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Deputy Comptroller For Large Bank Supervision, COP Evers testimony Before the Congressional Oversight Panel

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TESTIMONY OF

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OFFICE OF THE COMPTROLLER OF THE CURRENCY

BEFORE THE

CONGRESSIONAL OVERSIGHT PANEL

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Statement Required by 12 U.S.C. § 250:

The views expressed herein are those of the Office of the Comptroller of the Currency and do not necessarily represent the views of the President.

Introduction

Chairman Kaufman and members of the Congressional Oversight Panel (Panel), my name is Joe Evers and I am a Deputy Comptroller and national bank examiner in the Large Bank Supervision division at the Office of the Comptroller of the Currency (OCC). In this role I oversee the collection, analysis, and reporting of data the OCC collects from national banks relating to the performance of first-lien residential mortgages. I appreciate the opportunity to share with the Panel insights that this data provides on mortgage modification activities.

The OCC instituted loan-level mortgage data collection from the banks it supervises in 2008 and published this information in quarterly Mortgage Metrics Reports. Later that year, we expanded our reporting and joined with the Office of Thrift Supervision (OTS) to publish data on the performance of loans and loan modifications, and to highlight trends in loss mitigation activities, foreclosures, and re-defaults occurring on mortgages held by national banks and federally regulated thrifts. Our efforts to report on this very large portfolio of mortgage loans, using validated, loan-level data based on standardized definitions and data elements, has allowed us to develop what we believe to be one of the most accurate and comprehensive data sets available on first-lien mortgages in the country.

The Mortgage Metrics Reports are dynamic documents that continue to evolve to address areas of supervisory interest, better inform policy makers, and contribute to the public discussion. The scope of our data requests from servicers is large, and the effort to validate the data is extensive. The data included in the Mortgage Metrics Reports today represent 65 percent of all first-lien residential mortgages outstanding in the country. In our most recent report, which reflects data at the end of June 2010, the reporting institutions serviced almost 34 million first-lien mortgage loans, totaling nearly $6 trillion in outstanding balances. More than 90 percent of the mortgages in the portfolio are serviced for third parties because of loan sales and securitization.

In order to best address the areas of interest described in the Panel's letter of invitation, my testimony will first provide general background about our Mortgage Metrics Reports. My statement will then discuss the evolution of mortgage modification efforts and address trends the OCC has observed pertaining to loan modifications and delinquencies on loan modifications including:

- Home retention actions (number of payment plans and loan modifications);
- Types of modification actions;
- Changes to monthly payments resulting from modifications; and
- Post modification performance (re-defaults).

Background of the OCC and OTS Mortgage Metrics Reports

In late 2007, the OCC recognized the supervisory need for more comprehensive data on the performance of mortgages and loss mitigation activities of the largest national bank servicers regulated by the OCC. We realized that the mortgage data being reported to the banking agencies were not giving us a sufficiently granular look at mortgage performance and loss mitigation activities. At the same time, the lack of standardized loan modification data and reporting within the industry made it difficult to obtain accurate, reliable and timely information on loan modifications including post loan modification performance. Given this combination of a lack of information and inconsistent standards for reporting the information that was available, the OCC undertook a comprehensive initiative to improve the way that mortgage performance could be measured, thus producing better information for our particular supervisory purposes, and better information for policymakers. To accomplish this, the OCC made a formal information request to the Chief Executive Officers of the largest national banks to submit monthly loan-level mortgage data to the OCC. The results of this first data call were published in June 2008, as the *OCC Mortgage Metrics Report, October 2007-March 2008*.[1] Before even completing this first report, the OCC began to work with the OTS[2] to issue a joint report in September 2008.[3]

Evolution of Mortgage Modification Efforts

Early in the mortgage crisis, servicers' informal payment plans and loan modifications were done in low volume and often resulted in mortgage payments that increased or did not change. This traditional approach to loss mitigation, which was previously successful in normal economic times, gave delinquent borrowers experiencing temporary financial problems a chance to catch-up on making their loan payments. However, as the mortgage crisis unfolded and the number of delinquent borrowers increased to unprecedented levels, servicers increasingly shifted from traditional loss mitigation activities to loan modification programs designed to achieve affordable and sustainable loan payments. This shift was aided by implementation of the Home Affordable Modification Program (HAMP) and OCC's mortgage metrics data that put a bright spotlight on high re-default rates for loan modifications completed in 2008. As a result of those high re-default rates, the OCC in March 2009 directed the largest national banks to implement programs designed to achieve more sustainable modifications.

