%. This rate will remain in effect until the end of a five (5) year period beginning with your first payment after the down payment. At the end of this period, your interest rate will be calculated according to the terms of your original loan documentation.

6348635

Ocwen Loan Servicing, LLC
P.O.Box 785052
Orlando, Florida 32878

WWW.OCWEN.COM

5. You promise to make payments of principal and interest on the same day of each succeeding month until May 1, 2036, at which time a final balloon payment in an amount equal to all remaining amounts under the Note and Modification will be due.

6. You will comply with all other covenants, agreements, and requirements of your Mortgage, including without limitation, the covenants and agreements to make all payments of taxes, insurance premiums, assessments, escrow items, impounds, and all other payments that you are obligated to make under the Mortgage, except as otherwise provided herein.

7. If you sell your property, refinance, or otherwise payoff your loan during the 12 months following the date of Modification, the Modification will be voidable at the sole option of Ocwen and all amounts owed under the obligations existing prior to the Modification will be due and owing.

8. You understand and agree that:

   (a) All the rights and remedies, stipulations, and conditions contained in your Mortgage relating to default in the making of payments under the Mortgage will also apply to default in the making of the modified payments hereunder.

   (b) All covenants, agreements, stipulations, and conditions in your Note and Mortgage will remain in full force and effect, except as herein modified, and none of the your obligations or liabilities under your Note and Mortgage will be diminished or released by any provisions hereof, nor will this Agreement in any way impair, diminish, or affect any of Ocwen's rights under or remedies on your Note and Mortgage, whether such rights or remedies arise there under or by operation of law. Also, all rights of recourse to which Ocwen is presently entitled against any property or any other persons in any way obligated for, or liable on, your Note and Mortgage are expressly reserved by Ocwen.

   (c) Any expenses incurred in connection with the servicing of your loan, but not yet charged to your account as of the date of this Agreement, may be charged to your account after the date of this Agreement.

   (d) You have no right of set-off or counterclaim, or any defense to the obligations of your Note or Mortgage.

   (e) Nothing in this Agreement will be understood or construed to be a satisfaction or release in whole or in part of your Note and Mortgage.

   (f) You agree to make and execute such other documents or papers as may be necessary or required to effectuate the terms and conditions of this Agreement which, if approved and accepted by Ocwen, will bind and inure to your heirs, executors, administrators, and assigns.

   (g) You understand that this agreement is legally binding and that it affects your rights. You confirm that you have had the opportunity to obtain, independent legal counsel concerning this Agreement and are signing this Agreement voluntarily and with full understanding of its contents and meaning.

   (h) Corrections and Omissions. You agree to execute such other and further documents as may be reasonably necessary to consummate the transactions contemplated herein or to perfect the liens and security interests intended to secure the payment of the loan evidenced by the Note.

9. BY EXECUTING THIS MODIFICATION, YOU FOREVER IRREVOCABLY WAIVE AND RELINQUISH ANY CLAIMS, ACTIONS OR CAUSES OF ACTION, STATUTE OF LIMITATIONS OR OTHER DEFENSES, COUNTERCLAIMS OR SETOFFS OF ANY KIND WHICH EXIST AS OF THE DATE OF THIS MODIFICATION, WHETHER KNOWN OR UNKNOWN, WHICH YOU MAY NOW OR HEREAFTER ASSERT IN CONNECTION WITH THE MAKING, CLOSING, ADMINISTRATION, COLLECTION OR THE ENFORCEMENT BY OCWEN OF THE LOAN DOCUMENTS, THIS MODIFICATION OR ANY OTHER RELATED AGREEMENTS.

10. BY EXECUTING THIS MODIFICATION, YOU IRREVOCABLY WAIVE ALL RIGHTS TO A TRIAL BY JURY IN ANY ACTION, PROCEEDING OR COUNTERCLAIM ARISING OUT OF OR RELATING TO THIS MODIFICATION AND ANY RELATED AGREEMENTS OR DOCUMENTS OR TRANSACTIONS CONTEMPLATED IN THIS MODIFICATION.

______________________________ ______________________________

6348635

Ocwen Loan Servicing, LLC
P.O.Box 785052
Orlando, Florida 32878

WWW.OCWEN.COM

Ocwen Loan Servicing, LLC

By: ______________________

Borrower: [redacted]

6348635

Ocwen Loan Servicing, LLC
P.O.Box 785052
Orlando, Florida 32878

WWW.OCWEN.COM

June 3, 2009

[redacted]

Loan Number: [redacted]
Property Address: [redacted]

PROPOSED MODIFICATION AGREEMENT

Dear Borrower(s):

Enclosed please find a proposed modification agreement (the "Agreement") on your loan referenced above for your review and consideration.

In order to accept this modification on your loan, you must complete ALL of the following steps **on or before** June 12, 2009, ("Due Date"):

1. **SIGN** the bottom of the Agreement on the line(s) for the Borrower(s);	
2. **FAX** the fully executed Agreement to:	Attention: Home Retention Department (407) 737-5693
3. **PAY** the full down payment in the amount of:	$287.00 *[See Payment Instructions Attached]*
4. NEW MONTHLY PAYMENT:	$94.12 (which may or may not include escrow) starting on July 1, 2009.
5. **SEND** proof of insurance coverage* (Send proof of insurance ONLY to Escrow Dept. DO NOT include the Agreement.)	Attention: Escrow Department Fax: 1-888-882-1816 E-mail:dateinsuranceinfo@ocwen.com

* Proof of insurance and the Agreement must be sent separately to the correct departments using the fax numbers provided above. Failure to send proof of insurance coverage before the Due Date will constitute acceptance of a force placed policy and agreement to pay the costs of such force placed policy, so long as all other items are complete.

Time is of the essence on this offer. If ALL of the items above are not completed by the Due Date, the Agreement shall have no force or effect and any down payment received will be returned to you. Please be advised that Ocwen Loan Servicing, LLC will not delay, postpone or otherwise stop any collection efforts until ALL of the steps above have been completed.

If you have any questions or require additional information, please contact the Home Retention Department directly at (877) 596-8580.

Sincerely,

Ocwen Loan Servicing, LLC

6348643

Ocwen Loan Servicing, LLC
P.O.Box 785052
Orlando, Florida 32878

WWW.OCWEN.COM

PAYMENT REMITTANCE INFORMATION
PLEASE DON'T FORGET TO:

1. Make checks payable to Ocwen Loan Servicing, LLC.
2. Always include your loan number with your payment.
3. The down payment must be in the form of certified funds.

OVERNIGHT DELIVERY
(Money Order & Certified Checks Only)
OCWEN LOAN SERVICING, LLC
ATTN: CASHIERING DEPARTMENT
12650 INGENUITY DRIVE
ORLANDO, FL 32826

MONEY GRAM
RECEIVER CODE: 3237
PAYABLE TO: OCWEN LOAN SERVICING, LLC
CITY: ORLANDO
STATE: FLORIDA
REFERENCE: [redacted]
AGENT LOCATER: (800) 926-9400

BY WUQC
Code City: Ocwen
State: FL
Reference: Loan [redacted]
Attn: Home Retention Department,
Home Retention Consultant

BANK WIRE
BANK: JPMorgan Chase Bank, NA
ABA: 021000021
ACCOUNT NAME: Ocwen Financial Corporation
ACCOUNT NUMBER: 00113339999
REFERENCE: Loan Number, Property Address, and Borrower Name

Email: Transferfunds@ocwen.com with the details of the wire.

LOAN MODIFICATION AGREEMENT

Ocwen Loan Servicing, LLC ("Ocwen") is offering you this Loan Modification Agreement ("Agreement"), dated June 3, 2009, which modifies the terms of your home loan obligations as described in detail below:

A. the Mortgage, Deed of Trust, or Security Deed (the "Mortgage"), dated and recorded in the public records of CLAY County, and

B. the Note, of the same date and secured by the Mortgage, which covers the real and personal property described in the Mortgage and defined therein as the "Property", located at [redacted]

Pursuant to our mutual agreement to modify your Note and Mortgage and in consideration of the promises, conditions, and terms set forth below, the parties agree as follows:

1. You agree that the new principal balance due under your modified Note and the Mortgage will be $31,082.01. Upon modification, your Note will become contractually current; however, fees and charges that were not included in this principal balance will be your responsibility.

2. You promise to make an initial down payment in the amount of $287.00 on or before June 12, 2009, after which you will commence payments of principal and interest in the amount of $94.12 beginning on July 1, 2009 and continuing on the same day of each succeeding month for a five (5) year period. At the end of this period, your payment is subject to change based on paragraph 4 below.

3. Any payments due for taxes and insurance will be your responsibility in addition to the payments of principal and interest required under the terms of this modification. If this loan is currently escrowed, Ocwen will continue to collect the escrow amounts with your monthly principal and interest payment.

4. Upon Modification, the annual rate of interest charged on the unpaid principal balance of your loan will be 2.00000%. This rate will remain in effect until the end of a five (5) year period beginning with your first payment after the down payment. At the end of this period, your interest rate will be calculated according to the terms of your original loan documentation.

6348643

Ocwen Loan Servicing, LLC
P.O.Box 785052
Orlando, Florida 32878

WWW.OCWEN.COM

5. You promise to make payments of principal and interest on the same day of each succeeding month until May 1, 2021, at which time a final balloon payment in an amount equal to all remaining amounts under the Note and Modification will be due.

6. You will comply with all other covenants, agreements, and requirements of your Mortgage, including without limitation, the covenants and agreements to make all payments of taxes, insurance premiums, assessments, escrow items, impounds, and all other payments that you are obligated to make under the Mortgage, except as otherwise provided herein.

7. If you sell your property, refinance, or otherwise payoff your loan during the 12 months following the date of Modification, the Modification will be voidable at the sole option of Ocwen and all amounts owed under the obligations existing prior to the Modification will be due and owing.

8. You understand and agree that:

   (a) All the rights and remedies, stipulations, and conditions contained in your Mortgage relating to default in the making of payments under the Mortgage will also apply to default in the making of the modified payments hereunder.

   (b) All covenants, agreements, stipulations, and conditions in your Note and Mortgage will remain in full force and effect, except as herein modified, and none of the your obligations or liabilities under your Note and Mortgage will be diminished or released by any provisions hereof, nor will this Agreement in any way impair, diminish, or affect any of Ocwen's rights under or remedies on your Note and Mortgage, whether such rights or remedies arise there under or by operation of law. Also, all rights of recourse to which Ocwen is presently entitled against any property or any other persons in any way obligated for, or liable on, your Note and Mortgage are expressly reserved by Ocwen.

   (c) Any expenses incurred in connection with the servicing of your loan, but not yet charged to your account as of the date of this Agreement, may be charged to your account after the date of this Agreement.

   (d) You have no right of set-off or counterclaim, or any defense to the obligations of your Note or Mortgage.

   (e) Nothing in this Agreement will be understood or construed to be a satisfaction or release in whole or in part of your Note and Mortgage.

   (f) You agree to make and execute such other documents or papers as may be necessary or required to effectuate the terms and conditions of this Agreement which, if approved and accepted by Ocwen, will bind and inure to your heirs, executors, administrators, and assigns.

   (g) You understand that this agreement is legally binding and that it affects your rights. You confirm that you have had the opportunity to obtain, independent legal counsel concerning this Agreement and are signing this Agreement voluntarily and with full understanding of its contents and meaning.

   (h) Corrections and Omissions. You agree to execute such other and further documents as may be reasonably necessary to consummate the transactions contemplated herein or to perfect the liens and security interests intended to secure the payment of the loan evidenced by the Note.

9. BY EXECUTING THIS MODIFICATION, YOU FOREVER IRREVOCABLY WAIVE AND RELINQUISH ANY CLAIMS, ACTIONS OR CAUSES OF ACTION, STATUTE OF LIMITATIONS OR OTHER DEFENSES, COUNTERCLAIMS OR SETOFFS OF ANY KIND WHICH EXIST AS OF THE DATE OF THIS MODIFICATION, WHETHER KNOWN OR UNKNOWN, WHICH YOU MAY NOW OR HEREAFTER ASSERT IN CONNECTION WITH THE MAKING, CLOSING, ADMINISTRATION, COLLECTION OR THE ENFORCEMENT BY OCWEN OF THE LOAN DOCUMENTS, THIS MODIFICATION OR ANY OTHER RELATED AGREEMENTS.

10. BY EXECUTING THIS MODIFICATION, YOU IRREVOCABLY WAIVE ALL RIGHTS TO A TRIAL BY JURY IN ANY ACTION, PROCEEDING OR COUNTERCLAIM ARISING OUT OF OR RELATING TO THIS MODIFICATION AND ANY RELATED AGREEMENTS OR DOCUMENTS OR TRANSACTIONS CONTEMPLATED IN THIS MODIFICATION.

6348643

Ocwen Loan Servicing, LLC
P.O.Box 785052
Orlando, Florida 32878

WWW.OCWEN.COM

Ocwen Loan Servicing, LLC

By: ______________________

Borrower: [redacted]

6348643

Attachment B—Aurora Loan Services Letter and Workout Agreement

Received Fax : May 23 2009 8:11PM Fax Station : GOLANT AND GOLANT PA p. 2

FROM :PROJEKT GROUP FAX NO. :561-272-6295 May. 23 2009 10:24PM P2

Aurora • Loan Services

LMIT 0038261699

2617 COLLEGE PARK • P.O. BOX 1706 • SCOTTSBLUFF, NE 69363-1706
PHONE: 800-550-0508 • FAX: 303-728-7648

May 20, 2009 12C

3640038261699534LM22405-20-09

[redacted]

RE: Loan No. [redacted]
Property Address: [redacted]

Dear Customer(s):

Enclosed please find two copies of a Special Forbearance Agreement which has been prepared on your behalf. Please sign, date and return one copy to Aurora Loan Services and retain the second copy for your records.

You have been conditionally approved for this Special Forbearance Agreement as a result of the information that you provided to Aurora Loan Services. Your approval for the Special Forbearance Agreement is conditional upon Aurora Loan Services verifying the information that you provided.

Please execute the attached Special Forbearance Agreement and return it along with (1) the information requested in the enclosed package; (2) the completed financial statement; and (3) your initial payment in the amount of $870.41. This payment as well as the requested information must be received in our office on or before 06/01/2009.

To expedite processing of your Special Forbearance Agreement, please fax the signed Agreement to Aurora Loan Services at 866-517-7975, and remit the initial payment via Western Union Quick Collect. When sending funds via Western Union, please use the Code City: BLUFF, NE and always include your Aurora Loan Services loan number for prompt posting to your account. Any funds received after 5:00 p.m. ET will be posted the next business day.

Certified Funds should be made payable to Aurora Loan Services. Please include your Aurora Loan Services loan number on the certified funds and mail the funds separately to our Payment Processing Center at:

Overnight Delivery Services	or	U.S. Postal Delivery Services
Aurora Loan Services		Aurora Loan Services
Attn: Cashiering Dept.		Attn: Cashiering Dept.
10350 Park Meadows Drive		P.O. Box 5180
Littleton, CO 80124		Denver, CO 80217-5180

IMPORTANT INFORMATION ON PAGE 2

Received Fax : May 23 2009 8:11PM Fax Station : GOLANT AND GOLANT PA p. 3

FROM :PROJEKT GROUP FAX NO. :561-272-6295 May. 23 2009 10:25PM P3

Aurora • Loan Services

2617 COLLEGE PARK • P.O. BOX 1706 • SCOTTSBLUFF, NE 69363-1706
PHONE: 800-550-0508 • FAX: 303-728-7648

Loan No. [redacted]

Please mail all correspondence, requested information and the executed agreement to our Servicing Center at:

Overnight Delivery Services	or	U.S. Postal Delivery Services
Aurora Loan Services Attn: Home Retention 2617 College Park Scottsbluff, NE 69361		Aurora Loan Services Attn: Home Retention P.O. Box 1706 Scottsbluff, NE 69363-1706

Not withstanding anything to the contrary contained in the Special Forbearance Agreement, the parties hereto acknowledge the effect of a discharge in bankruptcy that may have been granted to the Borrower(s) prior to the execution hereof and that the Lender may not pursue the Borrower(s) for personal liability. However, the parties acknowledge that the Lender retains certain rights, including but not limited to the right to foreclose its lien under appropriate circumstances. The parties agree that the consideration for this Agreement is Aurora Loan Services' forbearance from presently exercising its rights and pursuing its remedies under the Security Instrument as a result of the Borrower's default of its obligations there under. Nothing herein shall be construed to be an attempt to collect against the Borrower(s) personally or an attempt to revive personal liability.

Signing the attached documents in no way affects or eliminates any rights you have been given in this letter or any correspondence attached hereto.

If you have any questions, please contact one of our Home Retention Counselors at the address above or by calling 800-550-0509.

Sincerely,

Home Retention Group
Aurora Loan Services

Enclosure

Aurora Loan Services is a debt collector. Aurora Loan Services is attempting to collect a debt and any information obtained will be used for that purpose. However, if you are in bankruptcy or received a bankruptcy discharge of this debt, this communication is not an attempt to collect the debt against you personally, but is notice of a possible enforcement of the lien against the collateral property.

Received Fax : May 23 2009 8:11PM Fax Station : GOLANT AND GOLANT PA p. 4

FROM :PROJEKT GROUP FAX NO. :561-272-6295 May. 23 2009 10:25PM P4

Aurora • Loan Services

2617 COLLEGE PARK • P.O. BOX 1706 • SCOTTSBLUFF, NE 69363-1706
PHONE: 800-550-0508 • FAX: 303-728-7648

WORKOUT AGREEMENT

BY AND BETWEEN AURORA LOAN SERVICES

AND

[redacted]r

Property Address: [redacted] Loan No. [redacted]

This Workout Agreement is made May 20, 2009, by and between AURORA LOAN SERVICES ("Lender") located at 2617 College Park, Scottsbluff, NE 69361, and [redacted] (individually and collectively, "Customer").

WHEREAS, Lender is the servicing agent and/or the owner and holder of a certain Note dated 06-14-06, executed and delivered by Customer, in the original principal amount of $ 256,000 (the "Note"). The Note is secured by a mortgage, deed of trust or comparable security instrument dated 06-14-06, (the "Security Instrument"), on the property located at the address specified above (the "Property"). The Note and Security Instrument are collectively referred to as the "Loan Documents".

WHEREAS, Customer is in default under the Loan Documents, has failed to make payment of monthly installments of principal, interest, and escrow, if any, and has incurred additional expenses authorized under the Loan Documents, resulting in a total arrearage now due of $ 30,515.07, as more particularly set forth below:

Unpaid monthly payment(s) of PITI* from 07-01-08 through and including 05-20-09	$	25,906.65
Accrued Late Charges		689.92
NSF Charges		.00
Legal Fees		1,808.00
Corporate Advances**		2,110.50
Other Fees***		.00
Minus Credit (suspense balance/partial payment)		.00
Total Amount Due (the "Arrearage")	$	30,515.07

* "PITI" means the monthly payment of principal, interest, and escrows, required, for taxes and insurance premium installments.

** "Corporate Advances" include, but are not limited to, property inspection fees, property preservation fees, legal fees, foreclosure fees and costs, appraisal fees, BPO (i.e. broker price opinion) fees, title report fees, recording fees, and subordination fees.

*** "Other Fees" include, but are not limited to, short payment advances and Speed ACH fees.

Received Fax : May 23 2009 8:11PM Fax Station : GOLANT AND GOLANT PA p. 5

FROM :PROJEKT GROUP FAX NO. :561-272-6295 May. 23 2009 10:26PM P5

Aurora • Loan Services

2617 COLLEGE PARK • P.O. BOX 1706 • SCOTTSBLUFF, NE 69363-1706
PHONE: 800-550-0508 • FAX: 303-728-7648

Loan No. [redacted]

WHEREAS, as a result of Customer's default, Lender (i) has the right to accelerate, and to require Customer to make immediate payment in full, all of the sums owed under the Note and secured by the Security Instrument, (ii) has so accelerated and declared due in full all such sums, and (iii) may have already commenced foreclosure proceedings to sell the Property.

WHEREAS, as of the date of execution of the Agreement, Lender commenced Foreclosure proceedings to sell the property on 10/29/08 by legal filing in the county and state where the Property is located A Foreclosure sale has not yet been scheduled.

WHEREAS, customer has requested Lender's forbearance in exercising its rights and remedies under the default provisions of the Loan Documents and with regard to any foreclosure action that may now be pending.

WHEREAS, Customer has requested and Lender has agreed to allow Customer to repay the Arrearage pursuant to a loan work-out arrangement on the terms set forth herein.

NOW, THEREFORE, in consideration of the promises and mutual covenants herein contained, the parties hereto agree as follows:

1. Term. This Agreement shall expire on the "Expiration Date," as defined in Attachment A.

2. Lenders Forbearance. Lender shall forbear from exercising any or all of its rights and remedies now existing or arising during the term of this Agreement under the Loan Documents, provided there is no "Default", as such term is defined in paragraph 5.

3. Customer's Admissions. Customer admits that the Arrearage is correct and is currently owing under the Loan Documents, and represents, agrees and acknowledges that there are no defenses, offsets, or counterclaims of any nature whatsoever to any of the Loan Documents or any of the debt evidenced or secured thereby.

Customer admits and agrees that any and all postponements of a foreclosure sale, made during the term of this Agreement or in anticipation of this Agreement, are done by mutual consent of the Customer and Lender and that, to the extent allowed by applicable law, any such foreclosure sale may be postponed from time to time until the loan evidenced by the Note is fully reinstated or the foreclosure sale is consummated. Lender shall be under no obligation to dismiss a pending foreclosure proceeding until such time as all terms and conditions of this Agreement and Attachment A have been fully performed.

4. Terms of Workout. See Attachment A, which is made a part hereof.

Received Fax May 23 2009 8:11PM Fax Station : GOLANT AND GOLANT PA p. 6

FROM :PROJEKT GROUP FAX NO. :561-272-6295 May. 23 2009 10:26PM P6

Aurora • Loan Services

2617 COLLEGE PARK • P.O. BOX 1706 • SCOTTSBLUFF, NE 69363-1706
PHONE: 800-550-0508 • FAX: 303-728-7648

Loan No. [redacted]

5. Default. If Customer fails to make any of the payments specified in Attachment A on the due dates and in the amount stated, or otherwise fails to comply with any of the terms and conditions herein or therein (any such even hereby defined as a "Default"), Lender, at its sole option, may terminate this Agreement without further notice to Customer. In such case, all amounts that are then owing under the Note, the Security Instrument, and this Agreement shall become immediately due and payable, and Lender shall be permitted to exercise any and all rights and remedies provided for in the Loan Documents, including, but not limited to, immediate commencement of a foreclosure action or resumption of a pending foreclosure action without further notice to Customer.

6. No Waiver. Nothing contained herein shall constitute a waiver of any of all of the Lender's rights or remedies, including the right to commence or resume foreclosure proceedings. Failure by Lender to exercise any right or remedy under this Agreement or as otherwise provided by applicable law shall not be deemed to be a waiver thereof.1

7. Status of Default and Foreclosure. Customer acknowledges that if the Lender previously notified the Customer that the account was in default, that the Note and Security Instrument are accelerated and the debt evidenced by the Note is due in full, the account remains in default, such Loan Documents remain accelerated, and such debt due in full, although Customer may be entitled by law to cure such default by bringing the loan evidenced by Note current rather than paying it in full. Lender's acceptance of any payments from Customer which, individually, are less than the total amount due to cure the default described herein shall in no way prevent Lender from continuing with collection action, or require Lender to re-notify Customer of such default, re-accelerate the loan, re-issue any notice, or resume any process prior to Lender proceeding with collection action if Customer Defaults. Customer agrees that a foreclosure action if commenced by the Lender against Customer will not be withdrawn unless Lender determines to do so by applicable law. In the event Customer Defaults, the foreclosure will commence, or resume from the point at which it was placed on hold, without further notice.

8. Limited Modification. Except as otherwise provided in this Agreement, the Note and Security Instrument, and any amendments thereto, are ratified and confirmed and shall remain in full force and effect.

1 A typical example of this would be if Lender decides to accept a partial or untimely payment from Customer instead of returning such payment or terminating this Agreement as provided herein, Lender shall not be precluded from rejecting a subsequent partial or untimely payment, terminating this Agreement, or taking any other action permitted by applicable law.

