

# U.S. DEPARTMENT OF THE TREASURY

## Press Center

### **Treasury Assistant Secretary for Financial Stability Herbert Allison Written Testimony before the House Financial Services Committee “The Private Sector and Government Response to the Mortgage Foreclosure Crisis”**

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Chairman Frank, Ranking Member Bachus, and members of the House Financial Services Committee, thank you for the opportunity to testify today about the Administration's comprehensive initiatives to stabilize the U.S. housing market and support homeowners.

The Administration has made strong progress in ramping up the Making Home Affordable<sup>®</sup> programs. Over 680,000 borrowers have entered into trial modifications and are already achieving significant savings. For the program to succeed in the longer run, however, we recognize that we face several key challenges: reaching more borrowers who are eligible for the program, but who often don't know how to get help or are not starting trial modifications even when approved; helping more borrowers in trial modifications convert to permanent modifications so sustainable help can be offered; and continuing to improve transparency and enhance the borrower experience, so the public and homeowners can be confident the program is assisting eligible homeowners as intended. We can all do better in ensuring that the Making Home Affordable programs are a success.

On February 18, the Administration announced the Homeowner Affordability and Stability Plan – a broad set of programs designed to stabilize the U.S. housing market and keep millions of homeowners in their homes.

The Administration has taken broad action to stabilize the housing market, including providing support for mortgage affordability across the market. Continued support for Fannie Mae and Freddie Mac and the Treasury's Mortgage Backed Securities (MBS) purchase program, along with MBS purchases by the Fed have helped to keep interest rates at historic lows. Over 3 million Americans have taken advantage of these lower rates in 2009 to save money through refinancing. For example, on a median house purchase of \$200,000, a one-percent reduction in interest rates, on a purchase or refinance, saves the family over \$120 per month for the thirty-year life of the loan -- real help for America's homeowners. We are working to provide increased access to financing for state and local housing finance agencies, which provide sustainable homeownership and rental resources in all 50 states, for working Americans. In addition, the first-time homebuyer tax credit has helped hundreds of thousands of responsible Americans purchase a home. The American Recovery and Reinvestment Act also supported the Low Income Housing Tax Credit/Tax Credit market by creating an innovative Treasury Tax Credit Exchange Program (TCEP) and providing gap financing through the HUD Tax Credit Assistance Program (TCAP), in combination these programs are estimated to provide over \$5 billion in support for affordable rental housing. The Recovery Act also provided \$2 billion in support for the Neighborhood Stabilization Program, which is designed to rebuild value in areas hardest hit by foreclosures, in addition to \$4 billion provided for the program in the Housing and Economic Recovery Act.

There are clear signs that our efforts are having a substantial impact. While there are still risks, we are seeing signs of stabilization in housing, as housing inventories continue to fall. House prices measured on a year-over-year basis are declining less rapidly, with some house price measures posting increases in recent months. Conventional 30 year fixed rate mortgages remain near historic lows, and more than three million GSE borrowers refinanced in 2009 into loans with lower interest rates, and have saved \$150, on average per month.

The Home Affordable Modification Program<sup>SM</sup> (HAMP<sup>SM</sup>), which provides eligible homeowners the opportunity to significantly reduce their monthly mortgage payment, is a key part of this effort, designed to help millions of homeowners remain in their homes and prevent avoidable foreclosures. As of November 17, over 680,000 borrowers are in active modifications, saving an average of over \$550 a month on their monthly mortgage payments. Servicers report that over 900,000 borrowers have received offers to begin trial modifications.

HAMP is on track to provide a second chance for up to 3 to 4 million borrowers by the end of 2012, averaging over 20,000 trial modifications started per week. As with any new program of this size and complexity, HAMP faces a number of challenges, including converting trial modifications to permanent modifications and helping Americans stay in their homes in an environment of elevated unemployment. The Administration is working to address these challenges and to maximize the effectiveness of the HAMP program going forward.

Our most immediate and critical challenge is converting trial modifications to permanent modifications. All mortgage modifications begin with a trial phase to allow borrowers to submit the necessary documentation and determine whether the modified monthly payment is sustainable for them. As the first round of modifications reaches the deadline to convert, Treasury is implementing an aggressive conversion campaign to address the challenges that borrowers confront in receiving permanent modifications.

