Protecting Homeowners from Foreclosure

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Despite the recent "good news" we hear regarding the economy and housing recovery (indeed the total number of foreclosure s is down significantly from the height of the crises), the recovery remains uneven, with far too many communities still trying to regain financial and housing stability.

Overall, through September of 2014, the numbers of foreclosures were down by 32.6% from the previous year[1] and foreclosure rates are the lowest they have been since 2007[2]. At the same time, foreclosure and delinquency rates remain high in a significant number of states (New Jersey and Florida lead the list). The low and moderate income and communities of color hit hardest by the foreclosure crisis have not experienced the rise in home values seen elsewhere. According to a 2014 study by the Haas Institute, *Underwater America*, more than 10 million people live in the hardest hit areas and nearly half of those communities have a median income of less than $40,000. African American and Latino households make up a disproportionate segment of the hardest hit communities.[3]

As detailed below, several programs established by federal agencies and lenders offer assistance although they have not entirely met the need.

HISTORY

Making Home Affordable (MHA). The MHA program is the Obama Administration's broad strategy to help homeowners avoid foreclosure and attempt to stabilize the country's housing market. MHA offers homeowners different options to help them lower their monthly mortgage payments and get into more stable loans. For those homeowners for whom homeownership is no longer affordable or desirable, the MHA programs attempt to provide options out of ownership that avoid foreclosure. There are also options for unemployed homeowners and homeowners who owe more than their homes are worth. Many of the MHA elements are described below. For more information go to www.makinghomeaffordable.gov

The Home Affordable Modification Program (HAMP). HAMP continues to be an important federal effort to help homeowners avoid foreclosure. HAMP provides incentives to loan servicers (the organizations to whom monthly mortgage payments are made) and investors to modify first-lien mortgages for homeowners in default or in danger of default. By providing mortgage servicers with financial incentives to modify existing first mortgages, the Department of the Treasury (Treasury) hopes to help as many as 3 million to 4 million homeowners avoid foreclosure regardless of who owns or services the mortgage. Participation in the program is voluntary, and more than 140 servicers participate in the program under agreements with the Treasury. Modifications can be made under HAMP until December 31, 2016, an extension past the original December 31, 2013, expiration date.

The HAMP modification program is available to owner-occupants in one- to four-unit properties at risk of default because of unaffordable mortgage payments. The unpaid principal balance on the mortgage loan must be equal to or less than $729,750 for one-unit properties (there is a higher limit for two- to four-unit properties) and the mortgage loan must have been made on or before January 1, 2009. The mortgage payments must be unaffordable (i.e., exceed 31% of the borrower's pre-tax income). The modification will consist of a reduction of the interest rate to a point where loan payments do not exceed 31% of the borrower's income. This interest rate, which can be as low as 2%, will be in place for the first five years of the modified mortgage, at which time the interest rate will slowly increase to the market rate at the time the mortgage was modified. If a 2% interest rate does not result in a payment that is affordable,

1 National Foreclosure Report, CoreLogic, September, 2014

2 For Some States, Foreclosure Crisis Is Far From Over, Joe Light, *Wall Street Journal*, November 14, 2014

3 http://diversity.berkeley.edu/sites/default/files/HaasInsitute_UnderwaterAmerica_PUBLISH_0.pdf

the servicer can take additional steps to make the mortgage affordable, including extending the loan term out to 40 years, deferring repayment on a portion of the amount owed until a later time, or forgiving a portion of the debt.

Borrowers request to participate in HAMP by sending their servicer an initial set of documents to establish their eligibility for the program. If eligibility is established and an economic model shows that it is worth more to the investor to modify the mortgage than foreclose, the servicer must offer the borrower a modification. If the modified mortgage is worth less than the foreclosed mortgage, the modification is optional. Slightly different rules apply in the case of loans owned or guaranteed by Freddie Mac or Fannie Mae.

HAMP has several sub- or related programs.