Received Fax : May 23 2009 8:11PM Fax Station : GOLANI AND GOLANI PA p. 7

FROM :PROJEKT GROUP FAX NO. :561-272-6295 May. 23 2009 10:27PM P7

Aurora • Loan Services

2617 COLLEGE PARK • P.O. BOX 1706 • SCOTTSBLUFF, NE 69363-1706
PHONE: 800-550-0508 • FAX: 303-728-7648

Loan No. [redacted]

9. Application of Payments. The payments received by Lender from Customer pursuant to this Agreement shall be applied, at Lender's sole option, first to the earliest monthly payment under the Note that is due. Any amounts received by Lender that are less than the full payment under then due and owing under this Agreement shall be, at Lender's sole option, (1) returned to Customer, or (2) held by Lender in partial or suspense payment balance until sufficient sum is received by Lender to apply a full payment. If this Agreement is canceled and/or terminated for any reason, any remaining funds in this partial or suspense payment balance shall be credited towards Customer's remaining obligation owing in connection with the loan and shall not be refunded.

10. Methods of Making Payments. All payments made to Lender under this Agreement shall (i) contain the Lender's loan number shown above, (ii) unless otherwise agreed to by the Lender, be payable in certified funds by means of cashier's check, Western Union (code city: Bluff,NE) money order, or certified check, and (iii) be sent to AURORA LOAN SERVICES as specified in Attachment A. Any payment made other than strictly pursuant to the requirements of this paragraph 10 and Attachment A shall not be considered to have been received by Lender, although Lender may, in its sole discretion, decide to accept any non-conforming payment.

11. Credit Reporting. The payment status of Customer's loan in existence immediately prior to execution of this Agreement will be reported monthly to all credit reporting agencies for the duration of this Agreement and thereafter. Accordingly, Lender will report the loan subject to this Agreement as delinquent if the loan is not paid current under the Loan Documents, even if Customer makes timely payments to Lender under this Agreement. However, Lender may disclose that Customer is in a repayment or work-out plan. This Agreement does not constitute an agreement by Lender to waive any reporting of the delinquency status of loan payments.

12. Property Taxes, Insurance, and Other Amounts. If Customer's loan is not escrowed for taxes and insurance premium payments, it is Customer's responsibility to pay all property taxes, premiums for insurance, and all other amounts Customer agreed to pay as required under the terms of the Loan Documents. Customer's failure to pay property taxes, amounts owed on any senior lien security instrument, other amounts that may attain priority over the Security Instrument, or insurance premiums, in each case before their due date, shall constitute a Default hereunder.

13. The Entire Agreement. This Agreement sets forth all of the promises, covenants, agreements, conditions and understandings between the parties hereto with respect to the subject matter hereof. This Agreement supersedes all prior understandings, inducements or conditions, express or implied, oral or written, with respect thereto except as contained or referred to herein. This Agreement may not be amended, waived, discharged or terminated orally but only by an instrument in writing.

Aurora • Loan Services

2617 COLLEGE PARK • P.O. BOX 1706 • SCOTTSBLUFF, NE 69363-1706
PHONE: 800-550-0508 • FAX: 303-728-7648

Loan No. [redacted]

14. Time is of the Essence. The Customer agrees and understands that TIME IS OF THE ESSENCE as to all of the Customer's obligations under this Agreement. The grace period for monthly payments under the Loan Documents will not apply to payment under this Agreement. Therefore, the Lender must receive the payments under this Agreement on or before the Due Dates specified in Attachment A.

15. Assignment by Customer Prohibited. This Agreement shall be non-transferable by Customer. However, if the legal or beneficial interest or the servicing of this loan is transferred by Lender, this Agreement inures to the benefit of any subsequent servicer or beneficial interest holder of the Note.

16. Severability. To the extent that any word, phrase, clause, or sentence of this Agreement shall be found to be illegal or unenforceable for any reason, such word, phrase, clause, or sentence shall be modified or deleted in such a manner so as to make the Agreement, as modified, legal and enforceable under applicable law, and the balance of the Agreement or parts thereof shall not be affected thereby, the balance being construed as severable and independent; provided that no such severability shall be effective if it materially changes the economic benefit of this Agreement to either party.

17. Execution in Counterparts. This Agreement may be executed and delivered in two or more counterparts, each of which, when so executed and delivered, shall be an original, but such counterparts shall together constitute but one and the same instrument and Agreement. Facsimile signatures shall be deemed as valid as originals.

18. Customer Contact. If Customer has any questions regarding this matter, Customer should contact one of Lender's Loan Counselors at the address above or by calling 800-550-0509.

IN WITNESS HEREOF, the parties hereto have caused this Agreement to be duly executed as of the date signed.

Dated: ____________________ ____________________
[redacted] Borrower

Dated: ____________________ ____________________
[redacted] Borrower

Aurora Loan Services
Dated: ____________________ ____________________

Aurora Loan Services is a debt collector. Aurora is attempting to collect a debt and any information obtained will be used for that purpose. However, if you are in bankruptcy or received a bankruptcy discharge of this debt, this communication is not an attempt to collect the debt against you personally, but is notice of a possible enforcement of the lien against the collateral property.

EQUAL HOUSING LENDER AURORA LOAN SERVICES LLC

Aurora • Loan Services

2617 COLLEGE PARK • P.O. BOX 1706 • SCOTTSBLUFF, NE 69363-1706
PHONE: 800-550-0508 • FAX: 303-728-7648

ATTACHMENT A-STIPULATED PAYMENTS

a.1 For purposes of repayment of the Arrearage, Customer shall pay $870.41, on or before 06/01/2009. Thereafter, Customer shall pay three (3) stipulated monthly payments each in the amount of $870.41 (each, a "Plan payment"). On or before 06/01/2009 (the "Agreement Return Date"), Customer shall execute and return the Agreement, including this Attachment A, in accordance with the following instructions:

If by overnight mail service to	or if by US Postal Services to
Aurora Loan Services Attention: Home Retention 2617 College Park Scottsbluff, NE 69361	Aurora Loan Services Attention: Home Retention P.O. Box 1706 Scottsbluff, NE 69363-1706

The Agreement will be of no force and effect unless Lender receives the executed Agreement, including Attachment A, as well as the first Plan payment by the Agreement Return Date. Customer shall remit to Lender the first Plan payment, in the amount specified above, made payable to Aurora Loan Services in certified funds by means of cashier's check, money order, Western Union (code city: Bluff, NE), or certified check. All Plan payments, including the first Plan payment, shall contain the Lender's loan number shown in the Agreement and, unless otherwise agreed to by the Lender, shall be payable in certified funds as described above are to be sent to Lender's Payment Processing Center in accordance with the following instructions:

If by overnight mail service to	or if by US Postal Services to
Aurora Loan Services Attention: Cashiering Department 10350 Park Meadows Drive Littleton, CO 80124	Aurora Loan Services Attention: Cashiering Department P.O. Box 5180 Denver, CO 80217-5180

a.2 Plan payments are to be paid on or before the 1st day of every month (each, a "Due Date"). Lender must receive each Plan payment by the Due Date of each month. The Agreement shall expire on the Due Date of the last Plan payment contemplated by section a.1 above (the "Expiration Date"). At the time Customer makes the third (3rd) Plan payment under this Agreement, it shall be the Customer's responsibility to provide Aurora with accurate and complete financial information in support of the Customer's request for a loan modification or other workout option. Customer must also provide Lender with a completed Borrower's Financial Statement and proof of income (copies of Customer's two (2) most recent pay stubs) to enable Lender to properly evaluate Customer's current financial situation and the Customer's request for a loan modification or other loan workout option. Tender of the last Plan payment shall not be deemed acceptance by Aurora of a workout plan or loan modification.

Received Fax : May 23 2009 8:11PM Fax Station : GOLANT AND GOLANT PA p. 10

FROM :PROJEKT GROUP FAX NO. :561-272-6295 May. 23 2009 10:29PM P10

Aurora • Loan Services

2617 COLLEGE PARK • P.O. BOX 1706 • SCOTTSBLUFF, NE 69363-1706
PHONE: 800-550-0508 • FAX: 303-728-7648

Loan No. [redacted]

b. The aggregate Plan payment will be insufficient to pay the Arrearage. At the Expiration Date, a portion of the Arrearage will still be outstanding. Because payment of the Plan payments will not cure the Arrearage, Customer's account will remain delinquent. Upon the Expiration Date, Customer must cure the Arrearage through a full reinstatement, payment in full, loan modification agreement or other loan workout option that Lender may offer (individually and collectively, a "Cure Method.") Customer's failure to enter into a Cure Method will result in the loan being disqualified from any future Lender Home Retention Group program with respect to the loan evidenced by the Note, and regular collection activity will continue, including, but not limited to, commencement or resumption of the foreclosure process, as specified in paragraphs 5 and 7 of the Agreement.

IN WITNESS HEREOF, the parties hereto have caused this Attachment A to be duly executed as of the date signed below.

Dated: ____________________ ____________________
[redacted] Borrower

Dated: ____________________ ____________________
[redacted] Borrower

Aurora Loan Services

Dated: ____________________ By: ____________________

Title: ____________________

Aurora • Loan Services

2617 COLLEGE PARK • P.O. BOX 1706 • SCOTTSBLUFF, NE 69363-1706
PHONE: 800-550-0508 • FAX: 303-728-7648

May 20, 2009

3640038261699534LM02905-20-09

RE: Loan No. [redacted]
Borrower(s): [redacted]
Property Address: [redacted]

ITEMIZATION OF FEES, COSTS AND OTHER CHARGES

Dear Customer(s):

This Addendum supplements the Attached Letter.

Below is a detailed itemization of the unpaid fees, costs and other charges due on the above-referenced loan.

Description	Unpaid Balance
Foreclosure Fees	$1,609.50
Post Liquidation Transaction	$96.00
Property Value Fee	$405.00

Attachment C—Chase Waiver of HAMP Rights

JPMorgan Chase Bank, National Association,
successor interest to Washington Mutual Bank ("Lender")
has offered to try to qualify you for a modification (an "MHA Modification") under the Making Home Affordable Plan announced by the Obama Administration on March 4, 2009. You have declined to be considered for an MHA Modification, opting instead to go forward with the modification offer made by Lender to you prior to the March 4, 2009 announcement (the "Prior Modification").

Had you qualified for an MHA Modification, you may have been entitled to the following:

- A reduction in monthly payment to no more than 31% of documented and verified gross monthly income (DTI).
- A modification sequence requiring the Lender to first reduce the interest rate (subject to a rate floor of 2%), then if necessary extend the term or amortization of the loan up to a maximum of 40 years, and then if necessary forbearing principal to get to the 31% DTI.
- Up to $1,000 of principal reduction payments on your mortgage each year for up to five years for making your payments on time each year.

By signing below, you acknowledge that (i) you have been advised of and understand the above features of an MHA Modification, (ii) you understand and agree that Lender is not obligated to match such features in the Prior Modification, (iii) you have voluntarily declined consideration for an MHA Modification, and (iv) you have agreed to hold Lender, its successors and assigns, harmless as a result of your decision to decline consideration for an MHA Modification and enter into the Prior Modification.

Borrower Name	Date
Borrower Name	Date
Borrower Name	Date
Borrower Name	Date
Borrower Name	Date
Borrower Name	Date

First American Loan Production Services

Attachment D—WaMu HAMP Trial Plan Agreement provision requiring waiver of loan modification upon subsequent bankruptcy filing.

Page 3
Loan Number

WaMu

Washington Mutual
7255 Baymeadows Way
Jacksonville, FL 32256

TRIAL PLAN AGREEMENT

* Your loan is now due for the months of 06/09 to 06/09.
* You must send $0.00 to reduce your total delinquency.
* We must <u>receive</u> the initial payment of $922.37 along with your signed Trial Plan Agreement ("Agreement") by 07/01/09. After that, the payment schedule outlined below must be followed. If you do not make your payments on time, or if any of your payments are returned for non-sufficient funds, this Agreement will be in breach and collection and/or foreclosure activity will resume.

Your payments must be received in our office on or before the following dates:

$922.37 08/01/09
$922.37 09/01/09

Payments are subject to change due to escrow analysis and or interest rate changes, if applicable. If you are notified of a payment adjustment, please contact our office immediately so we can adjust the terms of your Agreement accordingly. If all payments are made as scheduled, we will reevaluate your application for assistance and determine if we are able to offer you a permanent workout solution to bring your loan current.

All of the original terms of your loan remain in full force and effect, unless specifically mentioned within this Agreement. If any part of this Agreement is breached, Washington Mutual has the option to terminate the Agreement and begin or resume foreclosure proceedings pursuant to your loan documents and applicable law.

You acknowledge that in the event you file a petition in bankruptcy, Washington Mutual may elect to take any and all actions necessary, including, but not limited to voiding this Agreement, filing a Motion for relief from the automatic stay or a Motion to dismiss or any permitted state law remedies, which in Washington Mutual's judgment are reasonably necessary to secure or protect our security, the value of the security and/or to enforce our rights under the original terms of your loan.

I/We agree to the above Agreement and will make payments as outlined above. I/We understand that foreclosure action can be taken if the terms of this Agreement are not met.

[redacted] Date

LA-LM036-004-B9E.5797.071006

Equal Housing Lender

TESTIMONY OF

JACK SCHAKETT

CREDIT LOSS MITIGATION STRATEGIES EXECUTIVE

BANK OF AMERICA HOME LOANS

Before the

HOUSE FINANCIAL SERVICES COMMITTEE

SUBCOMMITTEE ON HOUSING AND COMMUNITY OPPORTUNITY

WASHINGTON, DC

SEPTEMBER 9, 2009

Madame Chairwoman, Ranking Member Capito, and Members of the Committee. Thank you for the opportunity to update you on Bank of America's efforts to help responsible homeowners stay in their homes. I am Jack Schakett, Bank of America's Credit Loss Mitigation Strategies Executive. I report to Bank of America Home Loans President, Barbara Desoer, and have responsibility for foreclosure prevention programs for our mortgage servicing portfolio of nearly 14 million loans.

Bank of America is proud to be a leading partner in the Administration's Home Affordable Modification Program (HAMP) and understands and appreciates the responsibilities that come with that. We are committed to helping the Administration achieve its goal of 500,000 trial loan modifications by November 1. Bank of America is working to transition 125,000 at risk loans into trial modifications by November 1 as part of that goal. We have great momentum as demonstrated by our doubling the number of trial modifications over the course of the last month alone.

Throughout this historic downturn, Bank of America has extended credit to drive economic growth and worked to develop financial solutions for our customers. In the first six months of this year, we've helped 615,000 customers refinance into a more affordable mortgage payment. We were also one of the first lenders to leverage the Administration's Making Home Affordable Refinance program, and to date we have taken 121,000 applications and have completed refinancing under the program for more than 74,000 homeowners.

Bank of America has also been at the forefront of government and industry efforts to assist struggling homeowners. In July of 2008, Bank of America completed the purchase of Countrywide Financial Corporation at a time when that firm was at risk of failure and when its base of customers – the industry's largest – needed the strength and commitment of Bank of America to offer them solutions to sustain homeownership. Just three months later, in October 2008, we announced the creation of our National Homeownership Retention Program to help nearly 400,000 Countrywide borrowers with subprime and pay option ARM products.

Before HAMP implementation, through this program and others, Bank of America and its affiliates completed loan modifications for approximately 170,000 customers from January through July of 2009, compared with more than 230,000 for all of 2008.

We have made important progress under our programs, yet HAMP represents a watershed in loan modifications. The program applies lessons we learned in early efforts across the industry, establishes uniform national standards and provides appropriate incentives to borrowers, servicers and investors. We are confident HAMP enables servicers to help more struggling homeowners and will play a key role in stabilizing the housing markets and promoting economic recovery.

We are working hard and with a strong sense of urgency to ensure HAMP's success. We began months ago establishing an appropriate infrastructure to handle HAMP customer demand and program details. The program is now the first loan modification solution we consider in our home retention efforts. For Bank of America customers who don't qualify for the HAMP, they still benefit from the availability of multiple programs Bank of America continues to offer.

Our recent results reflect the conversion to HAMP as the centerpiece of our home retention efforts. We continue to gain momentum having doubled the number of customers with a trial modification in one month – from approximately 28,000 through July to more than 68,000 through the end of August. In that same period, we also increased the number of offers extended under HAMP to more than 135,000. These numbers reflect our loan modification activity for the entire month of August. We anticipate the August numbers that will be reported by Treasury this week will reflect less than a full month of activity.

Importantly, as we have ramped up, we placed on hold any foreclosure sale for borrowers who may be eligible for HAMP. Those holds remain in place during the time that it takes us to contact and evaluate the borrower and through the trial modification period.

As the largest servicer in America, we recognize the importance of helping our customers sustain home ownership. Significant resources have been devoted to this effort including expanding our default management staffing to more than 11,000 – a 55% increase since the beginning of the year. In addition to personnel, we have devoted substantial systems, training and other resources to our home retention efforts.

We continue to critically look at our loan modification process, and to listen to our customers, community partners, and other stakeholders about how we can improve. Three areas of particular focus right now are how we can make the process more customer-friendly, how we can more efficiently handle customer documentation, and how we can keep customers better informed throughout the process. For example, we are extending our Clarity Commitment™ to loan modifications to provide consumers greater transparency about the terms of their modified loan.

There are other obstacles we continue to confront in our efforts to help as many homeowners as possible realize the benefits of HAMP. Two of the most significant hurdles are customers not providing required financial information and a lack of borrower response to our outreach efforts. We recognize that we have an opportunity to improve our outreach efforts and are working to close this gap.

We have ramped up our outreach efforts through traditional avenues such as mail, telephone, and participation in community events. Since January, Bank of America has participated in more than 167 community outreach events in 27 states. About 50% of customers we reach at these events had no prior contact with us during the last 60 days. We recently started a nationwide door-to-door outreach campaign where we are reaching out to 50,000 customers who have received a trial modification offer but have not yet responded.

We have partnered with the National Council of La Raza, National Urban League, and the National Coalition for Asian Pacific American Community Development in the creation of the Alliance for Stabilizing Communities. And, we provided $2.5 million in funding to support this national coalition and their work to hold 40 housing rescue fairs over the next two years in 24 communities hardest hit by the foreclosure crisis.

Next week we launch a Customer Assistance Center pilot in California that will provide face-to-face counseling for customers experiencing financial difficulty. The center will be equipped to handle questions on all consumer products including loan modifications. If successful, we will expand it to more locations across the United States.

We will continue to pursue transformative initiatives that increase the number of customers receiving assistance and enhance the sustainability of the loans. As part of this, we are eager to hear and consider all ideas from public officials, community leaders and our customers.

Regrettably there are limits to what the current programs can achieve. Unemployment, lack of interest in remaining in the property and other eligibility issues are current impediments to qualifying for a HAMP modification. With unemployment still near 10%, even the most ambitious loan modification program will not be able to assist borrowers who have no ability to make a reasonable mortgage payment. To address this, we have begun exploring with the Administration methods for allowing responsible unemployed borrowers to stay in their homes. Such relief could include forbearance and temporary rate relief.

Beyond unemployment, we also frequently encounter customers with the following characteristics: 1) low-to-moderate income borrowers that have a mortgage debt-to-income ratio of less than 31%, but do not have enough discretionary income left over to cover all their other necessary expenses; 2) borrowers that can afford their mortgage payment but are unwilling to pay their mortgage debt because they believe it is in their best financial interest to walk away from their underwater mortgage; and, 3) borrowers that have run up too much other debt and are choosing to allocate funds to pay other debt instead of their mortgage. We believe the Administration should expand HAMP to cover the first group of lower income borrowers who could still benefit from this program.

Our goal is to keep as many customers in their homes as possible. Our efforts do not stop if we are unable to apply a HAMP solution. We will exhaust every other available option including our National Homeownership Retention program and other loan modification solutions, as well as short sales and deeds in lieu, when a homeowner chooses to sell their property or has no other option except foreclosure.

Bank of America is committed to driving economic growth, strengthening our communities and supporting our customers. Our pledge is to always be a responsible lender and help create successful homeowners - to ensure that our customers can enjoy their homes with confidence today and far into the future.

The entire mortgage servicing industry is racing against the clock to stem the tide of foreclosures and home loss. We fully understand the urgency and will never be satisfied that we have done enough until the country is through this difficult cycle. I am certain my colleagues in the industry would say the same. The strong focus from the Administration and the HAMP program have added substantially to our collective abilities, but we understand that we have a long way to go under very challenging circumstances. We look forward to continue working with Congress and the Administration on these important issues. I would be happy to answer any questions you might have.

TESTIMONY OF MOLLY SHEEHAN
JPMORGAN CHASE

SUBCOMMITTEE ON HOUSING AND COMMUNITY OPPORTUNITY
September 9, 2009

Chairwoman Waters, Ranking Member Capito and Members of the Subcommittee on Housing and Community Opportunity, we appreciate the opportunity to appear before you today on this most important topic of helping homeowners. We recognize that no one benefits in a foreclosure.

My name is Molly Sheehan and I work for the Home Lending Division of JPMorgan Chase as the Executive responsible for Housing Policy. Chase is one of the largest residential mortgage servicers in the United States, serving more than 10 million customers located in every state of the country with mortgage and home equity loans totaling about $1.4 trillion. We are proud to be part of one of this country's pre-eminent financial institutions with a heritage of over 200 years.

Continuing to Lend

As one of the largest residential mortgage originators in the country, we also continue to make mortgage credit available, even in these difficult times. We provide loans directly to consumers and we purchase loans from smaller lenders so they can lend to their customers. In 2009, through the end of August, Chase has made more than $106.8 billion in residential mortgage loans even though mortgage applications have declined significantly.

Keeping families in their homes

At Chase we are not only continuing to lend; we are also doing everything we can to help families meet their mortgage obligations and keep them in their homes. On a national level, Chase has been a leader in foreclosure prevention. Since 2007, Chase has continued to expand its comprehensive plan to keep families in their homes, and we have helped prevent 730,412 foreclosures. From April 6, when Chase began processing trial modifications through the Making Home Affordable (MHA) Program, through August 31st, 2009, Chase has approved 144,054 MHA trial mortgage modifications. Of these trial plans offered, 113,000 are currently active as of August 31st and borrowers are making their trial plan payments.

Together with 88,821 additional Chase loan modifications, 232,875 struggling Chase, WaMu and EMC customers have received approved trial modifications through August 31, 2009. Another 125,195 applications are currently being reviewed to see if they can be modified consistent with these program terms.

We are well under way to implementing the commitments we made in announcing our foreclosure prevention plan last October and in implementation of the Making Home Affordable Modification Program announced by President Obama this past March. In particular, we have:

- Created a dedicated website where borrowers and counselors can go for information about our programs and download the documents needed to apply for a modification. In the last six months, there have been more than 2.7 million visits to Chase's www.chase.com/myhome website
- Rolled out a dedicated customer hotline for modification inquiries that has handled almost 1.3 million calls as of August 31, 2009
- Improved our automated tool to pre-qualify borrowers for MHA which is being rolled out broadly to customer-facing staff
- Continued development of new automated tools to meet program underwriting parameters and deliver recommended solutions more efficiently to our loan counselors
- Rolled out MHA training for our staff, non profit counseling partners and borrowers attending HOPE Now outreach events – reaching hundreds of internal and external loan counselors and borrowers
- Increased staff and shifts in our call centers and improved call routing
- Added over 1,700 loan counselors in 2009, bringing the total number to 4,200
- Hired 3,700 additional mortgage operations employees to handle the unprecedented volume
- Opened 27 Chase Homeownership Centers in 11 states – three more than originally planned – where struggling borrowers around the country can meet face to face with trained counselors
- More than 42,000 borrowers have met with counselors at the centers and the CHOCs have mailed over 538,000 letters to invite Chase customers to discuss their situation with our trained counselors
- Hosted over 120 homeowner events to educate and inform homeowners about the loan modification process in just the past six months
- Engaged in strategic outsourcing arrangements to increase customer solicitations and expedite the fulfillment of trial modification packages – over 460,000 letters have been mailed
- Instituted an independent foreclosure review process to avoid preventable foreclosures
- Continued improving customer communication through status letters and dedicated call center staff to respond to status requests

- Established a Program Management Office with dedicated teams to improve our execution, ensure management focus, track progress against goals and compliance with MHA Program requirements

Our Progress in Implementation of the MHA Modification Program

We believe that Chase has made significant progress in ramping up our modification capacity since April 6 by hiring people, adding office space and investing in technology. We also clearly understand that many more families are anxious about the mortgage on their home and need to hear from us as quickly as possible. Chase is committed to do whatever we can to help homeowners who qualify for these programs.