Currently servicers report that about 375,000 trial modifications will have finished a three month trial period with timely payments before 12/31/2009. Informal survey data from servicers indicate receipt of complete documents in about 30% of active trial modifications – these modifications where borrowers have returned all required documents need to be decisioned by servicers as quickly as possible. For other borrowers, servicers report that the large majority are current on their payments, but have some of the required documentation missing from applications. Housing counselors and homeowners report that servicers are losing documents, while servicers report that homeowners are not providing documents despite repeated outreach. Thousands of borrowers have successfully converted trial modifications to permanent modifications – but this is a low number compared to the total number of trial modifications. Although we know that not every borrower will qualify for a permanent modification, we are disappointed in the permanent modification results thus far. We all need to do better at converting borrowers to permanent modifications. For that reason, the program's central focus at this point is converting borrowers into permanent modifications where they qualify. As part of our conversion drive, the Administration remains committed to transparency – and to that end we will provide servicer specific data on permanent modifications this Thursday in our monthly public report.

Last week, Treasury kicked off a "Mortgage Modification Conversion Drive" including a number of aggressive actions to increase the number of permanent modifications. Those actions include the following:

- Streamlining the application process for servicers and borrowers. Standardized paperwork makes it easier for borrowers to request a modification and increases the efficiency with which servicers evaluate those requests.
- Publishing servicer-specific conversion rates in the next public report.
- Punitive measures for servicers. Those that do not meet their obligations under the program contracts will be subject to consequences which may include corrective action, withholding or clawbacks of servicer incentive payments and other remedies.
- Increased communication with servicers. On December 7, we held an in-person meeting with servicers in Washington, DC to focus on converting borrowers to permanent modifications where they qualify.
- Requiring each servicer to report to us twice a day on conversion progress.
- The implementation of "SWAT Teams," made up of Treasury staff, as well as staff from Fannie Mae, who have been sent to the largest servicer shops this week to ensure that servicers are processing conversions in a thorough, timely and efficient manner.
- New tools for borrowers have been added to our website, [www.makinghomeaffordable.gov](http://www.makinghomeaffordable.gov) to help borrowers submit their documents.
- Engaging key state and local organizations and housing counseling groups in an outreach campaign to help borrowers submit the documents required to convert to permanent modifications.

## Mortgage Modification Conversion Drive

We are focused on reaching homeowners who are eligible for permanent mortgage modifications. The mortgage modification conversion drive includes a number of elements mentioned above, but are outlined in more detail below.

- **Servicer Accountability.** In addition to the Administration's ongoing efforts to hold servicers accountable for their commitment to the program and responsibility to borrowers, the following measures will be implemented during the conversion campaign:
  - We required the seven largest servicers (representing nearly 90% of all active Trial Period Plans) to submit conversion plans demonstrating their ability to reach a decision on each loan for which they have documentation and to communicate either a modification agreement or denial letter to those borrowers on or before December 31, 2009. We also required servicers to submit their strategy for obtaining documentation from borrowers who are currently making payments under a trial period plan but have not submitted all of their documentation. Treasury reviewed the adequacy of these plans and required servicers to correct any deficiencies.
  - To emphasize for servicers the importance that Treasury places on the Conversion Campaign and to assist servicers in successfully transitioning the maximum number of eligible borrowers to permanent modifications, teams comprised of Treasury and Fannie Mae account liaisons are being assigned to the offices of the top seven servicers. The imbedded teams will monitor daily progress against the servicer's plan and help resolve policy issues that are impeding the conversion process. Daily progress will be aggregated at the end of each business day and reported to the Administration.
  - The December MHA Servicer Performance Report will include the number of active trial period modifications that will convert by the end of the year if all borrower documents are received, sorted by servicer and date, and support a permanent modification.
  - Servicers are being required to report to the Administration the status of all trial modifications in their portfolio in order to provide a more comprehensive understanding of the program's overall performance and effectiveness.
- **Web tools for borrowers.** Because the document submission process can be a challenge for many borrowers, the Administration has created new resources on [www.MakingHomeAffordable.gov](http://www.MakingHomeAffordable.gov) to simplify and streamline this step. A new section of the web site includes comprehensive information about how the trial phase works and what borrower responsibilities are to convert to a permanent modification. Other features include:
  - A new instructional video which provides step by step instructions for borrowers;
  - Links to all of the required documents and an income verification checklist to help borrowers request a modification in four easy steps;
  - A conversion guide for borrowers who are in the trial phase;
  - New web banners and tools for outreach partners to drive more borrowers to the site and Homeowner's HOPE™ Hotline (888-995-HOPE);
  - An outreach toolkit for housing counselors, state, local and community leaders to use in their direct outreach to constituents.
  - Contact information for the U.S. Department of Housing and Urban Development to report suspected housing discrimination.
- **Engagement of state, local and community stakeholders.** Through the conversion drive, the Administration is engaging all levels of government - state, local and county to both increase awareness of the program and expand the resources available to borrowers as they navigate the modification process.
  - HUD is engaging staff in its 81 field offices to distribute outreach tools. HUD will also encourage its 2700 HUD-Approved Counseling Organizations to distribute outreach information to participating borrowers to ensure that they have the tools to serve as trusted resources
  - By engaging the National Governors Association (NGA), National League of Cities (NLC) and National Association of Counties (NACo), the Administration is connecting with the thousands of state, local, and county offices on the frontlines in large and small communities across the country that are hardest hit by the foreclosure crisis. These offices now have the tools to increase awareness of the program, connect with and educate borrowers and grassroots organizations on how to request a modification and take the additional steps to ensure they are converted to permanent status; and serve as an additional trusted resource for borrowers who are facing challenges with the program.