- The Home Price Decline Protection program provides incentives to offset potential losses in home values after a modification to encourage servicers and investors to modify mortgages in declining markets. The incentives are based on projections of future home prices.
- The Principal Reduction Alternative program provides funds to be used to reduce the principal for homes worth less than the amount remaining on the first-lien mortgage.
- Home Affordable Unemployment Program or Homeowners Loan Program is intended to offer assistance to unemployed homeowners through temporary forbearance of a portion of their mortgage payments.
- Home Affordable Foreclosure Alternatives provides incentives to servicers and borrowers to pursue short sales or deeds in lieu of foreclosure in cases where the borrower is unable or unwilling to enter into a modification. In a short sale, a servicer allows the borrower to sell the property at its current value, even if the sale nets less than the total amount owed on the mortgage. With a deed in lieu, the borrower simply voluntarily transfers ownership of the property to the servicer. While not desirable alternatives, these procedures allow the homeowner and the servicer to avoid the time and expense of a foreclosure.
- Second Liens. According to Treasury, up to 50% of at-risk mortgages have second liens, and many properties in foreclosure have more than one lien. Under the Second Lien Modification Program, when a HAMP modification is initiated on a first lien, servicers participating in the Second Lien Program must modify or extinguish the associated second lien. Modifications to the second lien are made based on the nature of the second lien according to a set of specific rules, or the servicer can extinguish the second lien in return for a lump sum payment from Treasury.
- The Housing Finance Agency Innovation Fund for the Hardest-Hit Housing Markets (Hardest-Hit Fund or HHF) is designed to support innovative programs created by state housing finance agencies (HFAs) to stabilize housing markets and help families avoid foreclosure. HHF provides targeted aid to families in the states most impacted by the housing downturn. These HFA programs include assistance to unemployed homeowners, principal reduction, funding to extinguish second liens, and facilitation of short sales and deeds-in-lieu. HHF is available in Alabama, Arizona, California, Florida, Georgia, Illinois, Indiana, Kentucky, Michigan, Mississippi, Nevada, New Jersey, North Carolina, Ohio, Oregon, Rhode Island, South Carolina, and Tennessee.
- HAMP Tier 2. Treasury further expanded the HAMP program in 2012. These expansions, known as HAMP Tier 2, expand HAMP eligibility. Borrowers must still have a mortgage on a single family property. The mortgage must have been originated prior to January 2, 2009. Borrowers must also have a documented difficulty in making the payments, and the borrower's unpaid principal balance must fall below thresholds established in the program. Notably, HAMP Tier 2 allows for some rental properties to be eligible for modifications.

Through August 2014, the HAMP program had completed 1.4 million permanent modifications. Servicers have provided an additional 4.2 million proprietary modifications outside of the HAMP program. An important issue to note related to the HAMP programs is that borrowers who received interest rate reduction modifications early on are seeing rate increases beginning in 2014. The program called for these increases after five years in their modification, and 83% of HAMP Tier 1 homeowners will experience an increase. The first interest rate increases went into effect in the third quarter of 2014 for the earliest group of borrowers who received loan modifications under the program. Additional borrowers will see increases in 2015 and 2016. Additionally, many of these borrowers will face two or three annual increases. The median amount of the first monthly payment increase is $95, and the median monthly payment increase after the final interest rate increase is $211. For additional information, visit the 2014 HAMP program report issued by Treasury Department

Home Affordable Refinance Program. Through the Home Affordable Refinance Program (HARP), Fannie Mae and Freddie Mac allow the refinancing of mortgage loans they own or that they placed in mortgage-backed securities. This refinancing allows borrowers to move to a less expensive fixed-rate mortgage even if their mortgage is greater than the current value of their homes, a situation known as being "underwater." Currently, these underwater mortgages cannot be easily refinanced, leaving few options for borrowers facing unaffordable increases on their adjustable rate mortgages. To be eligible, the mortgage must be on an owner-occupied one- to four-unit home and the borrower must be current on his or her mortgage payments and be able to afford the new mortgage. Initially, homeowners were eligible if, among other criteria, they owed up to 105% of the value of their homes. The program was expanded by the administration in 2009 to include homeowners who owe up to 125% of the value of their homes. This cap was removed entirely by the Federal Housing Finance Agency (FHFA) altogether in 2011. The HARP program's expiration date has been extended to December 31, 2015, from the initial expiration date of December 31, 2013. To determine if a mortgage loan is owned by Freddie Mac or Fannie Mae, the borrower can call his or her mortgage lender or servicer and ask about the program. Contact information can be found on monthly statements or in mortgage coupon books. In addition, Fannie Mae and Freddie Mac have established toll-free telephone numbers and websites to help borrowers.