We believe that the industry as a whole is making significant capacity investments like those made by Chase to provide assistance to as many families as possible. However, it is hard to predict specific numbers of completed trial plans and loan modifications, as much of the responsibility to complete the loan modification process rests with borrowers. After being granted relief through a trial modification, borrowers must document income, hardship, debts and other important information to enable underwriters to complete final loan modification offers that conform to MHA guidelines.

As of August 31, 2009, Chase estimates that it services approximately 417,000 loans potentially eligible under the MHA Modification Program guidelines. Estimates of the number of MHA Modification eligible borrowers will always be subject to fluctuation and change due to the influence of a variety of constantly evolving market factors affecting the housing market, including self-cure rates, seasonality, employment, local housing prices, and other economic variables.

On a weekly basis, Chase mails letters to borrowers with loans that become 50 days past due and meet basic MHA Modification eligibility criteria according to information on our servicing databases. These letters are designed to comply with investor servicing guidelines under applicable agreements, are sent using letterhead from the customer's known servicing entity and feature prominently the logo of the Making Home Affordable program.

Chase believes that servicers, investors and borrowers benefit whenever a preventable foreclosure can be avoided. Whenever the value of a loan modification (under the MHA Modification Program or the Chase Modification Program) or other foreclosure prevention technique exceeds the value of a foreclosure, it is in everyone's best interest (servicer, investor and borrower) to try to find and execute on the appropriate foreclosure prevention alternative that is consistent with applicable contractual servicing obligations.

Chase's policy is to stop foreclosure sales while reviewing a mortgage for loan modification and other foreclosure prevention steps. If a borrower does not qualify for the MHA Modification Program or the Chase Modification Program, the loan is referred to the loss mitigation department, which will consider more traditional foreclosure prevention techniques, including short sales and deeds in lieu of foreclosure.

The cornerstone of loan modifications continues to be affordability and sustainability. No one benefits from a loan modification that is unsustainable and likely to re-default. Chase has created an independent review before a loan enters the foreclosure process. This review acts as a control to ensure that all appropriate actions have been taken to attempt to avoid foreclosure. An additional pre-sale review is conducted within the appropriate business unit.

Borrowers who do not qualify for the MHA Modification Program are next considered for the Chase Modification Program, or, in the case of FHA/VA and loans owned or in securities issued by Fannie Mae or Freddie Mac, for modification or other loss mitigation programs they offer.

Our Loan Modification Programs

Last October, we expanded the loan modification alternatives Chase already offered as part of our Foreclosure Prevention program. The enhanced modification tools allow for more flexibility based on the borrower's current loan type and the borrower's specific financial situation.

Chase-owned subprime hybrid Adjustable Rate Mortgages (ARMs) scheduled to reset for the first time will remain at the initial interest rate for life of the loan. Borrowers will qualify for this program if they have a clean payment history on a hybrid ARM with an interest rate that adjusts after the first two or three years. Borrowers do not need to contact Chase to benefit from this program – the rate lock will happen automatically.

We use the ASF Fast Track program to reduce payment shock for subprime hybrid ARMs serviced but not owned by Chase and scheduled to reset for the first time. Qualifying borrowers will have their initial ARM rate frozen for five years.

Borrowers not eligible for any of the systematic modification programs described above are reviewed on case-by-case basis to determine the suitability of a modification or other foreclosure prevention approach. For example, borrowers who are only in early stage delinquency may qualify for the Early Workout Program offered by Fannie Mae.

Loan modifications under the Chase programs are evaluated by developing an estimated target affordable payment of 31% to 40% of the borrower's gross income. We use the lowest percentage for borrowers with the lowest incomes. Once the target payment is calculated for the borrower, we will test each modification option to see if it will get the borrower to an affordable payment. Concurrently, we apply a net present value (NPV) analysis to each option to determine whether the value of the modification exceeds the value expected through foreclosure. We recommend the modification option that produces both an affordable payment and a positive NPV result.

Other Foreclosure Prevention Options

Loan modifications are not the only foreclosure prevention technique used by Chase. Chase believes that a refinance into a fully-amortizing FHA- or GSE- insured loan with lower payments may be a better alternative for a number of distressed homeowners. So we offer refinance options for borrowers we believe are at risk of default or may be already delinquent, as well as provide economic incentives (such as principal forgiveness, principal forbearance or rate subsidization) required to refinance these borrowers.

In addition, Chase offers other foreclosure prevention options, such as

- Payment plans (where a borrower agrees to pay back arrearages over time),
- Deferments (where a borrower agrees to make late payments in the future),
- Borrower stipulations (where a borrower agrees to make a set of payments, often as a prelude to a modification), and
- Short-sales / settlements (a form of principal forgiveness where Chase agrees to accept less than the amount of the mortgage in exchange for the underlying property or the proceeds of the sale of the underlying property).

Although borrowers do not keep their homes in short sales and settlements, these may be appropriate solutions when the borrower has no interest in remaining in the home or simply cannot afford the home over the long term, even if payments are reduced by a modification.

We are pleased to have this opportunity to share our progress with you. We look forward to continuing to work with the members of Congress, the Administration, our federal banking regulators and our community partners in implementing these initiatives to help families, stabilize neighborhoods – and the U.S. economy.

Thank you for your attention and I would be happy to answer any questions you may have.

Respectfully submitted,

Molly Sheehan
SVP, Housing Policy
JPMorgan Chase

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410

Written Testimony of Dave Stevens
Assistant Secretary for Housing/FHA Commissioner
U.S. Department of Housing and Urban Development

"Progress of the Making Home Affordable Program: What Are the Outcomes for Homeowners and What Are the Obstacles to Success?"

Hearing before the Subcommittee on Housing and Community Opportunity
U.S. House Committee on Financial Services
September 9, 2009

Chairwoman Waters, Ranking Member Capito, and Members of the Subcommittee, thank you for the opportunity to testify on the progress that the Obama Administration is making to stabilize the U.S. housing market through the Making Home Affordable (MHA) program and other Administration efforts to provide relief to homeowners and neighborhoods suffering from the affects of the foreclosure crisis.

Making Home Affordable: Progress to Date

We are all aware that the nation is facing an unprecedented foreclosure crisis – with millions of Americans projected to lose their homes within the next few years. The Obama Administration, from its first day in office, has made reversing this decline a top priority, with a particular focus on preventing foreclosures and mitigating the impact that foreclosed and abandoned properties have on neighborhoods, communities and the broader economy. Working with the White House, Treasury Department and other key Administration agencies, HUD has played a central role in these efforts.

At the center of the Administration's response to the housing crisis is the Making Home Affordable Program, a comprehensive program to stabilize the housing markets by providing affordable refinance and modification opportunities for at-risk borrowers. The initiative includes the following two key components:

(1) **The Home Affordable Refinance Program (HARP):** HARP expands access to refinancing for families whose homes have lost value and whose mortgage payments can be reduced at today's low interest rates. It helps to address the problems faced by homeowners who made what seemed like conservative financial decisions three, four or five years ago, but who have found themselves unable to benefit from the low interest rates available today because the value of their homes have declined below that of their existing mortgages.

(2) **The Home Affordable Modification Program (HAMP)**: HAMP is providing up to $75 billion dollars, including $50 billion of funds from the Troubled Assets Relief Program (TARP), to encourage loan modifications that will provide sustainable, affordable mortgage payments for borrowers. Importantly, HAMP offers incentives to investors, lenders, servicers, and homeowners to encourage mortgage modifications.

MHA has achieved clear success in a relative short time period and there are some indications that the housing market is stabilizing with home price declines slowing. Since the launch of the program in March, [48] servicers -- representing more than [85%] of the market -- have signed contracts with the Administration. In the monthly progress report released today and detailing program activity through August, these servicers have collectively extended more than [571,000] loan modification offers and approximately [360,000] have entered the 90-day trial period which is required before the modification can become permanent, providing long-term assistance to homeowners. At the current pace, the program is well on its way to meet the goal of modifying mortgage loans for more than a half million deserving homeowners by November 1. This program is not only the largest single program of its kind, but unlike many previous loan modification efforts, the MHA program generates true affordability by ensuring that participating homeowners pay just 31 percent of their monthly income towards mortgage expenses.

In addition, since February there have been more than 2.7 million home loans refinanced, both as part of the HARP and more broadly as a result of historically low interest rates. By extending the HARP program to individuals with up to 125% loan-to-value (LTV) ratio, we expect to assist a large number of underwater borrowers who were previously unable to take advantage of the refinancing program, particularly in areas of the country that have seen larger than average drops in home prices. We expect the program to continue to ramp up in the coming months.

In addition to these MHA programs, the Administration is encouraging low mortgage rates more generally by increasing support for the Government-Sponsored Enterprises (GSEs), Fannie Mae and Freddie Mac, through an expansion of Treasury's Preferred Stock Purchase Agreements with the GSEs. To this effect, we have committed up to an additional $200 billion of capital to the GSEs.

Improving Servicer Accountability and Responsiveness

Despite the significant progress under MHA, we recognize that more needs to be done to improve the responsiveness and accountability of servicers participating in the program so that additional homeowners facing, or at risk of, foreclosure are contacted and assisted in a timely manner. . As the Chairwoman is well aware, many borrowers who are interested in modifying or refinancing their mortgages under MHA have experienced difficulties in contacting the servicers of their loans or obtaining information from the servicers. Others, having made contact with servicers, have found it difficult to shepherd their applications through the process, with instances of lost application materials, changing personnel and delays in response time.

Indeed, HUD has played a lead role in pressing the servicers to do more. Secretary Donovan along with Treasury Secretary Geithner sent a strong letter to the CEOs of all participating servicers on July 9, calling upon them to devote more resources to the program, and requiring each servicing entity to designate a senior official to serve as a liaison with the Administration and work directly with HUD and Treasury on implementation of all aspects of MHA. On July 28, I along with other senior HUD and Treasury officials, met with top executives from servicers participating in the MHA program to discuss ways to improve the effectiveness and efficiency of the program. The meeting addressed challenges to modifications, strategies for improvement, and collective goals that the servicers and Administration are committed to reaching. Servicers in attendance committed to significantly increase the rate at which they are performing loan modifications. As mentioned earlier in my testimony, this goal is to reach half a million modifications begun by November 1.

At the meeting, Administration officials also detailed plans to take three important steps to improve the program's performance: (i) public reporting results under the program based on servicer-specific performance, (ii) working with servicers to set more exacting operational metrics to measure the performance of the program, and (iii) development of a "second look" process to minimize the likelihood that applications are overlooked or that applicants are inadvertently denied a modification. No family should ever lose their home because the servicer of their mortgage took too long to tell them whether they qualified for assistance or made a mistake during their review of a homeowner's application that denied them assistance.

Servicers participating in HAMP are now being held to higher performance measurements. Servicer-specific performance details were first published on August 4 and will be made publicly available on a monthly basis. In addition, Freddie Mac has been assigned the role of giving a "second look" at the servicers' performance, as a further way of measuring success, by reviewing a sample of declined applications to make sure that eligible homeowners are not being denied. The servicer-specific data shows a wide range in terms of the performance of the various companies that are participating in the program, and the expectation is that, with the performance records now public, the servicers will increase their efforts and raise the number of borrowers they are assisting.

Evolving Nature of MHA

To respond to the changing nature and magnitude of the foreclosure crisis, we have continued to make changes and additions to the MHA program that build on the core HAMP and HARP programs over the past five months. These include:

- **Second Liens Program**. In August, the Administration released the supplemental directive providing specific implementation guidelines for the second lien program, which will help to provide a more comprehensive affordability solution for borrowers by addressing their total mortgage debt. Second mortgages can create significant challenges to helping borrowers avoid foreclosure because they can increase borrowers' monthly mortgage payments beyond affordable levels and make it difficult for borrowers to refinance or receive modifications. Up to 50% of at-risk mortgages have second liens, and many properties in foreclosure have more than one lien. Under the Second Lien Program, when a Home Affordable Modification is initiated on a first lien, servicers participating in the Second Lien Program will automatically reduce payments on the associated second lien according to a pre-set protocol. Alternatively, servicers will have the option to extinguish the second lien in return for a lump sum payment under a pre-set formula determined by Treasury, allowing servicers to utilize principal extinguishment for those borrowers where extinguishment is more appropriate. We expect those servicers that hold a substantial majority of second liens to sign contracts to participate in this program.

- **Foreclosure Alternatives Program.** Because we know that the MHA program will not reach every at-risk homeowner or prevent all foreclosures, on May 14th the Administration announced the Foreclosure Alternatives program that will provide incentives for, and encourage, servicers and borrowers to pursue short sales and deeds-in-lieu (DIL) of foreclosure in cases where the borrower is generally eligible for a MHA modification but does not qualify or is unable to complete the process. These options eliminate the need for potentially lengthy and expensive foreclosure proceedings, preserve the physical condition and value of the property by reducing the time a property is vacant, and allows the homeowners to transition with dignity to more affordable housing. The new details simplify the process of pursuing short sales and deeds-in-lieu, which will facilitate the ability of more servicers and borrowers to utilize the program. The program provides a standard process flow, standard documentation, and short performance timeframes. The final details of the program are being finalized, and will be announced as soon as completed.

- **Home Price Decline Protection Incentives**. As part of our ongoing effort to expand relief to struggling homeowners, the Administration released details of its Home Price Decline Program (HPDP) on July 28th. A component of the HAMP, HPDP provides additional incentive payments to lenders and investors for modifications on properties located in areas where home prices have recently declined. The purpose of the program is to encourage additional lender participation and HAMP modifications in areas with recent price declines by helping to offset any incremental collateral loss on modifications that do not succeed. HPDP will help ensure that borrowers in areas with recent home price declines have the opportunity to stay in their homes, thereby minimizing foreclosures, which further depress home values in affected communities.

Collectively, these efforts should signal to every American that the Obama Administration is absolutely committed to the success of the Making Home Affordable program and helping as many families as possible avoid foreclosure.

HUD's Central Role in Preventing Foreclosures and Stabilizing Neighborhoods

In addition to efforts to improve the execution of MHA, HUD is utilizing long-existing mechanisms as well as additional authority provided in recently enacted legislation to aid distressed homeowners and to address community blight resulting from foreclosed and abandoned properties.

Established FHA Loss Mitigation Efforts. Homeowners of FHA-insured loans have long been eligible for a variety of loss mitigation programs to help protect them from foreclosure. In 2008, more than 500,000 families were assisted through a variety of methods, including forbearance, partial claim, loan modification, pre-foreclosure sale, and deed-in-lieu of foreclosure. Servicers of FHA-insured loans are required to notify delinquent homeowners about the option(s) that are available to help them make their monthly payments and to implement loss mitigation efforts before they take the final step of initiating foreclosure proceedings. FHA expects that even more than 500,000 families will be protected from foreclosure in 2009 through these benefits provided by FHA insurance.

FHA-Home Affordable. When initially introduced to the public, the MHA program excluded FHA-insured mortgages and stated that FHA would develop its own stand alone program. On July 30, HUD announced final rules implementing the FHA's program -- the FHA Home-Affordable Modification Program (FHA-HAMP) -- which is an important complement to MHA and provides homeowners in default (or at-risk of imminent default) with greater opportunity to reduce their mortgage payments to sustainable level. All servicers were expected to begin offering FHA-HAMP by August 15. This new loss mitigation program was authorized under the "Helping Families Save Their Homes Act of 2009," signed into law on May 20, and allows FHA to give qualified FHA-insured borrowers the opportunity to obtain assistance under terms roughly comparable to borrowers in other segments of the market, without increasing costs to the taxpayer. This program will allow HUD to permanently reduce a family's monthly mortgage payment to an affordable level by offering a partial claim of up to 30% of the unpaid principal balance. This defers the repayment of the mortgage principal reduction through an interest-free subordinate mortgage that is not due until the first mortgage is paid off. FHA will pay an incentive to loan servicers for each FHA loan modified under this program. The implementation of this program will further the Obama Administration's efforts to stabilize the housing market by helping homeowners to stay current on their mortgages and stay in their homes, therefore preventing the destructive impact of foreclosures on families and communities.

Counseling. HUD is utilizing its vast network of counselors and other nonprofits to provide critical assistance to the record number of homeowners at-risk of foreclosure. It is estimated that more than half of all foreclosures occur without servicers and borrowers ever engaging in a discussion about potential options to prevent foreclosure. That is why we have directed HUD-approved counselors to educate homeowners about their various options, promote the MHA program in local communities, and assist distressed homeowners with navigating the system so they can reach servicers and obtain assistance to avoid foreclosure.

HUD-approved counselors are located across the nation and provide distressed homeowners with a wealth of information. The counselors provide assistance over the phone and in person to individuals seeking help with understanding the MHA program, explain options available to FHA-insured homeowners, and often work with borrowers eligible for the Administration's refinance or modification program to compile an intake package for servicers. These services are provided free of charge by nonprofit housing counseling agencies working in partnership with the federal government and funded in part by HUD and NeighborWorks® America. In addition, HUD, working with Treasury and the Homeownership Preservation Foundation, HUD encourages distressed borrowers to contact the Homeowner's HOPE Hotline at 866-995-HOPE to receive counseling and advice on avoiding foreclosures. The 24 hours a day, seven days a week hotline utilizes many HUD-approved counselors who can also help the homeowner reach and resolve issues with servicers.

Earlier this summer in Miami, the Administration launched a nationwide campaign to promote the Making Home Affordable Program in communities most in need. The campaign involves a series of outreach events to engage local housing counseling agencies, community organizations, elected officials and other trusted advisors in the target markets to build public awareness of Making Home Affordable, educate at-risk borrowers about available options, prepare borrowers to work more efficiently with their servicers and drive them to take action. HUD leverages local housing partners who are on the ground and on the front lines with at-risk borrowers to help broaden our outreach efforts and keep more people in their homes.

Lastly, we are exploring a variety of mechanisms to further encourage and enable servicers to leverage their relationships with nonprofits and other entities to help expedite the processing and approval of modification applications. HUD and Treasury are working to establish guidelines for servicers entering relationships with trusted advisors who would guide borrowers through the application process, help them prepare complete application packages, and troubleshoot if the borrower appears to have been improperly deemed ineligible for the program.

Hope for Homeowners (H4H) Program. HUD continues to work to implement new and improved program features for the H4H program authorized by the "Helping Families Save Their Homes Act of 2009." H4H was initially authorized under the Housing and Economic Recovery Act (HERA) of 2008 to provide a mechanism to help distressed homeowners refinance into FHA insured loans. The temporary program, established within the FHA, is premised on the view that preserving equity for troubled homeowners is likely to be an effective tool for helping families to keep their homes and avoid foreclosure. However, due to several obstacles to participation, including steep borrower fees and costs, complex program requirements, and lack of operational flexibility in program design, the original H4H program authorized under HERA has only served a handful of distressed homeowners. The new legislative improvements combined with the integration of H4H into the Administration's MHA program should now make the program a more attractive and less burdensome option for many more homeowners. Particularly, underwater borrowers seeking to refinance their loans and regain equity in their homes but who are not eligible to participate in GSE refinancing programs may be able to find a solution through H4H. When a borrower approaches participating servicers for assistance, the servicer will be required to offer the option for a H4H refinancing in tandem with a MHA Trial Modification option.

Neighborhood Stabilization Program (NSP). HUD recognizes that concentrated foreclosures can wreak havoc on once-stable communities and is working to insure that the nearly $6 billion appropriated by Congress for NSP plays the intended role of helping to stabilize housing markets and combat blight through the purchase and redevelopment of foreclosed and abandoned homes and residential properties. NSP was initially authorized under the Housing and Economic Recovery Act (HERA) of 2008 for the purpose of stabilizing communities that have suffered from high levels of foreclosure and abandonment. A second round of funding for NSP was authorized by the American Recovery and Reinvestment Act of 2009. HUD worked to quickly allocate the funds under NSP1 to 309 grantees in 55 states and territories and 254 selected local governments. Under NSP2, HUD allocated $1.93 billion on a competitive basis to states, local governments and non-profit organizations. NSP is starting to generate real results and is emerging as a vital resource in facilitating the transformation of foreclosed homes into affordable housing and other useful properties. HUD continues to monitor program activities, identify strategies that produce real results, and work to make program modifications that will help ensure that this funding is deployed quickly, wisely, and effectively.

Additional Challenges

The Administration continues to examine new approaches to expand the reach of the foreclosure avoidance efforts and stabilize housing markets in communities around the nation:

- HUD is working with representatives from Treasury and other Administration agencies to conduct a high level review of the Making Home Affordable Program. As the evidence suggests, the program is already having a positive effect on helping to stabilize markets. For instance, home price declines have slowed, the sale of existing and new homes have increased for five consecutive months, and homebuyer confidence is on the rise. The Administration is exploring a series of programmatic options to insure that these initial signs of stabilization are maintained and strengthen.

- Although much of the spotlight has been on the single family home mortgage foreclosures, there is increasing evidence that there are also material and growing challenges in the multifamily mortgage sector, which could have negative consequences for tenants including specific concerns stemming from under investment in over-leveraged buildings as well as s growing delinquencies. HUD has led the Administration's assessment of these developments and evaluation of possible measures that could be taken in response. . The Commercial Data Book from the Mortgage Bankers Association shows that first quarter 2009 delinquency rates among multifamily mortgages in commercial mortgage backed securities (CMBS) and held by banks and thrifts has jumped to the highest levels experienced since 1996: 1.85% for CMBS and 2.23% for bank and thrifts. This is up dramatically from first quarter 2008 when the delinquency rates were 0.48% for CMBS and 1.01% for banks and thrifts. HUD has also created an internal task force to develop a better understanding of the multifamily crisis, reached out to Treasury and the Federal Housing Finance Agency (FHFA) to explore new approaches to confront this situation, and is now completing a top to bottom review of HUD's own multifamily initiatives to identify new programmatic alternatives.

Conclusion

Once again, I would like to thank you for the opportunity to participate in today's hearing and for your continued leadership and commitment. HUD shares your concerns about the speed of progress of the Administration's efforts to address the foreclosure crisis. We are working hard to resolve issues related to the implementation of core programs and to develop new elements that improve and refine MHA. As noted earlier, recent data on modifications suggest that our efforts to hold servicers accountable are generating significant results.

As always, the Administration stands ready to explore with Congress additional ideas to aid at-risk borrowers and those that may not currently qualify for the MHA program. We are completely committed to the success of this program and to the families that rely on it.

I am happy to answer any questions you may have.

TESTIMONY OF

Paul S. Willen
Senior Economist and Policy Advisor
Federal Reserve Bank of Boston

BEFORE

The U.S. House of Representatives Committee on Financial Services
Subcommittee on Housing and Community Opportunity

Hearing on
"Progress of the Making Home Affordable Program:
What Are the Outcomes for Homeowners
and What Are the Obstacles to Success?"

September 9, 2009

Chairman Waters, Ranking Member Capito, and members of the Committee, thank you for your invitation to testify. My name is Paul Willen, and I am a Senior Economist and Policy Advisor at the Federal Reserve Bank of Boston. I come to you today, however, as a researcher and as a concerned citizen and not as a representative of the Boston Fed, the other Reserve Banks, or the Board of Governors.

Over the last two years, we have searched for policies to help troubled borrowers avoid foreclosure. In New England, we at the Boston Fed have worked with banks to set up a lending facility to help subprime borrowers refinance into prime mortgages. We brought borrowers and servicers together in large-scale Foreclosure Prevention Events that have served as a national model. In the research department, we have gathered and analyzed detailed loan-level data to help us evaluate policies to ameliorate the effects of the crisis on our communities and on the country.

In my remarks today, I would like to focus on three key aspects of the foreclosure crisis that we believe should be taken into account in designing an effective program.

The first is that an effective plan must address the problem of unemployed borrowers. Many analysts have argued that an appropriate policy response is to encourage long-term modifications to loans that are both affordable to borrowers and attractive to lenders. Such modifications will help some but they cannot help unemployed borrowers. 31 percent of an unemployed person's income – nothing – is still nothing, and a payment of zero will never be attractive to a lender. A modifications that only modestly reduces the monthly payment will never be a workable proposition for a borrower with no income.