- In partnering with the Conference of State Bank Supervisors (CSBS) and the American Association of Residential Mortgage Regulators (AARMR), state regulators now have enhanced tools to assist borrowers who are facing challenges in converting to permanent modifications. Regulators are now able to work directly with our escalation and compliance teams to ensure that HAMP guidelines are consistently applied.

## **Operations and Compliance**

### *Compliance*

Freddie Mac, Treasury's compliance agent for HAMP, has a robust compliance program in place for HAMP. Freddie Mac began reviewing servicers in July. Recognizing that many of the servicers' processes are newly developed and most modifications are still in trial periods, these reviews have focused on the servicers' implementation activities, looking to identify process improvements. As loans move into permanent modification status and as servicers' processes mature, Freddie Mac's reviews will focus more on risk-based activities and compliance trend issues.

Freddie Mac also began a "second look" review process, where Freddie Mac is reviewing a sample of delinquent loans to ensure that borrowers have been solicited and properly evaluated for HAMP. This "second look" process began in August, and is designed to minimize the likelihood that borrower applications are overlooked or that applicants are inadvertently denied a modification.

Treasury has a compliance committee for HAMP to review and understand servicers' compliance results and determine appropriate remedies. The compliance committee's actions range from requiring improperly denied loans to be re-assessed and the borrower solicited, to operational enhancements, additional servicer oversight or monetary actions. Monetary remedies may include withholding or reducing incentive payments to servicers, or requiring repayments of prior payments made to servicers with respect to affected loans. In addition, underperforming or non-performing servicers may become subject to additional, stricter compliance reviews and monitoring.

### *Escalation Enhancements*

Treasury has made a number of improvements to its escalation process. We have worked with Fannie Mae to set up an escalation call center so that borrowers may seek immediate assistance in completing a modification request, or to report suspected misapplication of HAMP program rules by a servicer. The staff at this center have had training specific to the HAMP program so that they will be able to work with servicers to resolve borrower issues, and to report non-compliance through the appropriate channels. The staff are to review file documentation, review decisions, and connect with servicers to reevaluate HAMP applications. In addition, the escalation team is able to refer cases to our compliance team and/or Treasury to report program violations. Fannie Mae has created a hotline for counselors and government officials who are working on behalf of borrowers and have specific HAMP concerns. Treasury also collects data from the call center to monitor case response times, common problems, and help Treasury monitor the program's effectiveness.

### *Servicer Metrics & Data*

On August 4, we began publicly reporting servicer-specific results on a monthly basis. These reports provide a transparent and public accounting of individual servicer performance by detailing the number of trial modification offers extended and the number of trial modifications underway. As more detailed data is collected from servicers and validated through Treasury's data processing systems, Treasury will release reports with greater detail on servicer performance. The October report contained trial modification data by state. The November report, set to be released on December 10<sup>th</sup>, will contain permanent modifications by servicer. Beginning in January, the reports will include operational metrics to measure the performance of each servicer in categories such as borrower wait time in response to inquiries and response times for completed applications.