The Hardest Hit Fund. The Hardest Hit Fund was created in 2010, when the Obama Administration announced the commitment of $1.5 billion to be made available to the housing finance agencies in the five states that had experienced the greatest drops in home prices: Arizona, California, Florida, Michigan, and Nevada. A second round of funding, $600 million, was made available later in 2010 for states with high levels of economic distress and unemployment: North Carolina, Ohio, Oregon, Rhode Island, and South Carolina. A third round of funding made $2 billion available for states with unemployment rates higher than the national average. States must spend their funds under the program by December 31, 2017. Additional rounds of funding are not expected.

Legal settlements. There have been a number of legal settlements between law enforcement (federal agencies or state attorneys general) and banks that have expanded opportunities for principal reduction. The first settlement was between state attorneys general and the federal government and five large national banks (Wells Fargo, Bank of America, Citibank, Chase, and Ally) to address robo-signing and other problems in mortgage servicing and foreclosure processes. The settlement mandated the banks modify loans, some with reduction in principal, although the settlement did not extend to mortgages bought by Fannie Mae and Freddie Mac. Total principal reduction credited under the settlement was $10.7 billion out of a total of $20.7 in consumer relief.

There have been a series of subsequent settlements between the U.S. Department of Justice and individual banks for their practices in producing and marketing mortgage-backed securities. Each of these settlements included combinations of fines and consumer relief. The most recent and largest was a $16.6 billion settlement with Bank of America in August 2014, which included $7 billion in consumer relief, including principal reduction targeted at communities hardest hit by foreclosures.

The National Foreclosure Mitigation Counseling Program. The National Foreclosure Mitigation Counseling (NFMC) program was launched in December 2007 with funds appropriated by Congress to address the nationwide foreclosure crisis by dramatically increasing the availability of housing counseling for families at risk of foreclosure. NeighborWorks America distributes funds to competitively selected grantee organizations, which in turn provide the counseling services, either directly or through sub-grantees. Grants also fund legal assistance for homeowners and the training of foreclosure counselors. More than 1,700 counseling agencies participate in the program. As of August 2014, more than 1.8 million individuals have been provided counseling under

NFMC. Foreclosure counseling organizations can be found at www.findaforeclosurecounselor.org

The Urban Institute recently completed a four-year evaluation of rounds three through five of the NFMC program. Analyzing more than 100,000 loans, the Urban Institute was able to employ robust statistical techniques to isolate the impact of NFMC counseling on loan performance through June 2013. The results of the study demonstrated that counseled homeowners were nearly twice as likely to cure a serious delinquency or foreclosure with a modification or other cure, 1.5 times more likely to stay current after obtaining a cure, and for NFMC clients who cured a serious delinquency, avoid foreclosure altogether. See: *Urban Institute NFMC Evaluation 2014*. Overall, the Urban Institute evaluation demonstrates that the NFMC program had its intended effect of helping homeowners facing loss of their homes through foreclosure. The positive effects demonstrated in the final report are consistent with those found in prior analyses of rounds one and two.

The FY2015 NFMC program was funded by Congress at $50 million, which includes $4 million for the wind-down and close out of the program.

HOPE NOW. An alliance composed of counselors, mortgage companies, investors, and other mortgage market participants, HOPE NOW members work together to reach out to homeowners in distress to help them stay in their homes and to create a unified, coordinated plan to help as many homeowners as possible. The alliance supports the HOPE for Homeowners Hotline, 1-888-995-HOPE, where borrowers can receive pre-foreclosure counseling.

FORECAST FOR 2015

- **Requiring Fannie Mae and Freddie Mac to do principal reduction.** Perhaps the biggest unknown for 2015 is whether the FHFA, the agency that oversees mortgage financing giants Fannie Mae and Freddie Mac, will allow or require these entities to offer principal reduction modifications for underwater borrowers. The issue has been a point of great controversy as a broad range of servicers has employed principal reduction on non-government sponsored enterprise loans. With the confirmation of Mel Watt as FHFA director, there is a new opportunity to revisit the decision of his predecessor and allow for principal reduction.

  There is convincing evidence that principal reduction is the most effective form of modification in limiting future re-defaults. A 2012 study by Amherst Securities Group found that principal reduction is the most effective form of mortgage modification, with only 12% of borrowers re-defaulting on such modifications, compared with 23% for interest rate reduction modifications and 30% for forbearance modifications.[4] Similarly, the Congressional Budget Office found that a targeted principal reduction program would result in savings to the government, reduce mortgage foreclosure and delinquency rates and modestly boost economic growth.[5]

  Advocates are urging FHFA to allow and/or require principal reduction modifications. It is one of the more important outstanding questions in assisting large numbers of struggling underwater homeowners.