And unemployment and other life-events like illness and divorce are not a sideshow in this crisis. Our research shows that, contrary to popular belief, life-events much more than problematic mortgages, have been at the heart of this crisis all along, even before the collapse of the labor market in the fall of 2008. This may seem counterintuitive: life-events could not explain the surge in defaults in 2007, because there was no underlying surge in unemployment or illness that year. But that view reflects a misunderstanding of the interaction of house price depreciation and life events in causing default. Foreclosures rarely occur when borrowers have positive equity, for the simple reason that a borrower is almost always better off selling if they have to leave the house anyway. Thus, detrimental life events have no effect on foreclosures when prices are rising. Consider that in 2001, Massachusetts suffered a fairly severe recession which led to a big increase in delinquencies, but the number of foreclosures actually fell to a record low, as shown in the chart I have included with my testimony (Figure 1). But when home prices fall, some borrowers can no longer profitably sell, and then the income-disrupting life-events that are always present, even in normal times take a toll. Thus we did not need to see a surge in life-events to get a surge in foreclosures, but rather a fall in house prices – which is exactly, and unfortunately, what we saw.

The second policy-related finding from our research is that it is unlikely that a modest financial nudge to servicers will lead to millions of modifications that will help millions of worthy borrowers. In a recent paper, we showed that in the period 2005-2008, lenders gave payment-reducing modifications to only 3 percent of seriously delinquent borrowers. In addition, we showed that this did not result from contractual issues related to securitization: lenders were just as reluctant to modify loans when they owned them as when they serviced them for the securitization trusts. We argued that the main reason we see so few modifications is that it simply isn't profitable for lenders. I'm using lenders loosely here to mean the bearers of the loss – the investors – or their appointed representatives – the servicers. The reason is that lenders face two risks that can make modification a losing proposition. The first, which has been recognized as an issue by many observers and researchers, is "redefault risk" – the possibility that the borrower who receives a modification will default again, and thus the modification will have only served to postpone foreclosure and increase the loss to the investor as house prices fall and the home itself deteriorates. The second risk, which has been largely ignored, is "self-cure risk" – the possibility that the borrower would have repaid the loan without any assistance from the lender. About a third of the borrowers in our large sample are current on their mortgages or prepay a year after they become sixty days delinquent. An investor would view assistance given to such a borrower as "wasted" money. Some have suggested that our estimates overstate self-cure risk but we would argue the opposite: the borrowers most likely to benefit from, for example, a twenty-percent cut in payments are borrowers without substantial income loss or deep negative equity and are thus the ones most likely to cure without assistance from the lender.[1]

The third result from our research is that policymakers need to exercise care in designing foreclosure prevention policies that provide the right incentive to borrowers and servicers. A program that offers monetary incentives to do as many modifications as possible and to minimize the probability that modified loans redefault may not in fact prevent many foreclosures. To see why, one must realize that the easiest way to ensure that a borrower doesn't redefault is to choose a borrower who was unlikely to default in the first place. Thus a servicer could make minor modifications to millions of loans to perfectly creditworthy borrowers, collect large sums from the government and then collect even more as the borrowers continue to repay the loan. Anecdotal evidence from borrower testimonials suggest that individual loan officers have engaged in precisely this practice.

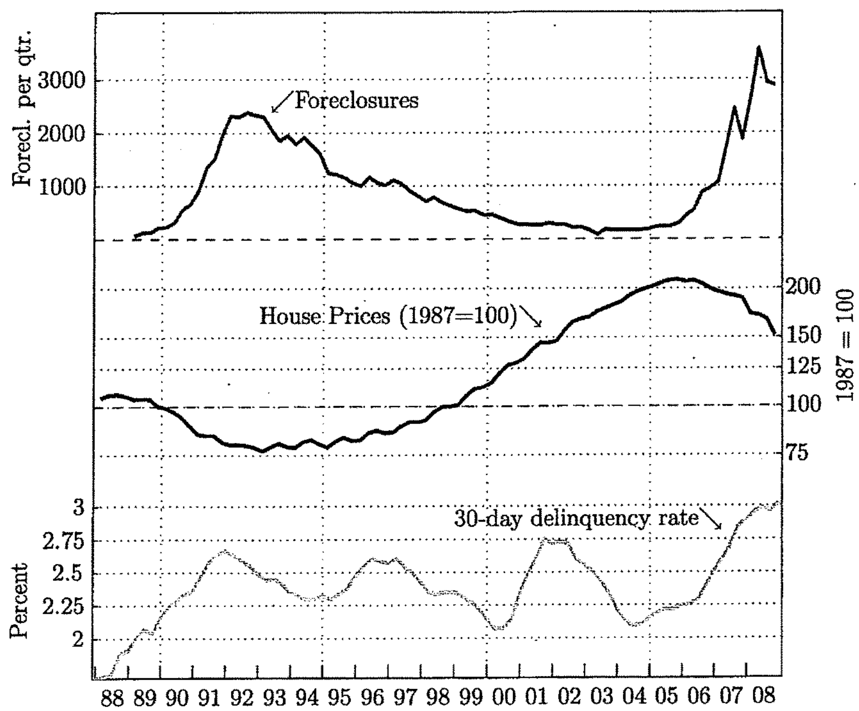
Taking these research results into account we believe that the most effective use of government money for foreclosure prevention would involve direct assistance to borrowers rather than to servicers. We believe that a plan that targets the unemployed to help them to cover their housing expenses until they get their feet back on the ground would prevent large numbers of foreclosures. Several Federal Reserve colleagues and I have written a proposal that involves grants or loans to unemployed borrowers, and researchers at the University of Wisconsin have a proposal that offers housing assistance to all victims of unemployment, whether they own or rent. Both plans get assistance to temporarily unemployed borrowers and avoid the incentive problems that I have just highlighted. Either plan would be a good starting point for an effective foreclosure relief plan.

We hope that these findings add perhaps unexpected insights to your work as policymakers. Thank you again for the opportunity to appear before you today. I

[1]See attached, Adelino, M., K. Gerardi and P. Willen. "Why Don't Lenders Renegotiate More Home Mortgages? Redefaults, Self-Cures and Securitization." FRBB PPDP 09-04, July 2009.

would of course be happy to address any questions you might have.

Figure 1: Massachusetts House Price Growth, Foreclosures and Delinquencies, January 1989 to December 2008



Public Policy
Discussion Papers

FEDERAL RESERVE BANK OF BOSTON

No. 09-4

Why Don't Lenders Renegotiate More Home Mortgages? Redefaults, Self-Cures, and Securitization

Manuel Adelino, Kristopher Gerardi, and Paul S. Willen

Abstract:
We document the fact that servicers have been reluctant to renegotiate mortgages since the foreclosure crisis started in 2007, having performed payment-reducing modifications on only about 3 percent of seriously delinquent loans. We show that this reluctance does not result from securitization: servicers renegotiate similarly small fractions of loans that they hold in their portfolios. Our results are robust to different definitions of renegotiation, including the one most likely to be affected by securitization, and to different definitions of delinquency. Our results are strongest in subsamples in which unobserved heterogeneity between portfolio and securitized loans is likely to be small, and for subprime loans. We use a theoretical model to show that *redefault risk*, the possibility that a borrower will still default despite costly renegotiation, and *self-cure risk*, the possibility that a seriously delinquent borrower will become current without renegotiation, make renegotiation unattractive to investors.

JEL Classifications: D11, D12, G21

Manuel Adelino is a Ph.D. candidate in financial economics at MIT and a graduate fellow in the research department of the Federal Reserve Bank of Boston. Kristopher Gerardi is a research economist and assistant policy adviser in the economic group in the research department at the Federal Reserve Bank of Atlanta. Paul Willen is a senior economist and policy advisor in the research department of the Federal Reserve Bank of Boston. Their email addresses are: madelino@mit.edu, kristopher.gerardi@atl.frb.org, and paul.willen@bos.frb.org.

We thank John Campbell, Chris Foote, Anil Kashyap, Chris Mayer, Julio Rotemberg, and seminar audiences at Freddie Mac, Harvard Business School, University of Connecticut, LSE, and the MIT Finance Lunch for thoughtful comments. We thank Studienzentrum Gerzensee, where the authors completed this paper, for their gracious hospitality.

This paper, which may be revised, is available on the web site of the Federal Reserve Bank of Boston at http://www.bos.frb.org/economic/ppdp/2008/ppdp0904.htm.

version of: July 6, 2009

1 Introduction

Many commentators have attributed the severity of the foreclosure crisis in the United States in the 2007–2009 period to the unwillingness of lenders to renegotiate mortgages, and, as a consequence, have placed renegotiation at the heart of the policy debate. Every major policy action to date has involved encouraging lenders, in one way or another, to renegotiate loan terms in order to reduce borrower debt loads. According to the Treasury-sponsored HopeNow initiative, in December of 2007 lenders were expected to prevent adjustable-rate mortgages from increasing to higher rates at the first reset of the mortgage.[1] "Hope For Homeowners," enacted by Congress in July of 2008, envisioned that lenders would write off a substantial portion of the principal balance of mortgages for financially distressed households.[2] The Obama Adminstration's Making Home Affordable Plan, announced in February of 2009, provided financial incentives to servicers to renegotiate loans on the condition that the lenders reduce the interest rate for a significant period of time.[3]

The appeal of renegotiation to policy makers is simple to understand. If a lender makes a concession to a borrower by, for example, reducing the principal balance on the loan, it can prevent a foreclosure. This is clearly a good outcome for the borrower, and possibly good for society as well. But the key to the appeal of renegotiation is the belief that it can also benefit the lender, as the lender loses money only if the reduction in the value of the loan exceeds the loss the lender would sustain in a foreclosure. In short, according to proponents, renegotiation of home mortgages is a type of public policy holy grail, in that it helps both borrowers and lenders at little or no cost to the government.[4]

In this paper, we explore the renegotiation of home mortgages using a dataset from Lender Processing Services (LPS), a large, detailed sample of residential mortgages. Our primary empirical analysis involves following borrowers over the year subsequent to their first serious delinquency and counting the frequency of renegotiation.[5] Measuring renegotiation in the LPS data is a challenge because there is no field in the data that identifies whether or not a servicer has changed the terms of, or "modified," the loan. We overcome this difficulty by developing an algorithm to identify modifications that we validate on an unrelated dataset that includes a modification flag.

We explore several different definitions of renegotiation in the data. Our first definition of "renegotiation" is concessionary modifications that serve to reduce a borrower's monthly

[1]Edmund L. Andrews, In Mortgage Plan, Lenders Set Terms, *New York Times*, Dec. 7, 2007.

[2]"Bush Signs Wide-Ranging Housing Bill Into Law," *Wall Street Journal*, July 31, 2008.

[3]See "$275 Billion Plan Seeks To Address Crisis In Housing," *New York Times*, Feb. 18, 2009.

[4]See this discussion in Congressional Oversight Panel (2009), Zingales (2008), and Geanakoplos and Koniak (2008), as examples.

[5]Until 2008, the dataset was known as McDash.

payment. These may be reductions in the principal balance or interest rate, extensions of the term, or combinations of all three. This definition of renegotiation is a key focus of our analysis because there is a consensus among many market observers that concessionary modifications are the most, or possibly the only, effective way of preventing foreclosures. As the Congressional Oversight Panel (COP) for the Troubled Asset Recovery Program (TARP) has written, "Any foreclosure mitigation plan must be based on a method of modifying or refinancing distressed mortgages into affordable ones. Clear and sustainable affordability targets achieved through interest rate reductions, principal write-downs, and/or term extensions should be a central component of foreclosure mitigation."[6]

Because the pooling and servicing agreements (PSAs), which govern the conduct of servicers when loans are securitized, often place limits on the number of modifications a servicer can perform, we broaden our definition of renegotiation to include any modification, regardless of whether it lowers the borrower's payment. Modifications are often thought to always involve concessions to the borrower, but many, and in some subsets most, modifications involve the capitalization of arrears into the balance of the loan, and thus lead to increased payments.

Finally, we attempt to include in our definition of renegotiation the transactions whereby lenders allow borrowers to extinguish their liabilities by repaying less than the outstanding balance of the loan. These transactions are known as short payoffs, short sales, or deeds-in-lieu of foreclosure, depending on the structure. We measure this component of renegotiation by counting the number of seriously delinquent loans that the servicer reports as "paid off."

No matter which definition of renegotiation we use, one message is quite clear: lenders rarely renegotiate. Fewer than 3 percent of the seriously delinquent borrowers in our sample received a concessionary modification in the year following the first serious delinquency. More borrowers received modifications under our broader definition, but the total still accounted for fewer than 8 percent of the seriously delinquent borrowers. And finally, fewer than 5 percent of all of our troubled borrowers repaid their mortgages, putting an upper bound on the number who could have repaid less than the principal balance of the loan. These numbers are small both in absolute terms, and relative to the approximately half of the sample for whom foreclosure proceedings were initiated, and the nearly 30 percent for whom they were also completed.

We next turn to the question of why renegotiation is so rare. If the logic described in the second paragraph is correct, lenders should find renegotiation attractive, even in the

[6]See the Congressional Oversight Panel (2009). This view is widely held and is the main focus of the Administration's Making Home Affordable foreclosure prevention plan was to encourage servicers to modify loans to reduce monthly payments to 31 percent of income.

absence of government prodding. Yet, we observe very little renegotiation in the data. We address this apparent paradox.

The leading explanation attributes the reluctance of lenders to renegotiate to the process of securitization.

> The complex webs that securitization weaves can be a trap and leave no one, not even those who own the loans, able effectively to save borrowers from foreclosure. With the loan sliced and tranched into so many separate interests, the different claimants with their antagonistic rights may find it difficult to provide borrowers with the necessary loan modifications, whether they want to or not. In the tranche warfare of securitization, unnecessary foreclosures are the collateral damage. (Eggert 2007)

More precise institutional evidence appears to confirm the role of securitization in impeding renegotiation. As mentioned in more detail below, PSAs do sometimes place global limits on the number of modifications a servicer can perform for a particular pool of mortgages. In addition, the rules by which servicers are reimbursed for expenses may provide a perverse incentive to foreclose rather than modify. Furthermore, because servicers do not internalize the losses on a securitized loan, they may not behave optimally. Another issue is the possibility that those investors whose claims are adversely affected by modification will take legal action. Finally, historically, SEC rules have stated that contacting a borrower who is fewer than 60-days delinquent constitutes an ongoing relationship with the borrower and jeopardizes the off-balance sheet status of the loan.

But some market observers express doubts about the renegotiation-limiting role of securitization. Hunt (2009) conducted an exhaustive review of a sample of PSAs and concluded, "it appears that large-scale modification programs may be undertaken without violating the plain terms of PSAs in most cases." Although some servicers have expressed concern about lawsuits, of the more than 800 lawsuits filed by investors in subprime mortgages through the end of 2008, not one involved the right of a servicer to modify a loan.[7] Even the Congressional Oversight Panel (2009), which did view securitization as a problem in general, conceded, "The specific dynamics of servicer incentives are not well understood." Finally, the SEC ruled in 2008 that if default was "reasonably forseeable," then contact with a borrower prior to 60-day delinquency would not affect the accounting status of the loan.

Our empirical analysis provides strong evidence against the role of securitization in preventing renegotiation. The LPS dataset includes loans that are serviced for private securitization trusts that are not sponsored by any of the government sponsored enterprises

[7] Navigant report, Congressional Oversight Panel (2009).

(GSEs), so-called "private-label" loans, which are subject to all of the contract frictions described above. It also includes loans owned by servicers, so-called "portfolio" loans, which are immune to such problems. We compare renegotiation rates, controlling for observable characteristics of the loans. For our narrowest definition of renegotiation, payment-reducing modification, we find that the differences in the likelihood of renegotiation in the 12 months subsequent to the first 60-day delinquency between the two types of loans is neither economically nor statistically significant. When we consider the broader definition that includes any modification at all, which, as we mentioned above, we would expect to be most affected by securitization, the data even more strongly reject the role of securitization in preventing renegotiation. We also find that servicers are *more* likely to peform modifications, broadly defined, and to allow the borrower to prepay on a private-label loan than on a portfolio loan.

Our results are highly robust. One potential problem with the data is that there is unobserved heterogeneity in the characteristics of portfolio and private-label loans. To address this, we exploit subsets of the LPS data, in which servicers provide an exceptional amount of information about borrowers. When we exclude observations where the servicer failed to report whether the borrower fully documented income at origination, or what the debt-to-income ratio was at origination, our results become even stronger. When we focus only on loans for which the borrower fully documented income, we obtain results that are broadly consistent or, in some cases, stronger than the results for the full sample. Finally, we limit our sample to only subprime loans (as defined in LPS). These loans comprise only 7 percent of the LPS data, but they account for more than 40 percent of all serious delinquencies and almost 50 percent of the modifications that we identify in the data. The results that we obtain for the subprime sample are also consistent with our results for the full sample.

Another potential issue with our focus on 60-day delinquent loans is that portfolio lenders can contact borrowers at any time, whereas some securitization agreements forbid lenders from contacting borrowers until they are at least 60 days delinquent (two missed payments). When we shift our focus to 30-day delinquent borrowers (one missed payment), our results continue to show no meaningful difference between renegotiation of private-label and portfolio loans.

One other possibility is that our algorithm for identifying modifications is somehow missing a class of loss-mitigation actions taken by servicers. Forbearance agreements and repayment plans, for example, would not necessarily show up in our data. However, neither of these actions constitutes renegotiation in any classic sense, because the lender still expects the borrower to repay in full, including interest on any delayed payment. In addition, unlike modifications, PSAs never place any limits on the use of forbearance agreements or repayment plans, so, *a priori*, we would have less reason to expect a difference in their use across private-label and portfolio loans. Finally, most successful forbearance agreements conclude with a modification to allow the borrower to repay the arrears incurred in forbearance. With all of that said, we test the proposition that servicers engage in other loss mitigation actions by looking at the "cure rate." This is the percentage of loans that transition to current status after becoming 60-days delinquent. We find that in the full sample, private-label loans are less likely to cure, but that the gap, although statistically significant, is small — correcting for observable characteristics, we estimate a cure rate of around 30 percent for the typical portfolio loan and a cure rate of about 2 percentage points less for an otherwise equivalent private-label loan. However, for the subprime subsample, the subsample with information about documentation and debt-to-income (DTI) status, and the sample of fully documented loans, we find that private-label loans are significantly *more* likely to cure.

The policy debate has focused exclusively on the ways securitization impedes renegotiation and implicitly assumes that portfolio lenders face no institutional impediments, but this is not realistic. Portfolio lenders complain about accounting rules, including the need to identify modifications, even when the borrowers are current prior to the modification, as "troubled debt restructurings," which leads to reduction of the amount of Tier II capital and increased scrutiny from investors and cumbersome accounting requirements. The shortage of qualified staff, an oft-heard complaint from borrowers seeking renegotiation, affects servicers of portfolio loans and private label loans equally. Finally, the interests of the managers of a loan portfolio are not necessarily any more likely to be aligned with their investors than are the interests of the trustees of a mortgage pool; many have attributed the catastrophic failures of financial institutions like AIG in 2008 to misaligned incentives of managers and shareholders.

Our results are consistent with the hypothesis that securitization does impede renegotiation but that a different set of impediments leads to similar problems with portfolio loans and generates our finding that there is no difference. However, the small differences would represent a remarkable coincidence.[8] More importantly, the low overall levels of renegotiation mean that even if contract frictions cut the overall number of concessionary modifications in half, 94 percent of seriously delinquent borrowers would still fail to receive a concessionary modification. So the puzzle remains why so few loans are renegotiated.

If contract frictions are not a significant problem, then what is the explanation for

[8]Yet another possible explanation is that equal treatment provisions in PSAs force servicers to modify similar numbers of portfolio and private-label loans and that servicers are reluctant to modify portfolio loans in spite of the fact that they internalize the benefits because they must then modify private label loans for which they don't.

why lenders do not renegotiate with delinquent borrowers more often? We argue for a very mundane explanation: lenders expect to recover more from foreclosure than from a modified loan. This may seem surprising, given the large losses lenders typically incur in foreclosure, which include both the difference between the value of the loan and the collateral, and the substantial legal expenses associated with the conveyance. The problem is that renegotiation exposes lenders to two types of risks that can dramatically increase its cost. The first is what we will call "self-cure" risk. As we mentioned above, more than 30 percent of seriously delinquent borrowers "cure" without receiving a modification; if taken at face value, this means that, in expectation, 30 percent of the money spent on a given modification is wasted. The second cost comes from borrowers who redefault; our results show that a large fraction of borrowers who receive modifications end up back in serious delinquency within six months. For them, the lender has simply postponed foreclosure; in a world with rapidly falling house prices, the lender will now recover even less in foreclosure. In addition, a borrower who faces a high likelihood of eventually losing the home will do little or nothing to maintain the house or may even contribute to its deterioration, again reducing the expected recovery by the lender.

In Section 4 of the paper, we formalize the basic intuition of the investor renegotiation decision, with a simple model. We show that higher cure rates, higher redefault rates, higher expectations of house price depreciation, and a higher discount rate all make renegotiation less attractive to the investor. Thus, one cannot evaluate a modification by simply comparing the reduction in the interest rate on the loan or in the principal balance with the expected loss in foreclosure. One must take into account both the redefault *and* the self-cure risks, something that most proponents of modification fail to do.[9]

To our knowledge, this paper is the first to estimate directly the likelihood of renegotiation of private-label and portfolio-held loans. Piskorski, Seru, and Vig (2009) address the question of the effects of securitization on renegotiation, but rather than directly identifying renegotiation, they run "black-box" foreclosure regressions using LPS data and argue that observed differences in foreclosure rates *imply* differences in renegotiation activity. Our results contradict this interpretation. For renegotiation to explain the differences in foreclosure rates, there would have to be large errors in our algorithm for identifying renegotiation, and those errors would have to be significantly biased toward portfolio loans, a possibility that is particularly problematic given that the renegotiations we focus on are precisely the type that PSAs supposedly prevent. In addition, most of the loan histories in the LPS

[9]Many proponents of aggressive modification take into account redefault risk, and the MHA plan did address it by providing some insurance against further house price declines to investors who modified loans. However, none of the main proponents ever mentions self-cure risk, even though it is well-known in the industry, see: http://www.calculatedriskblog.com/2008/09/loan-modifications-anecdotes-and-data.html.

sample are right-censored, meaning that the borrowers have neither lost their homes nor paid off their mortgages when the data end, making it impossible to equate the absence of a foreclosure with successful renegotiation. By contrast, a "cure" is a necessary condition for renegotiation, and thus the differences we report in cure rates across portfolio and private-label loans that are neither large nor of consistent sign contradict the claim that securitization is a major obstacle to renegotiation.

The implications of our research for policy are three-fold. First, "safe harbor" provisions, which shelter servicers from investor lawsuits, are unlikely to affect the number of modifications and should have little effect. Second, and more broadly, the number of "preventable foreclosures" may be far fewer than many believe.

Finally, we point out that while our model shows why investors may not want to perform modifications, that does not necessarily imply that modifications may not be socially optimal. One key input to our theoretical model is the discount rate, and it is possible that investors, especially in a time when liquidity is highly valued, may be less patient than society as a whole, and therefore foreclose when society would prefer renegotiation. Large financial incentives to investors or even to borrowers to continue payment could mitigate this problem.

1.1 Related Literature and Existing Evidence

Our research draws on existing literature in several different fields. First, there has been substantial interest in the question of renegotiation of home mortgages among real estate economists, both prior to, and as a result of the current crisis. Riddiough and Wyatt (1994a), Riddiough and Wyatt (1994b), and Ambrose and Capone (1996) addressed informational issues that inhibit efficient renegotiation. We draw extensively on this research in Section 4. Springer and Waller (1993), in an early example, explores patterns in the use of forbearance as a loss mitigation tool. Capone (1996) and Cutts and Green (2005) both discuss the institutional issues, with the former study providing historical evidence and focusing on issues in the mid-1990s, and the latter study discussing innovations since then.

The start of the subprime crisis in 2007 led to a resurgence of interest in the topic among real estate economists and aroused new interest from other fields, in particular, the field of law. In real estate, Quercia, Ding, and Ratcliffe (2009), Cutts and Merrill (2008), Stegman, Quercia, Ratcliffe, Ding, Davis, Li, Ernst, Aurand, and Van Zandt (2007), and Mason (2007), all discuss issues with contemporary loss mitigation approaches. Legal researchers, White (2008) and White (2009), for example, have addressed empirical questions about the frequency and characteristics of loan modifications, closely related to the analysis in this paper. In addition, they have also looked at issues related to the restrictions imposed by contracts (Hunt 2009 and Gelpern and Levitin 2009) and the interactions among foreclosure, renegotiation, and personal bankruptcy (Levitin 2009a and Levitin 2009b).