## **Home Affordable Modification Program Design and Goals**

### *HAMP Guiding Principles*

HAMP is built around three core concepts, designed to help the large segment of at-risk homeowners where foreclosure is both avoidable and where the homeowner wants to stay in the home.

First, the program focuses on affordability, in an effort to ensure that borrowers who hope to remain in their homes will be able to afford the modified mortgage payment structure. Every modification under the program must lower the borrower's monthly mortgage payment to 31 percent of the borrower's monthly gross income. The borrowers' modified monthly payment of 31 percent debt to income (DTI) will remain in place for five years, provided the borrower remains current. We believe HAMP creates newly modified affordable loans that homeowners can both afford and understand.

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.

HAMP offers "pay for success" incentives to servicers, investors and borrowers for successful modifications. 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 for three years, provided the borrower remains current. Homeowners may earn up to \$1,000 towards principal reduction each year for five years if they remain current. 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,

requiring lenders/investors to share in the burden of achieving affordability. To encourage the modification of current loans expected to default, HAMP provides additional incentives to servicers and lenders/investors after current loans are modified.

Third, participating servicers are required to evaluate every eligible loan using a standard net present value (NPV) test. If the test is positive, the servicer must modify the loan. 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.

#### *HAMP Goals and Eligible Population*

The Administration expects that HAMP can help millions of at risk homeowners remain in their homes, and we are progressing toward our goal of providing assistance to as many as 3-4 million borrowers through the end of 2012.

Today, many borrowers are facing foreclosure or in some stage of the foreclosure process. These homeowners are struggling for a number of reasons, many of them outside the control of the borrower:

- Some were put in unsustainable loans;
- Many have seen their incomes decline;
- And some just bought too much home in the hopes of being able to refinance or sell after further appreciation.

HAMP is intended to help an important segment of these borrowers who are currently at-risk of foreclosure or who will be at risk prior to the end of 2012. The program is targeted to help homeowners who:

- Occupy their home as their primary residence,
- Have a loan balance less than \$729,750,
- Took out their mortgage prior to Jan. 1, 2009,
- Have a mortgage payment that is greater than 31% of their gross monthly income, and
- Can afford to make a reasonable payment on a modified mortgage.

Among this target population, we also expect that there will unfortunately still be some borrowers who will not respond to outreach efforts or who will not act on trial modification offers when extended, though every effort is planned to reach out to this population.

Based on a recent survey of servicers, we estimate that as of the *beginning of November* there were fewer than 1.5 million homeowners who were both 60+ days delinquent and likely to meet the HAMP requirements. This puts the approximately 650,000 borrowers who had begun trial modifications as of the beginning of November in a more complete context. As we have continually stressed, while no one wants to see foreclosures, not all delinquent borrowers will qualify for HAMP modifications.

Borrowers who are in a trial modification, or have moved to permanent are seeing significant benefits:

- Borrowers have had, on average their payments reduced by over \$550 per month, a reduction of roughly 35 percent from their prior payment.
- Over 230,000 adjustable rate mortgages, and nearly 450,000 fixed rate mortgages have been modified, on a trial basis, to sustainable levels.

For the millions of homeowners who are eligible for HAMP, the program provides a critical opportunity to stay in their homes. It is providing peace of mind to families who could not stay current on their mortgages or who only recently have fallen behind on payments. It is helping to stabilize home prices for all American homeowners and, in doing so, aiding the recovery of the U.S. economy. However, it will not reach those outside of the eligibility criteria and was not designed to help every struggling homeowner. Even with HAMP expected to help millions of homeowners remain in their homes, we unfortunately should still expect millions of foreclosures for the reasons mentioned above, as President Obama noted when he launched the program in February.

#### **Policy Developments and Challenges:**

As with any new program with the size and complexity of HAMP, the program faces a number of challenges, which the Administration is addressing aggressively.