- **Monitoring, enforcement and refining of CFPB servicing standards**. New Consumer Financial Protection Bureau (CFPB) servicing rules took effect in January 2014. These rules set industry-wide requirements and standards for all facets of foreclosure prevention and loss mitigation and timely crediting of payments. In November 2014, CFPB issued reforms to these rules for public comment, including new borrower protections when mortgage servicing is transferred from one servicer to another, requirements for servicers to notify borrowers when they have provided all the materials necessary for a complete loan modification application, and to clarify that widows and orphans who inherit a home but are not on the mortgage are eligible for loss mitigation protections, among other protections. The CFPB has printed a summary of the servicing rules.

  In 2015, the CFPB will implement these changes and continue to monitor and enforce servicing rules. CFPB took one high profile action in September 2014 against Flagstar Bank for failing to meet foreclosure prevention

4 Amherst Securities Group LP, Modification Effectiveness: The Private Label Experience and Their Public Policy Implications, May 30, 2012, p.6

5 https://www.cbo.gov/publication/44115

requirements. Flagstar was required to pay $20 million in compensation to harmed borrowers and a $7.5 million fine.

- **Improving settlements.** There are a number of potential improvements that should be made to provide more relief to borrowers. One idea is give some decision-making authority over who receives principal reductions pursuant to a settlement to local housing advocates and/or community groups. Additionally, unclaimed funds that were available to borrowers through the Office of the Comptroller of the Currency and Federal Reserve's Independent Foreclosure Review should be used to fund housing counseling and legal services programs that can help homeowners, rather than sending the money to the states to be held as unclaimed property. The latter strategy has allowed states to absorb the money into the general fund.
- **Federal funding for foreclosure avoidance programs**. There is a push for funding for the National Foreclosure Mitigation Counseling (NFMC) Program to be maintained at $50 million and that funding for the HUD Housing Counseling Assistance program to be increased to $65 million. Appropriators have been steadily winding down NFMC funding and seem likely to continue to do so in FY16. The crisis is not over and, as noted above, the recovery has not been felt in low- and moderate-income communities, communities of color, and in many hardest-hit areas and funding for NFMC remains critical to provide counseling assistance to borrowers at risk of foreclosure.
- **HAMP marketing and outreach campaign.** Consumer groups have been working with Treasury on an outreach and marketing campaign to reach more eligible borrowers with loss mitigation programs, including homeowners in mid-tier cities. An increased focus is needed in mid-tier cities, among limited English proficiency households, homeowners who have previously tried to engage in the foreclosure mitigation process and who are now discouraged, and homeowners who face rate resets in 2015.

WHAT TO SAY TO LEGISLATORS:

Legislators and agency officials, such as those at FHFA, must hear about the ongoing problems in communities on the one hand and the real causes of those ongoing issues on the other. Legislators, in particular, are hearing that the market is recovering and that any remaining problems are being caused by the new "burdensome" rules to protect borrowers. There are several efforts to undermine the new protections and block any new measures to aid struggling borrowers.

Key messages include that the foreclosure crisis persists in the hardest hit areas and that modifying loans with principal write-downs remain the most effective way to keep people in their homes. The new mortgage rules, including the servicing standards, have created clear rules of the road for lenders while reassuring borrowers that they will be treated more fairly. Legislators must not reverse the protections that were just put in place to protect borrowers at risk of foreclosure. ■

FOR MORE INFORMATION:

HOPE for Homeowners Hotline: 1-888-995-HOPE to connect borrowers to foreclosure counselors

CFPB's Find a Housing Counselor Tool: http://www.consumerfinance.gov/find-a-housing-counselor/

Find a Nonprofit Foreclosure Counselor Tool: www.findaforeclosurecounselor.org

Information about the National Foreclosure Mitigation Counseling Program: http://www.neighborworks.org/Homes-Finances/Foreclosure/Foreclosure-Counseling-(NFMC)

Making Home Affordable initiatives: www.makinghomeaffordable.gov

HUD information on foreclosure avoidance: http://1.usa.gov/VBqaKL

Find a lawyer to assist with legal assistance: http://www.consumeradvocates.org/find-attorney