More broadly, real estate economists have explored the factors that lead delinquent mortgages to transition to foreclosure or to cure, one of which is renegotiation. Pre-crisis papers include Ambrose and Capone (1998), Ambrose, Buttimer Jr, and Capone (1997), Ambrose and Capone (2000), Lauria, Baxter, and Bordelon (2004), Danis and Pennington-Cross (2005), Pennington-Cross (2009), and Pennington-Cross and Ho (2006). Mulherin and Muller (1987) discusses conflicts between mortgage insurers and owners that may lead servicers to induce or postpone foreclosure inefficiently. In light of the crisis, Piskorski, Seru, and Vig (2009) and Cordell, Dynan, Lehnert, Liang, and Mauskopf (2008a) have revisited the question.

The issue of dispersed ownership and debt renegotiation has received a fair amount of attention in the corporate finance literature. Gan and Mayer (2006), for example, focus on commercial mortgages, and find that servicers delay liquidation of delinquent mortgages when they are also the holders of the equity tranche of the deal. This suggests that participating in the losses due to liquidation may alleviate some of the agency problems posed by the separation of ownership and servicing pointed out before. However, it may also lead to conflicts of interest between holders of different tranches. In their setting, Gan and Mayer (2006) find that the servicers' behavior is consistent with asset substitution, as servicers seek to benefit from the option-like payoff of their position. Also, the contractual restrictions imposed by PSAs (discussed above) and standard economic arguments on the effects of dispersed ownership of debt (as in Bolton and Scharfstein 1996 and Asquith, Gertner, and Scharfstein 1994) further reduce the incentives of servicers to modify mortgages.

2 Data

We use a dataset constructed by LPS. This is a loan-level dataset that covers approximately 60 percent of the U.S. mortgage market and contains detailed information on the characteristics of both purchase-money mortgages and mortgages used to refinance existing debt.[10] This dataset is especially useful in the context of this paper, as it includes both securitized mortgages and loans held in portfolio.[11] The LPS data specifically denote whether a mort-

[10]We use a 10 percent random sample of the LPS data when estimating all of our empirical models. The dataset is simply too big to use in its entirety from a computational standpoint. However, we have checked the robustness of our results to using different sample sizes, and we do not find substantial differences.

[11]For a more detailed discussion of the LPS data, we direct the reader to Foote, Gerardi, Goette, and Willen (2009).

gage is held in portfolio, or securitized by a non-agency, private institution.[12] If institutional constraints are restricting the modification process for private-label, securitized loans, we would expect to see relatively few modifications among them, as compared to portfolio loans. Unfortunately, our LPS sample does not include direct information regarding loan modifications.[13] However, LPS does provide monthly updates to loan terms, so it is possible to identify loan modifications indirectly (and imperfectly). Table 1 shows two examples of modifications in the data. In the first example, the servicer cuts the interest rate, capitalizes arrears into the balance of the loan, and extends the term of the loan to 40 years. In the second example, the servicer just capitalizes arrears into the balance of the loan. In both cases the loan is reported as "current" after the modification, whereas before it was 90+ days delinquent.

We denote a loan as being modified if there is a change in its terms that was not stipulated by the initial terms of the contract. Such modifications include interest-rate reductions, principal-balance reductions, and term extensions. We can also identify principal-balance and mortgage-payment *increases* that reflect the addition of arrears into the balance of a loan.[14] We spell out our algorithm for identifying modifications in more detail in Appendix A.

There are two potential mistakes we can make in this exercise. First, we may falsely identify modifications ("false positives") because of measurement error in the data (for example, a mistake in the updated balance or interest rate) or some endogenous behavior on the part of the borrower (for example, a borrower making extra principal payments). Second, we could miss modifications ("false negatives") because our algorithm for finding modifications is incomplete. In order to test our algorithm, we use data from the Columbia files put together by Wells Fargo's CTSLink service. This dataset includes a similar set of variables to those in the LPS dataset (on performace of the loans and characteristics of the borrower at origination) but is limited to private-label loans. These files do include,

[12]The LPS data also denote when a loan is securitized by a GSE (Government Sponsored Enterprise) such as Freddie Mac or Fannie Mae. We eliminate this class of loans, since the GSEs hold all credit risk, and thus are not subject to any modification restrictions.

[13]In a recent report, the Office of Thrift Supervision (OTS), in collaboration with the Office of the Comptroller of Currency (OCC), used data from LPS to analyze the outcomes of recent mortgage modification programs (OCC and OTS Mortgage Metrics Report, Third Quarter 2008). In this report, they had access to supplementary data from servicers that include the identification of loans in the LPS data that had been modified. We have not been able to obtain access to this data.

[14]One of the major types of loan modifications that we are largely unable to identify are interest rate freezes for subprime ARMs, which reset after two or three years. However, the reason that we cannot identify those freezes is because many are not binding; the fully-indexed rate is lower than the initial rate. These modifications will have no major effect on the current terms of the mortgage, so we do not view this as a major drawback.

however, explicit flags for modifications. This allows us to use the same algorithm described in Appendix A and compare the modifications we identify to the "true" modifications. Results are reported in Table 2. Overall our algorithm performs well, with 17 percent false negatives (that is, we do not identify around 17 percent of the "true" modifications) and around the same percentage of false positives (that is, approximately 17 percent of the modifications we identify are not flagged as modifications on the CTSLink data). By type of modification, our algorithm performs best for principal reductions, term increases, and fixed-rate mortgage reductions, and comparatively worse for ARM rate reductions and for principal increases.

2.1 Summary Statistics from the Data

Table 3 reports the number of modifications performed each quarter from the first quarter of 2007 through the final quarter of 2008, disaggregated by the type of modification. Each of the numbers is a multiple of 10 because we used a 10 percent random sample and scaled up the numbers we found. The first column of Table 3 simply reports the total number of loan modifications made. Not surprisingly, modifications have become more common as the housing market has weakened. There appear to be more than 7–8 times as many modifications performed in the fourth quarter of 2008 as in the first quarter of 2007. In addition to the rapid growth in loan modifications, the composition of modifications has changed over time. This can be seen in the remaining columns of Table 3, which list the incidence of modifications of different types.[15]

An interesting finding is that most modifications entailed *increases* in the principal balance of a mortgage. Such increases are likely due to the addition of arrears to the outstanding mortgage balance for delinquent borrowers, and these often increase the monthly mortgage payment by a nontrivial amount. While the absolute numbers of balance-increasing modifications are still rising, they are falling as a percentage of total modifications. In the last few quarters, interest-rate reductions, which necessarily involve a decrease in the monthly mortgage payment, have become more frequent, rising to more than 26 percent of all modifications performed in 2008:Q4. Table 3 provides further information regarding the behavior of monthly mortgage payments for loans that have undergone a modification. There are several notable patterns in this table. First, as of 2008:Q4, modifications that involved payment decreases were more common than those that involved payment increases. Furthermore, the

[15]In many cases a mortgage will experience multiple types of modifications at the same time. For example, we see cases in the data in which the interest rate is decreased and at the same time the term of the loan is extended. Thus, the percentages in Table 3 are not calculated with respect to the number of loans modified, but rather with respect to the number of modifications performed.

average and median magnitude of payment decreases has recently increased in our sample. From 2007:Q1 to 2008:Q2, the median payment decrease ranged from approximately 10 percent to 14 percent, but then increased to approximately 20 percent and 22 percent in 2008:Q3 and 2008:Q4, respectively. Based on the logic from our simple framework above, it is likely that these will have more success than modifications involving increases in the payment and/or balance.

Another interesting observation from Table 3 is that the incidence of principal reductions is quite low in our data. This is likely due to two factors. First, the LPS dataset under-represents the subprime mortgage market.[16] A few servicers that focus almost exclusively on subprime mortgages have recently begun modification programs that involve principal reduction.[17] In addition, from a theoretical perspective, principal reduction plans suffer from the severe incomplete-information problem noted earlier. Balance reductions are appealing to both borrowers in danger of default and those who are not. In a recent paper, we argued that to avoid such moral hazard concerns, lenders have a strong incentive to only provide modifications to those borrowers who are most likely to default.[18] Table 3 contains summary statistics regarding the characteristics at origination of both the sample of modified mortgages and the sample of all loans in the LPS dataset. The patterns that emerge from the table are consistent with such an argument. We discuss this point in more detail below. The sample of modified mortgages is characterized by substantially lower credit scores, higher loan-to-value (ltv) ratios, and slightly higher debt-to-income ratios. The discrepancy in ltv ratios may be underestimated, as the percentage of mortgages with an ltv ratio of exactly 80 percent is significantly higher in the modification sample than in the full sample. As we argued above, this likely implies a larger fraction of highly leveraged loans, for which the second liens are not observable in the data. In addition, the modification sample includes a higher fraction of mortgages with non-traditional amortization schedules, such as interest-only loans, option ARMS, hybrid ARMs, and subprime loans.

In Table 4 we compare the size of payment decrease and payment increase modifications for loans held in private-label trusts and loans held in portfolio. The results are somewhat mixed, as the size (as a percentage of the original payment) of the median payment decrease due to modification is larger for private-label loans in the first three quarters of 2008, but smaller in the final quarter. We see a similar pattern for the median payment increase due

[16]The majority of subprime mortgages are securitized by non-agency firms, and the LPS dataset includes approximately 35 percent of mortgages securitized by non-agency corporations.

[17]According to an October report by Credit Suisse, Ocwen Loan Servicing, LLC and Litton Loan Servicing LP were the only subprime servicers that had performed a nontrivial number of principal reduction modifications. Neither of these servicers contributes to the LPS dataset.

[18]See Foote, Gerardi, and Willen (2008) for a more detailed discussion.

to modification, while the differences are small for the mean and median payment increase.

3 Differences in Modification Behavior

In this section, we directly address the question of whether the incidence of modification is impeded by the process of securitization. We show evidence that private-label loans and portfolio loans perform similarly, both unconditionally and when observable differences between securitized and portfolio-held loans are controlled for, using both a logit model with a 12-month horizon and a Cox proportional hazard model that takes into account the problem of right censoring in the data.

To make sure that our results are robust to the type of modification performed, we use several different definitions of modification in this section. Our first measure is the number of concessionary modifications, which we define as reductions in the interest rate, reductions in the principal balance, extensions of the term, or combinations of all three. Any or a combination of these serves to reduce a borrower's monthly mortgage payment. We use this as our primary definition of modification in our analysis, as there is a consensus among most market observers that concessionary modifications are the most, or perhaps the only, effective way of preventing foreclosures. Because pooling and servicing agreements, which govern the conduct of servicers when loans are securitized, often limit modifications that change *any* of the contract terms (not just those that result in payment decreases), we broaden our definition of renegotiation to include any modification, regardless of whether it lowers the borrower's payment. As we discussed above, many, and in some subsets, most modifications, involve the capitalization of arrears into the balance of the loan and thus lead to increased payments. Finally, we attempt to include in our measure of renegotiation the number of times that lenders allow borrowers to extinguish their liabilities by repaying less than the outstanding balance of the loan. These transactions are known as short payoffs, short sales, or deeds-in-lieu of foreclosure, depending on the structure. We do this by counting the number of seriously delinquent loans that the servicer reports as paid off, and including these observations in our definition of modification.

Before turning to the regressions, however, it is instructive to look at the unconditional frequencies of modifications in the data. Panel A of Table 5 shows the unconditional frequencies for each type of investor. The first takeaway from the table is the extremely low percentages of modifications for *both* types of mortgages. Only 3 percent of 60-day delinquent loans received concessionary modifications in the 12 months following the first serious delinquency, and only 8.5 percent of the delinquent loans received *any* type of modification in the same period. These are extremely low levels of modifications, and they suggest that even if there are contract frictions that are preventing modifications in securitized trusts, the economic effects are small. The second takeaway from the table is that the unconditional differences between portfolio loans and private-label loans are very small in absolute terms. There is a difference of approximately 0.6 percentage points and 0.3 percentage points for concessionary modifications and all modifications, respectively. These are very small differences, and they suggest that contract frictions do not play an important role in inhibiting the renegotiation process for loans in securitized trusts. However, these are unconditional statistics, and it is possible that once observable differences in the characteristics of each type of loan and borrower are accounted for, the results may change.[19] Thus, we now estimate differences in modification behavior while controlling for observable loan and borrower characteristics. These characteristics include the contract interest rate at origination; the credit score of the borrower at origination; the loan-to-value ratio of the mortgage (not including second or third liens) at origination[20]; the logarithm of the nominal dollar amount of loan; an indicator of whether the purpose of the loan was a refinance of a previous mortgage or a home purchase; an indicator of whether the loan was considered to be subprime[21]; a measure of the amount of equity in the property at the time of delinquency, specified as a percentage of the original loan balance and updated by state-level house price indexes calculated by the Federal Housing Finance Agency (FHFA)[22] (and an indicator for a borrower who is in a position of negative equity at the time of delinquency, where the value of the mortgage exceeds the value of the home); and the unemployment rate of the county in which the borrower resides, calculated by the Burea of Labor Services (BLS).[23] We also include, but do not show because of space considerations, a set of cohort dummies that control for the quarter when the mortgage was originated, information regarding the amortization schedule of the mortgage (interest-only or negative amortization, including mortgages commonly referred to as option ARMs), an indicator for whether the size of the mortgage is greater than the GSE conforming loan limits, an indicator for whether the

[19]For example, if private-label loans are significantly riskier, and thus better candidates for modification on average, then the unconditional difference will significantly understate things.

[20]Because of the lack of information on second liens in the LPS data and the prevalence of second mortgages as a way to avoid paying mortgage insurance, we include an indicator variable if the ltv ratio is exactly equal to 80 percent. These are the borrowers who likely took out second mortgages, as the requirement for mortgage insurance occurs at ltv ratios above 80 percent. Our experience with other, more complete datasets also confirms that many of these borrowers are likely to have second mortgages that bring the cumulative ltv ratio up to 100 percent.

[21]This definition of subprime comes from the mortgage servicers that contribute to the LPS dataset.

[22]House prices are measured at the state level using the FHFA index. We also tried using Case-Shiller metropolitan area house price indexes and found no substantive differences. We chose to use the OFHEO prices for our primary specifications because of their greater sample coverage.

[23]Equity and periods of unemployment are very important determinants of a borrower's decision to default, and thus should also be important factors in the modification decision.

house is a primary residence, an indicator for adjustable rate mortgages that contain a reset provision (so-called "hybrid ARMs"), and, finally, an indicator for a borrower who does not use the corresponding property as a principal residence (this includes both properties used strictly for investment purposes, and vacation homes).

3.1 Canonical Specification Results

Panel B of Table 5 displays the estimated marginal effects from a set of logit models for the three different types of modification definitions. The dependent variable is 1 if a 60-day deliquent loan is modified at any point in the 12 months following the first delinquency. The first column considers payment-reducing (concessionary) modifications, the second column includes both payment-reducing and payment-increasing modifications, and the third column contains all modifications considered before, as well as prepayments. In all regressions, the group of portfolio-held loans is omitted from the estimation and is thus assumed to be the reference group. We cluster the standard errors at the zip code level to account for the fact that loans in the same geographical area are likely to suffer correlated (unobserved) shocks.

According to the estimates in the first column, private-label loans were approximately 0.3 percentage points less likely to receive concessionary modifications than loans held in portfolio. This estimate is economically small but statistically significant at the 10 percent level. When we consider all modifications the point estimate flips sign and becomes 0.2 percentage points (statistically insignificant), while for the third specification, private-label loans were actually 0.9 percentage points more likely to receive concessionary modifications (statistically significant). As discussed above, all of these specifications include a number of additional loan characteristics that are important in the underwriting process and, thus, likely to play an important role in the modification decision. The first observation to make regarding the results reported in Panel B is that the difference between the incidence of modification for portfolio-held loans and private-label loans becomes even smaller when these variables are controlled for in the estimation. The results also imply that loans with higher credit scores were modified less, loans with higher ltv ratios were modified less, larger loans were modified more, and loans with more equity at the time of delinquency were modified less. We find a sizeable difference in terms of the frequency of modification for both refinances and subprime loans. Conditional on being 60-days delinquent, subprime loans were modified about 2 percentage points more than prime loans. We estimate a model separately for subprime loans in Table 6.

Censoring is an important issue for any sample of mortgages, as there are currently many delinquent loans that are, or will soon be, good candidates for modification, as the housing market continues to decline. For this reason, we estimate a Cox proportional hazard model of the transition from serious delinquency to modification. The Cox model is very common in the survival analysis literature, and it has the advantage of being both flexible in terms of functional form considerations, as the baseline hazard function can be treated as an incidental parameter, and easy to estimate in terms of computational considerations. The results, expressed as hazard ratios, are reported in Panel C. A hazard ratio less than 1 indicates that private-label loans were less likely to receive a modification compared to portfolio loans, while a ratio greater than 1 signifies the opposite. The estimates are consistent with what we report for the logits in the previous panel. Private-label loans were less likely to receive concessionary modifications, but this coefficient estimate is statistically insignificant. For the our other two modification definitions the sign flips, but again the result is not statistically significant. All three specifications include the same covariates that were included in the logit models.

3.2 Subsample Results

Table 6 contains further logit estimation results for various subsamples of interest to see if there are different probabilities than in the full sample. Since the subprime indicator seems to be such a powerful predictor of modification conditional on serious delinquency in Table 5, we report the estimated marginal effects for only the sample of subprime loans in the second column of Table 6. The subprime sample also has the advantage that the agencies (Fannie Mae and Freddie Mac) were unlikely to be the marginal investor for this type of loans, so it is less likely that the portfolio and private-label samples differ significantly on unobservable characteristics. In the third column, we report results from the sample of LPS mortgages for which the borrower had a FICO score of less than 620, since automated underwriting systems generally instruct lenders to engage in increased scrutiny for such loans because of increased default risk. In the fourth and fifth columns, we focus on samples of loans that we believe contain the most information regarding the borrowers, in order to try to minimize the amount of unobservable heterogeneity that could potentially be biasing the results. In the fourth column, we focus on the sample of loans for which both the DTI ratio and the documentation status contain non-missing values, while the fifth column contains results for only the loans that were fully documented (in terms of income and assets) at origination. Panel A contains both unconditional means and estimated marginal effects for concessionary modifications, while Panel B contains results for the broader definition that also includes non-concessionary modifications.

The results are largely consistent with those contained in Table 5. We redisplay the results from the full sample in the first column of Table 6 for ease of comparison. The difference in modification frequency between private-label and portfolio-held, subprime mortgages for 60-day delinquent loans is small, and not statistically different from zero for both definitions of modification. Using a FICO cutoff of 620 as an alternative definition of subprime does not seem to make much difference. The unconditional means are smaller (for both types of loans) compared to the LPS subprime sample, as the LPS definition includes most of the loans with a FICO less than 620, but also some loans with higher associated FICOs. However, the marginal effects of private-label loans estimated from the logit models are quite similar to those from the LPS subprime sample, as they are economically small, and not statistically significant. Finally, we also find small and largely insignificant results for the last two subsamples, displayed in the fourth and fifth columns of Table 6. Although, it is worth pointing out that we do find a statistically significant, positive estimate of private-label loans for the broad definition of modification (Panel B).

3.3 Alternative Delinquency Definition

As an additional robustness check, we broaden our definition of delinquency and focus on modifications performed on loans subsequent to their first 30-day delinquency, which corresponds to one missed mortgage payment. While waiting until a borrower becomes seriously delinquent (defined as 60-days) to renegotiate is common practice in the servicing industry, there are no direct contractual stipulations (to our knowledge) that restrict a servicer from modifying the loan of a borrower who is 30-days delinquent. Thus, in Table 7 we repeat our analysis of Tables 5 and 6, but condition on 30-days delinquency rather than 60-days. The table contains three panels of estimation results, one for each of our modification definitions, and all of the subsamples described considered in Table 6. The unconditional means, logit marginal effects, and Cox hazard ratios are all reported for each combination of subsample and modification definition.

The results are very similar to those from the analysis of 60-day delinquent loans. According to the full sample and subprime sample logit models, portfolio loans received slightly more concessionary modifications, and the differences (0.3 and 0.5 percentage points respectively) are statistically significant at conventional levels. However, according to the subprime sample and full documentation sample Cox models, private-label loans actually received more concessionary modifications, although those differences are also small.[24] The results

[24]The logit marginal effects correspond to percentage point differences, while the Cox hazard ratios correspond to percent differences. If one expresses the logit marginal effects as a percent change of the unconditional means, those percent changes are very similar in magnitude to the Cox results.

for our second modification definition are similar, although we find more evidence of statistically significant, positive differences between the incidence of portfolio and private-level modifications. The samples of portfolio loans with non-missing information for DTI and documentation status were modified more often than the corresponding sample of private-label loans, but the magnitudes are still relatively small (10 to 20 percent difference from the unconditional mean). Finally, in Panel C, we see strong evidence for both the logit and Cox specifications, that delinquent private-label loans prepayed more often than portfolio loans. The differences are statistically significant for every one of the subsamples.

3.4 Redefault Probabilities and Cure Rates

In the previous subsections, we showed that there is little difference in the frequency of mortgage loan modifications between servicers of loans held in a private trust versus loans held in portfolio. There are two potential reasons that may explain the failure of those exercises to pick up important differences in servicer behavior that may truly exist. First, it may be that contract frictions in securitization trusts do not result in substantial differences in the frequency of modifications (the extensive margin) but do result in significant differences in the intensive margin, with respect to the types of modifications performed, the extent to which contract terms are modified, and, more broadly, the care or effort expended in each modification by private-label servicers compared to that expended by portfolio servicers. Second, there may be a type of renegotiation that our algorithm does not identify, but that is used to a large extent in loss mitigation efforts and used differently by servicers of private-label loans than by servicers of portfolio loans. For example, forms of forbearance, which are often called repayment plans in the industry, would not be picked up by our algorithm.[25] In this subsection, we use the LPS data to attempt to address these possibilities.

We perform two separate empirical exercises to address each of these concerns in turn. First, we compare redefault rates of private-label modified loans with those of portfolio modified loans. We define redefault as a loan that is 60 days delinquent or more, in foreclosure process or already foreclosed and now owned by the lender (REO for "real-estate-owned") six months after the time of the modification. If there are important differences in the manner by which servicers of private-label loans modify mortgages relative to the foreclosure procedures of servicers of portfolio loans, then we would expect to see significant differences in the subsequent performance of modified loans.

Second, to address the possibility that our algorithm misses an important aspect of

[25] However, as we argued above, PSAs do not contain restrictions on repayment plans, because they do not involve changing the terms of the mortgage. Thus, we would argue that differences in forbearance behavior that might exist could not be the result of contract frictions in securitization trusts.

renegotiation, we compare the cure rates of seriously delinquent, private-label loans to those of seriously delinquent portfolio loans. The idea behind this exercise is that any appreciable difference in servicer renegotiation behavior will manifest itself in differences in cure rates. It is important to stress however, that differences in servicer renegotiation behavior are only one potential explanation for differences that may exist in cure rates. To put this idea in the terms of logical reasoning, differences in cure rates are a necessary condition for significant differences in renegotiation behavior, but they are not a sufficient condition.

Table 8 contains the results of the redefault analysis. The first observation to note from the table is that the unconditional probability that a modified mortgage redefaults in this six-month period is very large, at about 20–40 percent for payment-reducing modifications (Panel A), and 40–50 percent for all modifications (Panel B). We argue below that the high level of redefault rates could explain why we observe so few modifications — very often they do not lead to successful outcomes even as little as six months after the modification. The second observation to note is that there is no statistically significant difference between the redefault rates of private-label loans and those of portfolio loans, once the observable characteristics of the mortgages are taken into account (this is valid for all of the subsamples). These results, combined with the statistics displayed in Table 4 suggest that there are no substantial differences in either the type of modification employed or in the care/effort expended by the two types of servicers.