#### *Home Affordable Foreclosure Alternatives<sup>SM</sup>*

We recognize that any modification program seeking to avoid preventable foreclosures has limits, HAMP included. HAMP does not, nor was it ever intended to address every delinquent loan. In these instances, the borrower may benefit from an alternative that helps the borrower transition to more affordable housing and avoid the substantial costs of a foreclosure. For instance, some borrowers do not have sufficient resources to support a HAMP modification at 31% of their income. For borrowers such as these, the Foreclosure Alternatives Program can help prevent costly foreclosures and minimize the damage that foreclosures impose on borrowers, financial institutions and communities. For those borrowers who meet the eligibility criteria for HAMP but do not successfully complete a Trial Period Plan, or default on a HAMP modification, on November 30 we published guidelines for the Foreclosure Alternatives Program, which provides incentives for short sales and deeds-in lieu of foreclosure where borrowers are unable or unwilling to complete the HAMP modification process. Borrowers are eligible for relocation assistance of \$1,500 and servicers will receive a \$1,000 incentive for completing a short sale or deed-in-lieu. In addition, investors will be paid up to \$1,000 for allowing short sale proceeds to be distributed to subordinate lien holders.

#### *Foreclosure proceedings*

We have heard from borrowers that more clarification is needed about the rules regarding foreclosure when borrowers apply for a trial modification and during the trial period. Borrowers have expressed particular concerns about notices regarding foreclosure actions that were begun before they were considered for HAMP. Under the contract that all participating servicers have signed, any pending foreclosure sale must be suspended and no new foreclosure proceedings may be initiated during the trial period. Foreclosure proceedings may not be initiated or restarted until the borrower has failed the trial period and the borrower has been considered and found ineligible for other available foreclosure prevention options. Servicers who violate any of these rules are considered non-compliant. Counselors and borrowers should report violations through the escalation channels. Freddie Mac receives trend information and can view all complaints recorded by Fannie Mae. This complaint information is then factored into Freddie Mac's risk analysis to determine frequency and type of compliance activities to be performed at servicers. If a pattern or significant increase in complaints occur, Freddie Mac will, and has, performed targeted reviews.

In addition, Treasury has convened an integrated working group including servicers, foreclosure attorneys and housing advocacy organizations to review and develop improvements to our existing foreclosure suspension rules, to ensure that no borrower being evaluated for HAMP is subject to foreclosure.

#### *Improving Transparency*

Every borrower is entitled to a clear explanation if they are determined to be ineligible for a HAMP modification. Treasury has established denial codes that require servicers to report the reason for modification denials in writing to Treasury. Servicers are now required to use those denial codes as a uniform basis for sending letters to borrowers who were evaluated for HAMP but denied a modification. In those letters, borrowers will be provided with a phone number to contact their servicer as well as the HOPE hotline, which has counselors who are trained to work with borrowers to help them understand reasons they may have been denied a modification and explain other modification or foreclosure prevention options that may be available to them.

Transparency of the Net Present Value (NPV) model – a key component of the eligibility test – is also important. We are increasing public access to the NPV white paper, which explains the methodology used in the NPV model. We are also working to increase transparency of the NPV model, including new tools that counselors can use to assist distressed homeowners applying for modifications. To ensure accuracy and reliability, Freddie Mac, acting as our compliance agent, conducts periodic audits of servicer's implementation of the model. If servicers' models do not meet Treasury's NPV specifications, Freddie Mac will require the servicers to no longer use their own implementation of the model and revert back the NPV application available through the MHA Servicer Portal.

#### *Unemployment*

HAMP has been designed to allow unemployed borrowers to participate in the program. Unemployed borrowers who have 9 months or more of unemployment insurance (UI) remaining are eligible to include UI in their income for consideration in the NPV calculation. Unemployed borrowers are also allowed to include other sources of passive income like rental income as well as income from an employed spouse, which will qualify some borrowers for a modification. We recognize, however, that some unemployed borrowers will have trouble qualifying for a modification because their income is insufficient to pass the NPV test.

Treasury is aware of a number of policy proposals that have been advocated to further assist unemployed borrowers, including the model provided by Pennsylvania's Homeowners' Emergency Mortgage Assistance Program (HEMAP), the Foreclosure and Unemployment Relief Plan proposed by academics at the University of Wisconsin, proposals put forward by economists from the Federal Reserve Bank of Boston, and other ideas. While our key focus is on helping as many borrowers as quickly as possible under the current program, Treasury recognizes that unemployment presents unique challenges and is still actively reviewing various ideas and suggestions in order to improve implementation and effectiveness of the program in this area.

#### **Conclusion**

In nine months, the Administration 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.

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

We look forward to continuing to work with you to help keep Americans in their homes, restore stability to the U.S. housing market and ensure a sustained economic recovery.

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