Table 9 shows the results of logit models for the probability that a seriously delinquent loan subsequently cures. Our definition of a cure is that the loan is either current, 30-days delinquent, or prepaid after 12 months following the first 60-day delinquency. The first important point to make is that the unconditional cure probabilities are large (around 30 percent). Given that the unconditional modification probability is about 8 percent, this means that many loans cure without any intervention on the part of servicers. The second important observation to note in this table is that the cure probabilities for portfolio loans and private-label loans are quite similar. The unconditional cure probability is smaller by about 4.4 percentage points for private-label loans in the whole sample, but that is reduced to only 2.2 percentage points (statistically significant) when we control for observable characteristics of the loans and borrowers. We also include results for the subsamples of interest in columns 2–5. For each of the subsamples the sign of the difference actually reverses, as private-label loans were *more* likely to cure (the marginal effects are statistically significant, with the exception of the $FICO < 620$ sample). This is an important robustness check, as we argued above that unobserved heterogeneity is likely to be less of a problem in the subsamples (especially for the non-missing documentation status and DTI ratios sample and the full documentation sample). Thus, the change in the sign of the differences in cure rates between private-label servicers and portfolio servicers suggests that unobserved heterogeneity between the two loan types plays an important role.

4 Understanding the Empirical Results

If securitization does not block renegotiation, then why is it so rare? In this section, we build a simple model of the renegotiation decision, which, in a stylized way, mirrors the net present value (NPV) calculation that servicers are supposed to perform when deciding whether to offer a borrower a modification. We show that servicer uncertainty about whether the borrower will redefault even after successful renegotiation or uncertainty about whether the borrower will cure without renegotiation can dramatically affect the NPV calculation, ruining what a naive observer might think of as a "win-win" deal for the borrower and lender. While many proponents of modification are aware of the former problem, "redefault risk," none seem to be aware of the latter problem, which we call "self-cure risk."

In addition to the model, we also provide institutional evidence in this section that supports our arguments and findings above. This includes evidence of low modification frequencies in previous housing busts, well before the advent of securitization trusts; the equal treatment provision statements contained in the PSAs, which direct the servicer to behave as if it was in fact the investor of the mortgage-backed security and thus the owner of the mortgages; and finally, the absence of lawsuits to date directed at servicers by investors in mortgage-backed securities, which one would expect to find if modifications were unambiguously better than foreclosures from an NPV calculation.

4.1 A Simple Model of Loss Mitigation

We consider a simple model of a lender's decision to modify a delinquent loan.[26] There are three periods: $t = 0, 1, 2$. The borrower owes a mortgage payment of size m at time 1 and is due to repay the loan balance M in period 2. The mortgage is collateralized by a house, which is worth P_1 and P_2 in periods 1 and 2, respectively. In period 0, the lender has to make a decision to either modify the loan, or do nothing. If the lender fails to modify the loan, then, with probability α_0, the borrower will default in period 1, and the lender will foreclose and recover $P_1 - \lambda$, where λ is the cost of foreclosing on the property. If the borrower does not default next period, then the lender receives the periodic payment m in period 1, and the borrower repays the loan in full in period 2. The value to the lender of

[26]Our model shares some basic similarities with the approach in Ambrose and Capone (1996), who also identify a role for self-cure risk in assessing the profitability of a loss mitigation action.

the loan without modification equals the present discounted value of the cash flow:

$$\alpha_0 * \min[(P_1 - \lambda), M] + (1 - \alpha_0)[m + (1/R)M], \tag{1}$$

where we ignore discounting for the first period because there is no income in period 0. If the lender modifies the loan, then we assume that the borrower makes a reduced periodic payment m^* in period 1 with certainty, but then either defaults with probability α_1 or repays a modified amount M^* in period 2. The value to the lender of the modified loan is:

$$m^* + (1/R)\alpha_1 * \min[(P_2 - \lambda), M^*] + (1 - \alpha_1)(1/R)M^*. \tag{2}$$

Taking the difference between expressions (2) and (1) yields the following proposition:

Proposition 1 *Modification makes sense if:*

$$\begin{aligned}(\alpha_0 - \alpha_1)[m^* + \tfrac{1}{R}M^* - \min[(P_1 - \lambda), M]]& \\ - (1 - \alpha_0)[m + \tfrac{1}{R}M - (m^* + \tfrac{1}{R}M^*)]& \\ + \alpha_1[m^* + \tfrac{1}{R}\min[(P_2 - \lambda), M^*] - \min[(P_1 - \lambda), M]] &> 0. \end{aligned} \tag{3}$$

To interpret equation (3), divide the population of borrowers into three groups. The first group, with mass of $\alpha_0 - \alpha_1$ are borrowers who will repay in full with a modification but who will default otherwise. For this group, the investor gains the difference between the present value of the modified repayment $m^* + \frac{1}{R}M^*$ and the recovery given foreclosure, $\min[(P_1 - \lambda), M]$. The second group, with mass $1 - \alpha_0$, includes borrowers who will repay whether or not they receive a modification. For this group, the investor loses the difference between full repayment and the modified repayment. Gerardi and Willen (2009) refer to the first two terms as Type I error and Type II error, respectively, in analogy with the statistical concepts. In this context, Type I error corresponds to the cost of not renegotiating loans that need modifying, while Type II error corresponds to the cost of modifying loans that would be repaid in the absence of assistance. The third term, with mass α_1, includes borrowers who will default regardless of whether they receive a modification. For these borrowers, modification yields a periodic payment, but postpones foreclosure. Whether this is good or bad for the lender depends on the evolution of house prices and the rate at which the lender discounts the cash flow.

To illustrate the implications of the model, we compute some simple comparative statics. All else being equal, an increase in α_0 makes modification more attractive to the investor, while an increase in α_1 makes modification less attractive. Intuitively, a higher α_0 means higher Type I error and lower Type II error, and a higher α_1 implies higher Type II error. Since, in general, one would think that α_0 and α_1 would move in the same direction across borrowers, it is useful to note that an increase the gap, $\alpha_0 - \alpha_1$, makes modification more attractive.

We make three points about the model. First, when looking at the data, it is not sufficient to show that one would recover more from a modified loan than from foreclosure *ex post*, to prove that modification is *ex ante* optimal. To prove that a modification makes sense from the perspective of the lender, one must show that the Type I error, the value of the modified loans that would have defaulted, exceeds the Type II error, the value of the modified loans that would have paid off in the absence of modification. White (2009), among many others, focuses entirely on Type I error:

> The average loss for the 21,000 first mortgages liquidated in November was \$145,000, representing an average loss of 55 percent of the amount due. Losses on second lien mortgages were close to 100 percent. In comparison, for the modified loans with some amount of principal or interest written off, the average loss recognized was \$23,610. This seven-to-one difference between foreclosure losses and modification write-offs is striking, and lies at the heart of the failure of the voluntary mortgage modification program. At a minimum, there is room for servicers to be more generous in writing down debt for the loans they are modifying, while still recovering far more than from foreclosures in the depressed real estate market of late 2008. I will consider some of the reasons for this apparently irrational behavior in a later section.[27]

To see why this is wrong, take an extreme example with $\alpha_1 = 0$. In that case, the gain to modifications equals

$$\alpha_0[m^* + \tfrac{1}{R}M^* - \min[(P_1 - \lambda), M]] - (1 - \alpha_0)[m + \tfrac{1}{R}M - (m^* + \tfrac{1}{R}M^*)]. \tag{4}$$

With α_0 sufficiently low, modification will not make sense. To be clear, our criticism of White (2009) and others has nothing to do with the possibility that the modified loan will default, as we have assumed here that the modified loan will pay off in full.

The second point here is that both the rate at which lenders discount future payoffs and the evolution of prices affect the gains to modification. For mass $(1 - \alpha_1)$ of the borrowers, modification will simply delay foreclosure. In that case, the lender will get some extra income from any mortgage payments the borrower makes before redefaulting, but the lender has to wait longer to obtain the final payout and will get less if prices continue to fall.

[27] White (2009), p. 14–15

The third point is that the lender's information set plays a crucial role here, and one could argue that it should only contain information outside the control of the borrower. This would limit the set to the origination characteristics of the loan, prices, and interest rates. Employment status, income, and marital status all present problems, although they can be partially overcome—as in the case of unemployment insurance. Delinquency status, which seems a natural candidate, is a difficult issue. On one hand, a borrower has virtually complete control over it. On the other hand, it is a costly signal, as a 60-day delinquency does adversely affect one's credit history and future access to credit markets. Thus, when considering ways to design a profitable modification program, which implies attempting to maximize α_0 and minimize α_1, a lender must restrict its information set to a relatively small set of variables that are contemporaneously exogenous to the borrower.

4.2 Institutional Evidence

While the results from Section 3 may be surprising to market commentators who believe that contract frictions inherent in securitization trusts are preventing large-scale modification efforts in mortgage markets, we argue in this section that both historical evidence and evidence from securitization contracts actually support our findings.

First, we look at history. If securitization, or more precisely private-label securitization, inhibits renegotiation, then we would expect that renegotiation would have been common in the 1990s, when there was little private-label securitization, or in the 1970s, when securitization itself was rare. But, the historical evidence we have does not bear that out. In 1975, Touche Ross surveyed loss mitigation activities at savings and loans and found, "Lenders... were unwilling to either modify loans through extended terms or refinancing to a lower rate."[28] In the 1990s, a report commissioned by Congress to study foreclosure alternatives, said, "Along with loan modifications, long-term forbearance/repayment plans are the most under utilized foreclosure avoidance tools currently available to the industry."[29]

Second, many observers have focused on institutional factors that inhibit loan modification when the loan is securitized, but other factors may play a similar role for portfolio lenders as well. In particular, accounting rules force lenders to take writedowns at the time of the modification (reducing Tier II capital), to identify modified loans as troubled debt restructurings (under FAS 15), and also to impose burdensome reporting requirements on modified loans including loan-specific allowances for potential losses (under FAS 114). Additionally, payments made by borrowers for loans that are subject to "troubled debt re-

[28]Capone (1996), p. 20–21.
[29]Capone (1996), p. x.

structurings" are recognized only as principal repayments and generate to interest income until the bank can demonstrate that a borrower is "performing." All of the above accounting requirements potentially make modifications costly for a bank. Downey Financial, for example, attempted to refinance current borrowers out of risky option ARMs into safer, fixed-rate instruments and argued that the change should not affect their balance sheet because the borrowers had never missed payments. However, their accountants viewed the refinancings as "troubled debt restructurings," and forced the firm to restate the share of nonperforming assets for November 2007 to 5.77 percent from 3.65 percent.[30]

If modifications were truly in the best financial interest of investors in mortgage-backed-securities (MBS) as many commentators have alleged, we would expect to see concern on their part regarding the low levels of modifications performed to date. But, according to Cordell, Dynan, Lehnert, Liang, and Mauskopf (2008b), who interviewed a number of MBS investors, they (the investors) are not concerned that servicers are foreclosing on many more mortgages than they are modifying. Thus, there does not seem to be much concern by market participants that either incentives or contract frictions are inhibiting servicers from performing loan modifications. The evidence in the literature seems to suggest a small role for contract frictions in the context of renegotiation. In a 2007 study of a small sample of PSAs, Credit Suisse found that fewer than 10 percent of the contracts ruled out modifications completely, while approximately 40 percent allowed modifications, but with quantity restrictions,[31] and the rest, about half, contained no restrictions on renegotiation behavior. Hunt (2009) also analyzed a sample of subprime PSAs and concluded that outright modification bans were extremely rare. A 2008 report by the COP analyzed a number of securitized mortgage pools with quantity restrictions and concluded that none of the restrictions were binding. In terms of incentive issues, Hunt (2009) found that most of the contracts in his sample explicitly instructed the mortgage servicer to behave as if it were the owner of the pool of the loans:

> The most common rules [in making modifications] are that the servicer must follow generally applicable servicing standards, service the loans in the interest of the certificate holders and/or the trust, and service the loans as it would service loans held for its own portfolio. Notably, these conditions taken together can be read as attempting to cause the loans to be serviced as if they had not been securitized. (p. 8, insertion added)

[30]http://www.housingwire.com/2008/01/14/downey-financial-accounting-rules-suck/

[31]The quantity restrictions often took the form of a limit (usually 5 percent) on the percentage of mortgages in the pool that could be modified without requesting permission from the trustee.

5 Conclusion

There is widespread concern that an inefficiently low number of mortgages have been modified during the current crisis, and that this has led to excessive foreclosure levels, leaving both families and investors worse off. We use a large dataset that accounts for approximately 60 percent of mortgages in the United States originated between 2005 and 2007, to shed more light on the determinants of mortgage modification, with a special focus on the claim that delinquent loans have different probabilities of renegotiation depending on whether they are securitized by private institutions or held in a servicer's portfolio. By comparing the relative frequency of renegotiation between private-label and portfolio mortgages, we are able to shed light on the question of whether institutional frictions in the secondary mortgage market are inhibiting the modification process from taking place.

Our first finding is that renegotiation in mortgage markets during this period was indeed rare. In our full sample of data, approximately 3 percent of the seriously delinquent borrowers received a concessionary modification in the year following their first serious delinquency, while fewer than 8 percent received any type of modification. These numbers are extremely low, considering that foreclosure proceedings were initiated on approximately half of the loans in the sample and completed for almost 30 percent of the sample. Our second finding is that a comparison of renegotiation rates for private-label loans and portfolio loans, while controlling for observable characteristics of loans and borrowers, yields economically small, and for the most part, statistically insignificant differences. This finding holds for a battery of robustness tests we consider, including various definitions of modification, numerous subsamples of the data, including subsamples for which we believe unobserved heterogeneity to be less of an issue, and consideration of potential differences along the intensive margin of renegotiation.

Since we conclude that contract frictions in securitization trusts are not a significant problem, we attempt to reconcile the conventional wisdom held by market commentators, that modifications are a win-win proposition from the standpoint of both borrowers and lenders, with the extraordinarily low levels of renegotiation that we find in the data. We argue that the data are not inconsistent with a situation in which, on average, lenders expect to recover more from foreclosure than from a modified loan. At face value, this assertion may seem implausible, since there are many estimates that suggest the average loss given foreclosure is much greater than the loss in value of a modified loan. However, we point out that renegotiation exposes lenders to two types of risks that are often overlooked by market observers and that can dramatically increase its cost. The first is "self-cure risk," which refers to the situation in which a lender renegotiates with a delinquent borrower who does not need assistance. This group of borrowers is non-trivial according to our data, as we find that approximately 30 percent of seriously delinquent borrowers "cure" in our data without receiving a modification. The second cost comes from borrowers who default again after receiving a loan modification. We refer to this group as "redefaulters," and our results show that a large fraction (between 30 and 45 percent) of borrowers who receive modifications, end up back in serious delinquency within six months. For this group, the lender has simply postponed foreclosure, and, if the housing market continues to decline, the lender will recover even less in foreclosure in the future.

We believe that our analysis has some important implications for policy. First, "safe harbor provisions," which are designed to shelter servicers from investor lawsuits, are unlikely to have a material impact on the number of modifications and thus will not significantly decrease foreclosures. Second, and more generally, if the presence of self-cure risk and redefault risk do make renegotiation less appealing to investors, the number of easily "preventable" foreclosures may be far smaller than many commentators believe.

A Appendix: Identifying Modifications in the LPS Dataset

In this section we discuss in detail the assumptions that we used to identify modified loans in the LPS dataset. The LPS dataset is updated on a monthly basis, and the updated data include both new mortgages originated and a snapshot of the current terms and delinquency status of outstanding mortgages. Essentially, for a given mortgage, we compare the updated terms to the terms at origination, as well as the change in terms from the proceeding month, and if there is a material change over and above the changes stipulated in the mortgage contract, then we assume that the contract terms of the mortgage have been modified.

A.1 Interest Rate Reductions

We use a different set of rules to identify reduced interest rates for fixed-rate mortgages (FRM) and adjustable-rate mortgages (ARM). In principle, identifying a rate change for an FRM should be easy, since by definition the rate is fixed for the term of the mortgage. However, after a detailed inspection of the LPS data, it became apparent that some of the smaller rate fluctuations were likely due to measurement error rather than to an explicit modification. Thus, we adopt a slightly more complex criterion: The difference between the rate at origination and the current rate must be greater than 50 basis points; *and* the difference between the rate in the previous month and the current rate must be greater than 50 basis points; *and* either the mortgage must be 30-days delinquent with the loan currently in loss mitigation proceedings (as reported by the servicer) or the difference between the rate in the previous month and the current rate must be greater than 300 basis points (which allows for the possibility that a loan that is current could feasibly qualify for a modification).

Identifying interest rate reductions for ARMs is slightly more complicated, since by definition the interest rate is variable and can move both up and down. The LPS data contain the information necessary to figure out how much the interest rate should move from month to month. This rate is often referred to as the fully indexed rate, as it is normally specified as a fixed spread above a common nominal interest rate. The LPS dataset contains information regarding the initial rate, the appropriate index rate, and the spread between the index and the mortgage rate. In addition, the majority of ARMs are characterized by a period at the beginning of the contract in which the interest rate is held constant (these mortgages are often referred to as hybrid ARMs). At the end of this period, the interest rate adjusts (or resets) to a certain spread above an index rate and then subsequently adjusts at a specific frequency. The LPS dataset also contains information regarding the length of the initial fixed period, enabling us to identify this period in the data and determine the point at which the interest rate should begin to adjust (we refer to this period as the reset date). Our criterion for identifying an interest rate reduction for an ARM is as follows: The difference between the rate at origination and the current rate must be greater than 50 basis points; *and* the difference between the rate in the previous month and the current rate must be greater than 50 basis points; *and* if the reset date has passed, then the difference between the fully-indexed rate and the current rate must be at least 100 basis points ; *and* either the mortgage must be 30-days delinquent with the loan currently in loss mitigation proceedings (as reported by the servicer) or the difference between the rate in the previous month and the current rate must be greater than 300 basis points (which allows for the possibility that a loan that is current could feasibly qualify for a modification). In addition, we allow for more modest month-to-month decreases in the interest rate (200 to 300 basis points) as long as there is also a positive change in the delinquency status of the loan (that is, the loan is reported to be less delinquent). Our inspection of the data suggests that the majority of modifications involve a resetting of the delinquency status back to current, or a minor delinquency, so conditioning on this change likely eliminates many false positives.

A.2 Term Extensions

In theory, it should be straightforward to identify term extensions in the LPS data, but it can be tricky to do so because of possible measurement error in the variable that measures the remaining maturity of each loan. We defined a term extension in the LPS dataset to be a case in which the loan was at least 30-days delinquent at some point and the number of years remaining increases by at least 20 months *or* the change in number of years remaining is greater than the difference between the original term of the loan and the remaining term (for example, if the original maturity is 360 months, and the loan has 350 months remaining, then the increase in length must be at least 10 months) and, finally, either the monthly payment decreases *or* the principal balance increases *or* the loan is in loss mitigation.

A.3 Principal Balance Reductions

A reduction in the remaining balance of a mortgage is perhaps the most difficult type of modification to identify because of the prevalence of "curtailment" or partial prepayment among mortgage borrowers. For example, it is common for borrowers to submit extra mortgage payments in order to pay down the loan at a faster rate. For this reason, we were forced to adopt strict criteria to limit the number of false positives. Our criterion for identifying a principal balance reduction is as follows: The month-to-month decrease in the remaining principal balance must be at least -10 percent and cannot be more than -30 percent (the upper bound does not matter as much as the lower bound—we experimented with -40 percent and -50 percent, but did not find a substantial difference); the principal balance recorded in the previous month must be greater than $25,000 (since we throw second liens out, and look only at mortgages originated after 2004, this cutoff does not bind often); the month-to-month payment change must be negative (there are only a few cases in which the principal balance is reduced without a corresponding decrease in the payment, but in these cases the term is extended, and thus is picked up in our code for identifying term extensions); and, finally, the mortgage must be either 30-days delinquent or currently in loss mitigation proceedings (as reported by the servicer).

A.4 Principal Balance Increases

For interest-only and fully-amortizing mortgages, identifying an increase in the principal balance due to the addition of arrears is relatively straightforward. It becomes trickier for mortgages that allow for negative amortization, as the principal balance is allowed to increase over the course of the contract, by definition. For interest-only and fully-amortizing mortgages our criterion is: The month-to-month principal balance must increase by at least 0.5 percent (to rule out measurement error in the data); the loan must have been at least 30-days delinquent at the time of the balance increase; and, finally, the month-to-month payment change must be positive unless there is also a corresponding increase in the term of the loan. For mortgages that allow for negative amortization, the criterion is similar, except that the balance increase must be at least 1 percent and there must be a positive change in the delinquency status of the loan.

References

Ambrose, B., R. Buttimer Jr, and C. Capone (1997). Pricing Mortgage Default and Foreclosure Delay. *Journal of Money, Credit & Banking 29*(3).

Ambrose, B. and C. Capone (1996). Cost-benefit analysis of single-family foreclosure alternatives. *The Journal of Real Estate Finance and Economics 13*(2), 105–120.

Ambrose, B. and C. Capone (1998). Modeling the conditional probability of foreclosure in the context of single-family mortgage default resolutions. *Real Estate Economics 26*(3), 391–429.

Ambrose, B. and C. Capone (2000). The hazard rates of first and second defaults. *The Journal of Real Estate Finance and Economics 20*(3), 275–293.

Asquith, P., R. Gertner, and D. Scharfstein (1994). Anatomy of financial distress: An examination of junk-bond issuers. *Quarterly Journal of Economics 109*(3), 625–658.

Bolton, P. and D. S. Scharfstein (1996). Optimal debt structure and the number of creditors. *Journal of Political Economy 104*(1), 1–25.

Capone, C. A. (1996). Providing Alternatives to Mortgage Foreclosure: A Report to Congress. US Department of Housing and Urban Development.

Congressional Oversight Panel (2009). Foreclosure Crisis: Working Toward a Solution. March Oversight Report.

Cordell, L., K. Dynan, A. Lehnert, N. Liang, and E. Mauskopf (2008a). The incentives of mortgage servicers: Myths and realities. *Federal Reserve Board Finance and Economics Discussion Series* 2008-46.

Cordell, L., K. Dynan, A. Lehnert, N. Liang, and E. Mauskopf (2008b). The Incentives of Mortgage Servicers: Myths and Realities. *Finance and Economics Discussion Series, Federal Reserve Board 46.*

Cutts, A. and R. Green (2005). Innovative servicing technology: smart enough to keep people in their houses? *Building Assets, Building Credit: Creating Wealth In Low-Income Communities*, 348–377.

Cutts, A. and W. Merrill (2008). Interventions in Mortgage Default: Policies and Practices to Prevent Home Loss and Lower Costs. Technical report, Working Paper.

Danis, M. A. and A. N. Pennington-Cross (2005). The Delinquency of Subprime Mortgages. *SSRN eLibrary*.

Eggert, K. (2007). Comment on michael a. stegman et al.: What prevents loan modifications? *Housing Policy Debate 18*(2).

Foote, C., K. Gerardi, L. Goette, and P. Willen (2009, June). Reducing foreclosures: No easy answers. Working Paper 15063, National Bureau of Economic Research.

Foote, C., K. Gerardi, and P. Willen (2008). Negative equity and foreclosure: Theory and evidence. *Journal of Urban Economics 6*(2), 234–245.

Gan, Y. H. and C. Mayer (2006). Agency conflicts, asset substitution, and securitization. *NBER Working Paper No. 12359.*

Geanakoplos, J. and S. Koniak (2008). The best way to help homeowners – and the economy. Available at http://cowles.econ.yale.edu/ gean/crisis/index.htm.

Gelpern, A. and A. Levitin (2009). Rewriting frankenstein contracts: Workout prohibitions in mortgage-backed securities. http://ssrn.com/abstract =1323546.

Gerardi, K. and P. Willen (2009). Suprime Mortgages, Urban Neighborhoods and Foreclosure. *The B.E. Journal of Economic Analysis & Policy 9*(3 (Symposium).

Hunt, J. P. (2009). What do subprime securitization contracts actually say about loan modification? *Berkeley Center for Law, Business and the Economy working paper.*

Lauria, M., V. Baxter, and B. Bordelon (2004). An investigation of the time between mortgage default and foreclosure. *Housing Studies 19*(4), 581–600.

Levitin, A. (2009a). Helping homeowners: Modification of mortgages in bankruptcy. *Harvard Law & Policy Review Online 3.*

Levitin, A. (2009b). Resolving the foreclosure crisis: Modification of mortgages in bankruptcy. *Wisconsin Law Review.*

Mason, J. (2007). Mortgage Loan Modification: Promises and Pitfalls.

Mulherin, J. and W. Muller (1987). Volatile interest rates and the divergence of incentives in mortgage contracts. *Journal of Law, Economics, and Organization 3*(1), 99–115.

Pennington-Cross, A. (2009). The duration of foreclosures in the subprime mortgage market: a competing risks model with mixing. *The Journal of Real Estate Finance and Economics*, 1–21.

Pennington-Cross, A. and G. Ho (2006). Loan Servicer Heterogeneity and the Termination of Subprime Mortgages.

Piskorski, T., A. Seru, and V. Vig (2009). Securitization and distressed loan renegotiation: Evidence from the subprime mortgage crisis. *Chicago Booth School of Business Research Paper No. 09-02.*

Quercia, R., L. Ding, and J. Ratcliffe (2009). Loan Modifications and Redefault Risk.

Riddiough, T. and S. Wyatt (1994a). Strategic default, workout, and commercial mortgage valuation. *The Journal of Real Estate Finance and Economics 9*(1), 5–22.

Riddiough, T. and S. Wyatt (1994b). Wimp or tough guy: Sequential default risk and signaling with mortgages. *The Journal of Real Estate Finance and Economics 9*(3), 299–321.

Springer, T. and N. Waller (1993). Lender forbearance: evidence from mortgage delinquency patterns. *Real Estate Economics 21*(1), 27–46.

Stegman, M., R. Quercia, J. Ratcliffe, L. Ding, W. Davis, W. Li, K. Ernst, A. Aurand, and S. Van Zandt (2007). Preventive Servicing Is Good for Business and Affordable Homeownership Policy. *Housing Policy Debate 18*(2).

White, A. M. (2008). Rewriting Contracts, Wholesale: Data on Voluntary Mortgage Modifications from 2007 and 2008 Remittance Reports. *Fordham Urban Law Journal forthcoming.*

White, A. M. (2009). Deleveraging the American Homeowner: The Failure of 2008 Voluntary Mortgage Contract Modifications. *Connecticut Law Review forthcoming.*

Zingales, L. (2008). Plan b. *Economists' Voice 5*(6), 4.

Table 1: Examples of modifications in the data.

Example 1: Servicer cuts interest rate, capitalizes arrears in the balance of the loan and extends term to 40 years.

Date	MBA Delinq. Stat.	Interest Rate	Monthly Payment	Outstanding Balance	Remaining Term in Months
2008m10	9	6.5	907	141,323	340
2008m11	9	6.5	907	141,323	339
2008m12	9	6.5	907	141,323	338
2009m1	C	4.5	660	146,686	479

Example 2: Servicer capitalizes arrears into the balance of the loan but otherwise leaves the loan unchanged.

Date	MBA Delinq. Stat.	Interest Rate	Monthly Payment	Outstanding Balance	Remaining Term in Months
2008m5	6	9.25	1,726	208,192	346
2008m6	9	9.25	1,726	208,192	346
2008m7	9	9.25	1,726	208,192	346
2008m8	C	9.25	1,815	218,316	341
2008m9	C	9.25	1,815	218,184	340

Table 2: Robustness of the modifications algorithm

False positives by type of modifications

	# of Modifications Using WF CTS Data	False Positives
FRM Rate Reduction	5,381	8.0%
ARM Rate Reduction	8,951	22.0%
Principal Reductions	470	1.9%
Principal Increases	13,010	12.8%
Term Increases	394	2.3%

Overall success of algorithm

	No Mod Using Our Algorithm	Mod Using Our Algorithm	Total
No Mod in WF Data	2,329,187	3,559	2,332,746
Mod in WF Data	3,627	17,514	21,141
Total	2,332,814	21,073	2,353,887

Notes: We test our algorithm on a dataset of securitized mortgages in which the trustee has identified modifications (data is from Wells Fargo Trustee Services). The lower panel shows that about 17.2% of our modifications are false positives, meaning that we identify modifications but the trustee does not and about 16.9% are false negatives, meaning that the trustee identifies a modification but we do not.

Table 3: Modification Statistics

(1) By Type of Modification: 2007:Q1–2008:Q4

	# Loans Modified	Interest Rate Reductions		Principal Balance Reductions		Principal Balance Increases		Term Extensions	
		#	(% total)	#	(% total)	#	(% total)	#	(% total)
2007:Q1	10,940	600	5.3	700	6.2	8,660	76.4	1,380	12.2
2007:Q2	14,600	820	5.4	550	3.7	11,630	77.3	2,050	13.6
2007:Q3	17,720	770	4.1	810	4.3	15,170	81.2	1,940	10.4
2007:Q4	27,150	2,990	9.7	700	2.3	22,520	72.8	4,740	15.3
2008:Q1	36,230	6,010	13.8	900	2.1	32,100	73.8	4,500	10.3
2008:Q2	44,750	9,050	16.4	1,300	2.4	39,750	72.1	5,030	9.1
2008:Q3	62,190	16,280	20.3	940	1.2	56,940	70.9	6,110	7.6
2008:Q4	74,800	28,630	26.7	1,450	1.4	65,960	61.5	11,230	10.5

(2) By Payment Change

	Payment Decreases					Payment Increases				
	#	mean Δ		median Δ		#	mean Δ		median Δ	
		$	%	$	%		$	%	$	%
2007:Q1	2,080	-492	-13.2	-157	-10.0	5,020	106	6.7	62	4.4
2007:Q2	2,060	-464	-12.7	-141	-9.6	7,710	120	7.0	63	4.4
2007:Q3	2,470	-290	-12.9	-125	-9.7	10,380	110	6.7	60	4.3
2007:Q4	5,600	-367	-15.3	-159	-11.7	14,540	100	5.9	59	3.9
2008:Q1	11,500	-358	-14.0	-210	-13.2	18,720	108	6.5	62	4.3
2008:Q2	18,660	-425	-16.1	-239	-14.1	20,770	124	7.4	69	4.1
2008:Q3	31,770	-562	-21.5	-365	-20.2	26,400	124	6.3	63	3.6
2008:Q4	48,000	-503	-22.9	-315	-21.7	22,520	104	6.0	53	3.6

(3) Loan Characteristics of Modified Mortgages

	All Loans					Modifications				
	#	mean	p25	p50	p75	#	mean	p25	p50	p75
FICO (at origination)	1,892,777	706	660	713	762	17,533	622	580	621	662
LTV (at origination)	2,250,162	75	67	79	85	21,675	82	78	80	90
DTI (at origination)	1,346,093	37	28	38	45	13,945	41	35	41	47
Mortgage balance (at origination)	2,267,497	231K	121K	185K	288K	21K	234K	121K	186K	294K
% characterized as										
LTV = 80	14.4					21.7				
Subprime	6.8					47.4				
Fixed	71.2					39.7				
Hybrid ARM	7.7					26.2				
IO-ARM	11.3					13.1				
IO-Fixed	2.1					2.7				
Option-ARM	5.1					12.0				
Option-Fixed	0.3					1.4				
Owner	89.3					96.0				
Investor	7.1					2.6				
Vacation Home	3.7					1.1				
Purchase	51.9					49.0				
Low/no documentation	29.2					20.4				

Notes: These statistics were computed using a 10% random sample of the LPS data. Quantities obtained from the data are multiplied by a factor of 10. The percentages in panels (1) and (2) are taken with respect to the total number of modifications, and *not* loans modified. Thus, there is double-counting in the sense that some loans received multiple types of modifications in a given quarter.

Table 4: Modification Comparison by Payment Change

Private-label Modifications

	Payment Decreases					Payment Increases				
	#	mean		median		#	mean		median	
		$	%	$	%		$	%	$	%
2007:Q1	106	-614	-14.42	-162	-10.85	239	121	6.02	76	3.37
2007:Q2	110	-505	-12.02	-222	-9.30	364	168	7.96	76	3.49
2007:Q3	128	-261	-11.82	-131	-8.42	558	145	7.52	75	3.65
2007:Q4	288	-313	-13.38	-163	-12.36	741	125	6.24	74	3.52
2008:Q1	634	-393	-16.12	-261	-15.65	938	133	6.76	79	4.08
2008:Q2	1,014	-540	-18.94	-334	-17.89	1,241	152	8.14	83	4.08
2008:Q3	1,778	-641	-22.01	-423	-19.95	1,805	137	6.22	70	3.31
2008:Q4	1,993	-565	-21.73	-367	-20.13	1,398	118	5.91	61	3.23

Portfolio Modifications

	Payment Decreases					Payment Increases				
	#	mean		median		#	mean		median	
		$	%	$	%		$	%	$	%
2007:Q1	28	-759	-20.90	-428	-17.19	128	106	7.78	52	5.46
2007:Q2	19	-1172	-25.17	-656	-28.07	222	81	6.11	55	5.28
2007:Q3	31	-395	-17.13	-168	-15.29	255	71	6.13	43	5.37
2007:Q4	90	-474	-11.11	-90	-2.48	292	70	5.50	37	4.29
2008:Q1	187	-369	-10.00	-183	-8.08	331	80	6.59	33	3.97
2008:Q2	309	-304	-10.90	-117	-6.64	405	63	5.59	34	3.56
2008:Q3	376	-585	-25.19	-295	-17.85	359	105	7.04	39	4.26
2008:Q4	616	-794	-31.91	-384	-25.04	389	59	5.48	35	3.51

Table 5: Modifications (Main Sample)

Panel A: Unconditional Percentages

	Concessionary Mods	All Mods	All Mods + Prepayments
Portfolio	0.032	0.087	0.147
Private-label	0.026	0.084	0.155

Panel B: Logit Regressions (12 month horizon)

	Concessionary Mods	All Mods	All Mods + Prepayments
Private-label	-0.003	0.002	0.009
	-1.69	0.58	1.95
Initial Rate	0.001	-0.004	-0.007
	1.45	-5.7	-7.25
LTV Ratio	0	0	-0.002
	-0.24	-1.68	-11.14
$LTV = 80$	0	-0.014	-0.034
	-0.18	-6.25	-11.7
FICO	0	0	-0.002
	-0.02	-0.43	-4.62
$FICO^2$	0	0	0
	-0.39	-0.08	3.95
$FICO < 620$	0.002	0.029	0.034
	0.53	3.43	3.42
$620 \leq FICO < 680$	0.005	0.017	0.024
	1.46	2.95	3.41
Log Original Amount	0.004	0.007	0.022
	3.12	2.96	7.47
Equity at Delinquency	-0.001	-0.003	0
	-0.4	-1.09	0
Negative Equity	-0.006	-0.022	-0.022
	-1.6	-3.17	-1.77
Unemployment	0	-0.002	-0.005
	-0.37	-3.13	-4.37
Refi	0.006	0.015	0.04
	4.14	5.98	11.67
Subprime	0.02	0.037	0.042
	9.32	11.71	10.87
Other Controls	Y	Y	Y
# Mortgages	66,541	66,541	66,541

Panel C: Duration Model

	Concessionary Mods	All Mods	All Mods + Prepayments
Private-label	0.921	1.002	1.018
	-1.41	0.07	0.68
# Mortgages	87,343	87,343	87,343

Notes: Other controls include indicator variables for Jumbo, Option, Hybrid and Interest-Only mortgages, as well as for condos and multifamily homes. Panel B shows the marginal effects of logit regressions with a 12-month horizon, t-statistics shown below the coefficients. Standard errors are clustered at the zip code level. Panel C shows hazard ratio estimates from a Cox proportional hazards model.

Table 6: Modifications (Robustness tests with alternative samples)

Panel A: Concessionary Modifications

	All Loans	Subprime	$FICO < 620$	Non-missing Documentation and DTI	Fully Documented
Portfolio Mean	0.032	0.047	0.034	0.028	0.023
Private-label Mean	0.026	0.037	0.031	0.033	0.037
Marginal Effect	-0.003	-0.004	-0.003	0	0.007
(private-label)	-1.69	-0.94	-0.77	-0.14	1.46
# Mortgages	66,541	33,719	27,639	25,543	18,097

Panel B: All Modifications

	All Loans	Subprime	$FICO < 620$	Non-missing Documentation and DTI	Fully Documented
Portfolio Mean	0.087	0.111	0.097	0.092	0.077
Private-label Mean	0.084	0.103	0.109	0.107	0.124
Marginal Effect	0.002	0.004	0.007	0.006	0.025
(private-label)	0.58	0.61	1.06	0.97	2.94
# Mortgages	66,541	33,719	27,639	25,543	18,097

Notes: Portfolio and private-label means are unconditional probabilities of modification in each sample. Marginal effects are computed from logit models with a 12-month horizon that include all the controls in Table 5. Standard errors are clustered at the zip code level. t-statistics are reported below the marginal effects.

Table 7: Modifications Conditional on 30 Days Delinquency (Logits)

Panel A: Concessionary Mods

	All Loans	Subprime	$FICO < 620$	Non-missing Documentation and DTI	Fully Documented
Portfolio Mean	0.014	0.025	0.016	0.014	0.012
Private-label Mean	0.014	0.021	0.016	0.017	0.019
Marginal Effect	-0.003	-0.005	-0.001	-0.002	0.001
(Logit)	-2.72	-2.31	-0.55	-1.57	0.37
Hazard Ratio	1.03	1.147	1.027	0.969	1.237
(Cox)	0.59	1.83	0.31	-0.42	2.34
# Mortgages	120,558	51,285	43,550	47,993	34,403

Panel B: All Mods

	All Loans	Subprime	$FICO < 620$	Non-missing Documentation and DTI	Fully Documented
Portfolio Mean	0.038	0.056	0.051	0.042	0.052
Private-label Mean	0.042	0.055	0.051	0.047	0.035
Marginal effect	-0.004	-0.007	-0.004	-0.008	-0.001
(Logit)	-2.39	-1.79	-1.22	-3.16	-0.2
Hazard Ratio	1.043	0.951	1.008	0.909	1.065
(Cox)	1.42	-1.05	0.17	-2.23	1.21
# Mortgages	120,558	51,285	43,550	47,993	34,403

Panel C: All Mods + Prepayment

	All Loans	Subprime	$FICO < 620$	Non-missing Documentation and DTI	Fully Documented
Portfolio Mean	0.145	0.195	0.152	0.147	0.13
Private-label Mean	0.174	0.211	0.218	0.185	0.198
Marginal effect	0.023	0.021	0.044	0.016	0.029
(Logit)	7.31	2.98	6.46	3.47	4.54
Hazard Ratio	1.158	1.05	1.181	1.098	1.202
(Cox)	9.09	1.69	5.72	3.88	6.56
# Mortgages	120,558	51,285	43,550	47,993	34,403

Notes: Portfolio and private-label means are unconditional probabilities of modification in each sample. Marginal effects are computed from logit models with a 12-month horizon that include all the controls in Table 5. Hazard ratios are computed from Cox proportional hazard models with the same controls as in Table 5. z-statistics are shown below the coefficients, and t-statistics are reported below the marginal effects. Standard errors are clustered at the zip code level. Sample sizes refer to the logit regressions. The sample sizes for the Cox models are slightly larger.

Table 8: redefault Conditional on Modification

Panel A: Payment Reducing Mods

	All Loans	Subprime	$FICO < 620$	Non-missing Documentation and DTI	Fully Documented
Portfolio Mean	0.308	0.386	0.332	0.228	0.249
Private-label Mean	0.358	0.392	0.371	0.362	0.359
Marginal effect	0.016	-0.001	-0.015	0.03	-0.004
(Logit)	0.66	-0.03	-0.35	0.81	-0.1
# Mortgages	4,626	2,514	1,562	1,475	1,135

Panel B: All Mods

	All Loans	Subprime	$FICO < 620$	Non-missing Documentation and DTI	Fully Documented
Portfolio Mean	0.393	0.53	0.444	0.404	0.403
Private-label Mean	0.449	0.5	0.501	0.482	0.482
Marginal effect	0.008	-0.023	-0.009	-0.021	-0.033
(Logit)	0.58	-0.84	-0.38	-0.97	-1.24
# Mortgages	14,796	7,073	5,344	4,594	3,620

Notes: redefault is defined as loans that are 60 days delinquent, 90 days delinquent, in the process of foreclosure or in REO 6 months after the modification. Marginal Effects refer to the marginal effects of a logit model with a horizon of 6 months. t-statistics shown below the marginal effects. Standard errors are clustered at the zip code level.

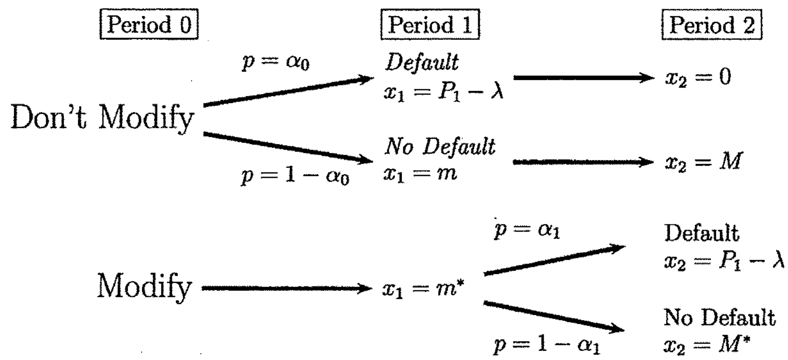
Table 9: Cure Conditional on 60 Days Delinquency

	All Loans	Subprime	$FICO < 620$	Non-missing Documentation and DTI	Fully Documented
Portfolio Mean	0.300	0.257	0.320	0.280	0.299
Private-label Mean	0.256	0.289	0.328	0.289	0.324
Marginal effect	-0.022	0.043	0.004	0.022	0.025
(Logit)	-4.32	4.31	0.44	2.8	2.43
# Mortgages	66,451	33,719	27,639	25,543	18,097

Notes: The dependent variable ("Cure") is defined as a loan that is either current, 30 days delinquent, or prepaid 12 months after the first 60-day delinquency. Portfolio and Private-label means are unconditional probabilities of modification in each sample. Marginal effects are computed from logit models with a 12-month horizon that include all the controls in Table 5. Standard errors are clustered at the zip code level. t-statistics are reported below the marginal effects.

Figure 1:

(1) Model of loan modification



(2) Understanding the lender's gains from modification

Share of borrowers	$1 - \alpha_0$	$\alpha_0 - \alpha_1$	α_1
Description	Borrower always repays Lender loses because borrower would have paid in full	Modification effective Lender gains because modified payments worth more than foreclosure	Borrower never repays Foreclosure is delayed May or may not help lender
Net gain	$m^* + \frac{1}{R}M^* - (m + \frac{1}{R}M)$	$m^* + \frac{1}{R}M^* - (P_1 - \lambda)$	$m^* + \frac{1}{R}(P_2 - \lambda) - (P_1 - \lambda)$
Error	"Type II error" Costly assistance to borrowers who can pay	"Type I error" Don't help borrowers who would have defaulted	"Type III error" Lender loses if R is large or if $P_1 - P_2$ is big

Questions to Wells Fargo Home Mortgage Servicing

Re a hearing of the Financial Services

Subcommittee on Housing and Community Opportunity

"Progress of the Making Home Affordable Program: What Are the Outcomes for Homeowners and What Are the Obstacles to Success?"

On September 9, 2009

Ms. Mary Coffin, Executive Vice President, Wells Fargo Home Mortgage Servicing

- According to your testimony, Wells Fargo has qualified more than 304,000 customers for trial and completed modifications and offered 78,000 trial modifications. However, according to the most Treasury report, this only makes up 11% of your total customers. Why haven't more customers received trial modifications after 6 months?

We are diligently working to increase the number of Trial Modifications that we start. The 11% is difficult to address since this is based on a percentage of loans that are 60 or more days delinquent, and does not address the broad range of eligibility criteria associated with HAMP (loans originated after January 1, 2009, properties that are not the borrower's principal residence, customers with payments already less than 31% of their gross income).

Through September 30, we now have done 62,989 trial and completed *Home Affordable Modifications*; nearly double what the U.S. Treasury reported through August month and 20% of the loans identified as HAMP eligible. Also, using its own programs, Wells Fargo has done 292,005 trial and completed home loan modifications. This brings the total number of modifications Wells Fargo has done this year to 354,994; a 25 percent increase over the total through August.

- Based on your testimony, Wells Fargo has improved the way borrowers submit documentation to ensure documents are processed in a timely manner.
  - What is the average wait time to process a loan modification?
  - How has this improved from the previous wait time?
  - What other measures are in place to improve wait times?

We do not have specific data on average wait times readily available, however we are accelerating our process to qualify borrowers for HAMP in our initial contact, and then send eligible customers the required documentation within 48 hours. On average, we have sustained our monthly internal goals of promptly responding to customers, and have introduced new means to facilitate customer contact during unusually high-volume periods. The rollout of the program specifics challenged our ability to deliver information and guidance to customers. As such, like other servicers, we experienced times where we fell short of our customer service goals despite our best efforts to forecast and prepare for demand. To assist homeowners in crisis, we have hired and trained 5,800 people this year for a total of more than 13,000 U.S.-based staff focused on home retention issues. New customer service reps begin work in the least complex areas and advance – over time – to handle more complex customer situations. Mentors sit with our new recruits (who receive four weeks of training) when assisting customers. We have also automated our systems to back up our customer service reps with information they can use to help customers. This has been especially important as the government guidelines have evolved over time. In addition, we are using document imaging to assist with the mountain of paperwork required to ensure only those homeowners truly in need are getting assistance.

- What measures are in place to assess quality control and assurance? How are you making sure that the borrowers who need assistance the most are receiving such assistance?

We have a number of quality control programs and measures in place. We routinely audit loans on a random basis, we are implementing a process whereby we re-review any loan that was denied a HAMP modification to ensure such denial was accurate. To ensure those most at risk are receiving priority, we attempt to segregate and score the potentially eligible loans based on delinquency and time to foreclosure to ensure those loans receive emphasis. As a last safeguard, before a home is moved to foreclosure sale, we conduct a final loan review to ensure all options have been exhausted. If we find that another option is possible, through HAMP or our own programs, we will institute a moratorium to give the customer time to qualify. We also work with the customer up to the point of the actual sale, and we have numerous cases in which customers qualify for newly available options at the 11th hour.

- There continue to be reports of some participating servicers refusing to offer modifications under the President's plan as well as staff ignorance of the plan's provisions. What steps have you taken or will undertake to ensure that your staff is adequately trained?

We certainly do not have a practice or policy of refusing to offer modifications under HAMP. We fully support the program, and are diligently working to properly train our more than 13,000 employees, including 5,800 hired this year to deal with the increase in volume related to home retention issues, including HAMP.

We have further enhanced our support systems, our training and our re-training to aide our service representatives in appropriately communicating modification programs and guidelines as they continue to change and expand to help more borrowers.

- Furthermore, borrowers are not offered an explanation for the reason for denial or how they may cure the reasons for denial. Why are borrowers not given a reason for denial? What steps will you take to ensure that all borrowers are provided a reason for denial and information on how they may cure the problem?

We are in the process of developing a letter to every borrower who is denied a HAMP modification. This letter will include the reason for the denial, however most reasons for denial are things that simply can not be cured by the borrower (loans originated after January 1, 2009, properties that are not the borrower's principal residence, customers with payments already less than 31% of their gross income).

- On average, how many times does a borrower have to call before the borrower connects with a servicer?

This should be one call. Follow-up calls may be necessary in order to permit the borrower to retrieve appropriate documentation and explain the program in detail.

- In your opinion, what are the obstacles to implementing more effective types of loan modifications?

We are encouraging Treasury to implement a short-term modification under HAMP, based on unique circumstances that can be remedied within a reduced time frame. We believe that such an option would be helpful to homeowners who experience a limited period of unemployment or otherwise have experienced a temporary reduction of income.

There also remains a gap in HAMP with respect to interest only loans. Converting an interest only loan into a fully compliant HAMP modification is difficult because the payment often must increase in order to achieve a fully amortizing, and fully escrowed mortgage payment.

- How many non HAMP loan modifications have you done since March 4?

As of September 30, 2009 we have placed over 292,000 borrowers into a non HAMP workout solution since the beginning of the year.

- Why were some homeowners provided non-HAMP loan modifications? Did they get formally turned down from a HAMP loan modification?

This is primarily because the borrower was already below the 31% housing debt to income ratio, which does not qualify that borrower for HAMP. In those cases, or in other cases where a borrower is not eligible for HAMP we continue to work with the borrower to find some form of loan modification or workout for their situation.

- How many of the non-HAMP recipients were evaluated for HAMP loan modifications?

Based on the timing of the HAMP program, many of the non-HAMP modifications in 2009 were entered into prior to HAMP's availability. Following implementation, HAMP is the first option we review for every eligible borrower.

- Between the HAMP and non-HAMP loan modifications, which provided greater returns to a) the servicer, and b) the investors? What were the differences in terms for the borrowers?

There is no general answer that can be provided to this question. Every borrower, modification, and investor is different. Therefore the "returns" provided to each can vary widely from loan to loan. Again, HAMP is the first option we review for every eligible borrower, and if that borrower qualifies and meets all other HAMP requirements, that is the option they are provided.

Questions to Chase Home Lending, JPMorgan Chase

Re a hearing of the Financial Services

Subcommittee on Housing and Community Opportunity

"Progress of the Making Home Affordable Program: What Are the Outcomes for Homeowners and What Are the Obstacles to Success?"

On September 9, 2009

Ms. Molly Sheehan, Senior Vice President, Chase Home Lending, JPMorgan Chase

- Can you describe the similarities or differences between your company's foreclosure prevention plan and the Making Home Affordable Program? *The Making Home Affordable (MHA) Program is the centerpiece of Chase's foreclosure prevention plan, but covers only customers that meet the eligibility criteria established by the Department of Treasury for the MHA Program. For customers that are not eligible or do not qualify for the MHA Program, Chase offers its own proprietary programs which allow greater latitude in product features and eligibility.*
- How does JPMorgan Chase plan to increase the level of eligible homeowner enrollment? *Chase is undertaking several outreach efforts to overcome borrower contact challenges, including creative national marketing campaigns, borrower event hosting, targeted regional marketing campaigns utilizing our 27 homeownership centers, and aggressive calling efforts.*

- What measures are in place to assess quality control and assurance? How are you making sure that the borrowers who need assistance the most are receiving such assistance? *Chase uses a combination of automated tools and standard underwriting policies to provide borrowers with a consistent evaluation and resolution based upon individual financial situations and account terms. Also, Chase has prioritized its efforts to assist delinquent borrowers by implementing an expedited process to begin trial periods upon the initial contact with the borrower, with verification of financial criteria occurring after a trial is underway, so customers receive payment relief as early in the process as possible. In addition, Chase has implemented a Quality Control Program to validate its processes are being properly followed and has an independent foreclosure review process pre-referral to foreclosure as another control to monitor that proper foreclosure prevention options are being offered to borrowers.*

- There continue to be reports of some participating servicers refusing to offer modifications under the President's plan as well as staff ignorance of the plan's provisions. What steps have you taken or will undertake to ensure that your staff is adequately trained? *Chase has adopted its participation in the MHA program* *as a matter of policy, adherence to which is required by all staff members. In furtherance of that policy, Chase has developed several training courses specifically to educate new and existing staff on the parameters of the Making Home Affordable program and its implementation within Chase. Chase has also incorporated training provided by Fannie Mae as Agent of the Treasury into its proprietary curriculum.*

Furthermore, borrowers are not offered an explanation for the reason for denial or how they may cure the reasons for denial. Why are borrowers not given a reason for denial? What steps will you take to ensure that all borrowers are provided a reason for denial and information on how they may cure the problem? *Customers that apply for the program and do not qualify for either an MHA or a Chase modification are provided a written notice and reason for denial. These customers will then be considered for other foreclosure prevention options, such as forbearance plans, deeds in lieu and short sales. If a customer qualifies for the either the MHA or Chase Modification Program and fails to submit required documentation or payments, there is a specified set of follow up steps that are taken to attempt to avoid the trial plan being broken.*

- On average, how many times does a borrower have to call before the borrower connects with a servicer? *We do everything we can to reach borrowers and allow them to reach us. We monitor call abandonment rates and add staff when we see a need to increase our capacity to serve our customers.*

- In your opinion, what are the obstacles to implementing more effective types of loan modifications? *We feel the current modification programs can be effective when borrower response is achieved, but this remains the greatest challenge. We have also suggested to the MHA Program Administrator that there are number of areas where we feel the documentation can be further streamlined to improve customer pull through.*

- How many non HAMP loan modifications have you done since March 4? *From March through August 30, 2009, 47,782 non-HAMP modifications have been completed. During this same period, Chase approved over 144,000 trial plans under the MHA Program and an additional 88,000 trial plans under the Chase Program.*

- Why were some homeowners provided non-HAMP loan modifications? Did they get formally turned down from a HAMP loan modification? *Borrowers may receive a non-HAMP loan modification if they do not qualify for HAMP or decide not to participate in HAMP. If borrowers do not qualify for HAMP or a Chase modification program, they receive a written notice and reason for denial and will then be considered for other types of foreclosure prevention options such as forbearance plans, deeds in lieu or short sales.*

- How many of the non-HAMP recipients were evaluated for HAMP loan modifications? *Since execution of the Servicer Participation Agreement in April, all borrowers requesting assistance have been evaluated for HAMP. Additionally all potentially eligible borrowers that are more than two payments late and are not already being considered for a modification or other loss mitigation option have received a solicitation to contact Chase to be evaluated for a HAMP modification.*

- Between the HAMP and non-HAMP loan modifications, which provided greater returns to a) the servicer, and b) the investors? What were the differences in terms for the borrowers? *Given that the first trial plans under MHA are just now coming up to be converted to permanent modifications, we have insufficient data at this time to conduct an analysis comparing the returns to servicer and investor between HAMP and non-HAMP programs. The non HAMP modifications offered by Chase allow greater latitude in product features, documentation and eligibility requirements.*

09/08/2009 18:13 FAX 5105684582 002/004

NID HOUSING COUNSELING AGENCY
A HUD APPROVED ORGANIZATION
NATIONAL OFFICE
25 YEARS O EXCELLENC

September 8, 2009

Honorable Maxine Waters
Chairwomen
Housing and Community Opportunity
2344 RHOB
Washington, D. C. 20515

RE: 09/09 Making Home Affordable Program (MHA) Hearing

Dear Chairwoman Waters:

The MHA program can only achieve intended results if Servicers, Banks owning the MBS's and or mortgages and Investors are held accountable for providing **workout solutions within 30 days** of receiving the third party authorization from the HUD approved counseling agency or receiving a **industry standard workout package** from the borrower; **substantial penalties should be assessed for non-compliance to this 30 day turnaround mandate.**

There has been substantial investigative evidence from the press and empirical data from a diverse group of credible industry sources detailing the dysfunctional nature of the lending industry's efforts to effectively implement and utilize the MHA program. Please see the attached one page summary of the feedback provided to NWA, manager of the NFMC program, from NFMC program grantees.

It is our view, initially expressed when Congress was developing the NFMC legislation, the first priority for banks and investors is to limit loses and maximize individual corporate/investor returns in a competitive environment with mortgage loan servicers being their lead agent in accomplishing this goal. Government efforts of providing financial support to the lender/servicers is being misused as leverage to improve individual corporation financial soundness to the detriment of families facing foreclosure, communities impacted by the prolonged foreclosure environment, the FHA insurance fund and the overall economic recovery effort.

The most recent S&P/CS indexes report a decline of home values in the lowest tier, primarily urban/minority and rural areas, of 45%, middle market areas, 33% and top tier areas of 27% since 2006. High foreclosure rates are a primary driver for this unusually high decline in across the board property values, which the MHA and NFMC programs, along with an enhanced FHA insurance program, were designed to help stem and help lead the housing market recovery

NID HOUSING COUNSELING AGENCY
A HUD APPROVED ORGANIZATION
NATIONAL OFFICE
25 YEARS OF EXCELLENCE

efforts. The same banks and lenders who felt we no longer needed the FHA insurance program back in 1995 now use it as their primary loan program.

FHA/VA insured 40% of all home mortgages in 08/09 originated by these same institutions and the FHA mortgage market share has grown from 3% in 2006 to 23% by 06/09, as reported by Inside Mortgage Finance. Inadequate utilization of the MHA program and pushing the actuarial soundness of the FHA/VA insurance fund to the limits represents a double subsidy to the conventional mortgage lending industry while also prolonging the economic recovery.

NAREB-Investment Division (NID) and the 53 urban communities in 22 states that we have served for 25 years thanks Chairwoman Waters and the House Financial Services Subcommittee on Housing and Community Development for addressing the critical issue of lender/servicer/investor accountability in adequately implementing and utilizing the Making Home Affordable Program.

Sincerely,

Jacqueline Carlisle
Executive Vice President, NID

Making Home Affordable Feedback from National Foreclosure Mitigation Counseling Program Grantees August 21, 2009

On March 4, 2009, President Barack Obama launched a new effort, the Making Home Affordable (MHA) program, to stabilize our housing market and help up to 9 million Americans reduce their monthly mortgage payments to more affordable levels.

The National Foreclosure Mitigation Counseling (NFMC) Program was created by Congress in December 2007 to address the nation's subprime foreclosure crisis. Three appropriations totaling $410 million have enabled thousands of housing counselors throughout the nation to assist more than 600,000 homeowner as of July 31, 2009.

The counselors in the NFMC Program are working in the MHA program in two ways – counselors assist clients who are trying to determine if they are eligible for a MHA modification or refinance, and they work with clients that have received a refinance or modification but have high back end debt to income ratios. Because these counselors are on the front lines in the foreclosure crisis, the NFMC Program has been holding feedback sessions on what they are finding regarding the implementation of the program.

Several themes have formed in the feedback the counselors provided on four conference calls (July 1, July 15, July 29, and August 12). They are:

(1) Difficulty trying to communicate with servicers
- Servicers will not work with counselors
- Servicer representatives and processes are difficult in general
- Servicers are bringing third parties and collection agencies into the process
- Servicers change contact information frequently and require documents to be resent
- Servicers ask for counselors' Social Security Numbers

(2) Servicers are not following the guidelines of the Making Home Affordable program
- Servicers will not help current homeowners and tell them to become delinquent
- Servicers won't disclose terms of a trial modification or payment breakdown
- Servicers give out wrong information about the program
- Servicers offer workouts that are not MHA
- Servicers are not halting foreclosures while reviewing files
- Servicers are extending trial modifications/delaying permanent modifications

(3) Frustrations with the system as a whole
- Servicers won't give a reason for denial
- It takes too long to get a response on modification requests
- Central portal for submitting modification requests

The feedback we have received on each section is discussed below.

ANTONIO R. VILLARAIGOSA
MAYOR

July 27, 2009

The Honorable Shaun Donovan
Secretary
U.S. Department of Housing and Urban Development
451 7th Street, S.W.
Washington, D.C. 20410

Dear Secretary Donovan

As representatives of a city with one of the largest foreclosure problems, we were very heartened when President Obama's announced the Making Homes Affordable (MHA) program. This program has been one of the most significant recent policy innovations in the country's efforts to address the foreclosure crisis. It offers the hope of widespread relief for homeowners facing foreclosure by encouraging systematic refinancing and loan modifications. Like you, we have been disappointed with the initial efforts by financial institutions to institute this promising program, but are encouraged that you are working with the Secretary of the Treasury and the financial sector to improve results.

It is our hope that MHA becomes more accessible to the people of Los Angeles who are currently threatened with losing their homes. As in other parts of the country, the tragedy of the foreclosure crisis is destabilizing neighborhoods and families. However, many zip codes in Los Angeles have experienced significant decline in value in the last year. This dramatic drop in value makes it difficult for banks and mortgage holders to participate in MHA. In addition, the city does not receive regular reporting from the outcomes of people seeking to refinance of modify their loans, making it difficult to track and leverage locally-controlled resources to help these families.

Given this situation, we would ask that you consider the following modifications to the program:

- Regular reporting to local government from banks on numbers, locations, and terms of modifications of homes within the respective jurisdictions.
- Regular reporting on the turn around time and staffing allocated to modifications

200 NORTH SPRING STREET • LOS ANGELES, CALIFORNIA 90012
PHONE: (213) 978-0600 • FAX: (213) 978-0750
EMAIL: MAYOR@LACITY.ORG

The Honorable Shaun Donovan
July 27, 2009
Page 2

- Requiring banks to designate a liaison to local government who can help mitigate the impacts of vacant properties and coordinate pending foreclosure sale dates when a modification has been agreed upon.
- Streamline the modification of loans – which could be achieved through the adoption of a standard web-based modification platform or through coordinated meetings directly between servicers and housing counseling agencies to facilitate high volume loan modifications.
- Concerted outreach to stop consumers from spending money on fraudulent modification schemes and encourage families to get help through MHA.
- Requiring banks engage in a specific percentage of modifications through Making Homes Affordable.

We are encouraged by your commitment to making this program a success and by your overall dedication to advancing inventive housing and urban development policies equal to the challenges we face. We look forward to working with Secretary Geithner and you to realize the full potential of the Making Homes Affordable program.

Very truly yours,

ANTONIO R. VILLARAIGOSA
Mayor

ERIC GARCETTI
Council President

HERB J. WESSON, JR.
Councilman, 10th District

HOUSING POLICY COUNCIL
THE FINANCIAL SERVICES ROUNDTABLE

Statement for the Record

John H. Dalton

President, Housing Policy Council

Subcommittee on Housing and Community Opportunity

Committee on Financial Services

United States House of Representatives

September 9, 2009, 10:00 a.m.

Hearing on

Implementation of the Making Home Affordable Program

2128 Rayburn House Office Building

INTRODUCTION

Chairman Waters, Ranking Member Capito and Members of the Subcommittee, thank you for the opportunity to present the views of the Housing Policy Council on the implementation of the Administration's Home Affordable Modification Program (HAMP), as well as the other important components of the mortgage lending industry's efforts to assist homeowners in distress and prevent foreclosures. The member companies of the Housing Policy Council are working hard to implement HAMP, and are continuing other comprehensive efforts to contact and provide loan modifications and other workout solutions to their mortgage customers who are experiencing difficulty.

OVERALL INDUSTRY EFFORTS

The member companies of the Housing Policy Council (HPC) are committed to working with their customers to find solutions that preserve homeownership and avoid foreclosure whenever possible. We have been working hard in this area for a number of years and mortgage servicers have voluntarily reported their results since 2007 through the HOPE NOW Alliance.

The latest industry data collected by HOPE NOW shows:

- Since January 2009, servicers have provided 1.77 million workout solutions to homeowners to avoid foreclosure.
- Since July 2007, servicers have provided more than 4.9 million workout solutions to homeowners.
- HPC companies and other HOPE NOW servicers work with every at-risk homeowner they can reach. There is a wide-variety of solutions available including, but not limited to, the new Government supported Home Affordable Modification Program (HAMP).

ADMINISTRATION'S HOME AFFORDABLE MODIFICATION PROGRAM

The Housing Policy Council supports the Administration's efforts to help at-risk homeowners through the Home Affordable Modification Program (HAMP). As you know, in its first report on HAMP on August 4, the Administration reported that the Program was having a positive impact. In the initial stages of HAMP, participating servicers offered more than 400,000 trial modifications to homeowners and more than 230,000 trial modifications were underway as of early August. These new modifications under HAMP are in addition to the non-HAMP workouts that continue to be offered to troubled homeowners by the industry. HAMP is a major new program and while it was announced on March 4, the actual requirements needed to implement the Program were developed and communicated to the industry over the next several months from April through June. Servicers had to determine if they could meet the requirements for HAMP for their non-GSE loans and have signed up for HAMP at different times during the initial period. The first report on August 4 was a positive snapshot, but as HAMP becomes more fully implemented, we believe its impact will continue to grow. We agree that more can be done, and our members will continue to increase their efforts to assist at-risk homeowners.

All servicers for Fannie Mae and Freddie Mac must participate in the Program for GSE-owned loans. Servicers for private label securities must examine their ability to apply HAMP to loans in private mortgage-backed securities. Those servicers have been making those decisions and more continue to join the Program. In evaluating the Treasury Department's August 4 and subsequent reports on the trial modifications initiated by servicers in HAMP, it is important to keep in mind that servicers have different loan servicing portfolios and joined the Program at different times. The types of loans being serviced and the date a servicer enters the Program can affect the reported number of trial modifications they have offered and initiated. We appreciate the Administration's willingness to work with servicers in the implementation of this Program and we hope the reporting on the Program will fully reflect the variety of issues facing servicers as they join and administer HAMP.

It is the responsibility of our industry to continue to provide solutions for our consumers who are facing difficulty. We continue to work hard to provide solutions to homeowners who have a desire and an ability to pay their mortgage with some assistance. HAMP will be an effective option for a growing number of homeowners. For those who do not qualify for HAMP, servicers are actively offering other workouts to their customers with the goal of avoiding foreclosures whenever possible.

The industry is committed to making the Home Affordable Modification Program as effective as possible. Mortgage servicers are in regular communication with Treasury and other Administration officials about the Program, companies communicate individually and we also work on issues that affect all servicers through the HPC and through the very effective working groups established through the HOPE NOW Alliance.

In a meeting hosted by Treasury at the end of July, HPC mortgage servicers and other servicers in the HOPE NOW Alliance offered Treasury a list of recommended improvements to HAMP to help streamline the mortgage modification process and make the Program more effective. Our members will continue to work cooperatively with the Administration and through HOPE NOW to strengthen the implementation of HAMP and to reach as many at-risk borrowers as possible. We support the Program and believe the Administration is on the right track by focusing on making loans affordable for at-risk homeowners. However, HAMP will continue to need to be refined to maximize its impact.

INDUSTRY EFFORTS TO ASSIST HOMEOWNERS ARE CONTINUING AND INCREASING

HPC member companies continue to work to keep as many people in their homes as possible. They are implementing HAMP and also offering other loan modifications and workouts to homeowners who do not qualify for HAMP, but need help to stay in their home. Servicers are also working hard to increase their capacity to respond to homeowners and offer aid.

HPC companies are taking individual steps that include:

- Hiring and training thousands of new staff in servicing and loss mitigation;
- Creating special offices and retail locations dedicated to homeowners in difficulty;
- Phone and mail campaigns to reach at-risk homeowners.
- Company outreach events with non-profits in select markets.

In addition, HPC member companies are engaged in cooperative efforts, such as participating in the HOPE NOW Alliance. The HOPE NOW Alliance is a broad-based voluntary collaboration between lenders, HUD-approved housing counselors, investors, mortgage market participants and trade associations. Activities of the HOPE NOW Alliance include:

- HOPE NOW mailings: The members of the Alliance have mailed over 4.9 million letters, averaging 200,000 per month, to at-risk homeowners offering assistance and urging them to call their servicer or the Homeowners HOPE hotline.
- Supporting the Homeowner's HOPE Hotline, 888-995-HOPE, by funding independent non-profit counseling for their customers, at no cost to the consumer.
- HOPE NOW is educating borrowers on HAMP through the HOPE Hotline and homeownership preservation events.
- HOPE NOW Homeowner Outreach Events: From March 2008 thru August 2009, HOPE NOW has held more than forty-six events across the country; reaching nearly 40,000 homeowners and providing them free counseling and an opportunity to meet with their servicer. Outreach partners include: Major mortgage servicers; NeighborWorks America, Fannie Mae, Freddie Mac, the Federal Reserve Banks and the US Treasury
- In July and August, HOPE NOW assisted 2,000 homeowners in the Washington DC, MD and VA area; 1,500 in Las Vegas; 2,800 in Phoenix; in June, 1,153 in Fresno and Bakersfield California, and 741 in St. Paul, MN; In April and May 3,300 homeowners in Atlanta, GA.; and, 3,900 in Orlando and Miami, FL. There are thirty HOPE NOW in-person homeowner outreach events planned for 2009. The next is September 17 in Boston, MA.
- The Homeowner's HOPE Hotline, 888-995 HOPE, is receiving thousands of calls per day from homeowners who are connected to a network of HUD-certified non-profit agencies for free counseling and can be connected to their servicer.

In addition to the actions listed above, servicers will continue to work through the HOPE NOW Alliance on these issues:

- <u>Technology</u>: HOPE NOW operates a website that provides homeowners with another option to contact their servicer or a certified counselor. HOPE NOW Servicers are exploring upgrading this to a "one-stop" web portal to provide improved communication with borrowers on loan workout options and applications.
- <u>Best Practices</u>: HOPE NOW serves as a work center and clearing house for servicers as they work toward best practices in servicing and assisting homeowners.

- Coordination with Government: HOPE NOW coordinates and shares information between the government, the GSEs and servicers as they implement HAMP and other solutions to assist homeowners.
- Cooperation with Non-Profits: HOPE NOW serves as a contact and facilitator between counseling agencies and servicers.
- Reporting on Results: HOPE NOW will continue to collect data on actual loan workouts and modifications and voluntarily publish these results.

CHALLENGES FOR HOMEOWNERS AND SERVICERS:

Unemployment: Unemployment continues to be a troubling issue. With unemployment approaching 10 percent, it is affecting an increasing number of homeowners, particularly those who have prime mortgages. The crisis facing homeowners is now most directly related to problems in the economy, rather than types of mortgages. If a homeowner is unemployed or has lost income, it makes it difficult to pay any debt. Regardless of why a homeowner is in trouble, they should contact their servicer or a non-profit counselor. In addition, the HOPE NOW Alliance is working closely with the U.S. Department of Labor to find solutions for the growing number of unemployed borrowers.

Homeowners with High Debt: Homeowners with high levels of non-mortgage debt face greater challenges in staying in their home. HAMP is the first wide scale program for uniform modifications that provides an affordability ratio of 31% housing debt to income for homeowners who need to have their payments reduced to be able to stay in their homes. Under HAMP, servicers are required to make changes to reduce the borrowers' housing debt ratio to 38% and then the government will share the cost of reducing it to a more affordable 31%.

For homeowners with significant other household debt - debts greater than 55% of income- counseling is required under HAMP. This is a necessary and positive requirement. Servicers are encountering a large number of homeowners who may already have a housing debt ratio of 31% or less, but they have excessive other non-mortgage debt that makes a loan modification or other workout difficult to achieve. This is an issue that will require additional review.

DELINQUENCIES, FORECLOSURE STARTS AND SALES:

HOPE NOW data indicates that there are roughly 2.9 million borrowers who are 60 days past due on their mortgages. This is a real challenge, but there are some encouraging signs as well. While foreclosure starts increased slightly from 251,340 in June to 283,682, in July, completed foreclosure sales decreased from 92, 661 to 89,173. The 60-day plus delinquencies show a slight increase of 5.9% or 3.1 million homeowners in July. As HOPE NOW reported on its July data, more than 253,000 borrowers were helped through loan work out solutions, while foreclosure sales dropped. This data reflects the industry's on-going efforts to assist homeowners and shows real progress that HAMP will continue to contribute to. At the same time, the economy continues to show weakness; unemployment has increased; and certain markets in California, Las Vegas, Phoenix Arizona and Florida face continued challenges in the number of properties at risk of foreclosure. The government and industry must continue to work together to address these issues.

A NOTE ON MORTGAGE HELP SCAMS

It is imperative that at-risk homeowners get assistance from reputable companies and HUD-certified non-profit agencies. They should be wary of paying third parties for services they can obtain directly from their mortgage servicer or a non-profit counselor. The HOPE NOW Alliance has been working with the Federal Trade Commission, the FBI and states' attorneys general to eliminate mortgage scams that hurt vulnerable consumers. HOPE NOW educates borrowers on how to recognize these scams through the Homeownership Preservation Foundation's Hotline (888-995-HOPE), its website (www.hopenow.com) and at consumer outreach events.

HOMEOWNERS IN DIFFICULTY SHOULD:

It is critical to repeat this basic message. Homeowners in difficulty should:

- Write to their lender/servicer
- Respond to letters and calls from their servicer
- Call: 888-995-HOPE
- Visit: www.hopenow.com
- Visit: www.makinghomeaffordable.gov

CONCLUSION

The Housing Policy Council supports the Home Affordable Modification Program (HAMP) and the other Making Home Affordable programs. Our members are working to implement the Program and offer trial modifications to every homeowner who qualifies. The Program will face implementation challenges, as well as new challenges from homeowners who have a significant loss of income or high levels of non-mortgage debt. It is important to stress that the industry also continues to offer other foreclosure prevention solutions to homeowners who do not qualify for HAMP. We want to continue to work with the Administration and Congress to address the evolving challenges facing homeowners and the mortgage industry. Our goal is to keep every American in their home who has a desire to stay in the home and an ability to meet their challenges, but needs some assistance. Thank you for considering our views.