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[1] See *OCC Mortgage Metrics Report*, *October 2007-March 2008*, released on June 11, 2008.
[2] The OTS separately issued its first report on mortgage metrics on July 3, 2008.
[3] See OCC and OTS News Release, "Agencies Release Joint Mortgage Metrics Report For the Second Quarter of 2008," September 12, 2008.

September 2010 Mortgage Metrics Report[4]

On September 24, 2010, the OCC and OTS released the most recent Mortgage Metrics Report on data through the second quarter 2010 which provides current information and trends in loan modification activity and performance.

Home Retention Actions

The report shows that during the second quarter 2010, servicers implemented 504,292 home retention actions, which include loan modifications, trial performance plans, and payment plans. During the quarter, servicers implemented 273,419 permanent loan modifications, including modifications made through HAMP and other modification programs, which is an increase of 18.1 percent from the first quarter of 2010. While the number of permanent modifications increased, the number of trial modifications and other payment plans declined as servicers worked through their portfolio of seriously delinquent mortgages to determine borrower eligibility under HAMP and each servicer's own proprietary loan modification programs.

***Table 1.* Number of New Home Retention Actions**

	6/30/09	9/30/09	12/31/09	3/31/10	6/30/10	1Q %Change	1Y % Change
Other Modifications	142,362	130,464	103,617	131,207	164,473	25.4%	15.5%
HAMP Modifications	--	783	20,679	100,269	108,946	8.7%	--
Other Trial Period Plans	64,201	127,902	96,048	101,764	73,673	-27.6%	14.8%
HAMP Trial Period Plans	79,994	272,709	259,015	188,503	64,666	-65.7%	-19.2%
Payment Plans	131,974	163,551	121,722	120,587	92,534	-23.3%	-29.9%
Total	418,531	695,409	601,081	642,330	504,292	-21.5%	20.5%

[4] The *OCC and OTS Mortgage Metrics Report, Second Quarter 2010* can be accessed at http://www.occ.gov/news-issuances/news-releases/2010/nr-ia-2010-112.html

Types of Modification Actions

Servicers generally use a combination of actions when modifying mortgages. The types of modification actions have different effects on borrowers' mortgage structures and payments. Over time, these differences may have varied effects on the long-term sustainability of mortgages. Consistent with the sequence of loss mitigation actions established by HAMP and generally followed for other modifications as well, servicers added past due interest and fees to the outstanding loan balance in 94 percent of all modifications during the second quarter, and reduced interest rates in 87 percent of modifications. As detailed in Table 2 below, term extensions were used in 51 percent of all modifications, principal deferrals were used in 11 percent, and principal reductions were used in two percent of the modifications.

In determining the appropriate mix of modification actions to take, mortgage servicers strive to balance the need of borrowers for affordable and sustainable payments with the rights and interests of investors. To balance these objectives, servicers are increasingly relying on modifications that emphasize payment affordability and sustainability through lower monthly payments, verification of income, and underwriting based on an affordable housing debt to income ratio. In such programs, payment affordability and sustainability is primarily achieved through some combination of rate reduction and term extension. The decline in the percentage of modifications involving principal reduction over the past year reflects servicers' emphasis on achieving affordable and sustainable payments for homeowners by a combination of reduced interest rates and other actions. The resulting outcome has been a substantial increase in modifications that provide borrowers with significantly lower monthly mortgage payments.

Table 2. Changes in Loan Terms for Modifications Made Through the Second Quarter of 2010							
(Percentage of Total Modifications)							
	6/30/09	9/30/09	12/31/09	3/31/10	6/30/10	1Q %Change	1Y %Change
Capitalization	65.8%	68.2%	82.8%	91.4%	94.1%	2.9%	42.9%
Rate Reduction	72.2%	81.1%	84.5%	82.6%	87.0%	5.2%	20.4%
Rate Freeze	8.0%	2.7%	1.9%	1.3%	4.2%	237.2%	-47.0%
Term Extension	45.8%	47.4%	45.3%	45.8%	51.4%	12.3%	12.2%
Principal Reduction	10.0%	13.0%	6.8%	1.9%	2.1%	11.2%	-78.5%
Principal Deferral	2.5%	3.1%	5.8%	10.2%	11.0%	8.1%	347.2%
Unknown*	5.8%	1.9%	1.2%	1.0%	0.5%	-53.0%	-91.6%
Total Number of Changes in Each Category							
Capitalization	93,677	89,553	102,885	211,630	257,183	21.5%	174.5%
Rate Reduction	102,811	106,443	105,060	191,281	237,801	24.3%	131.3%
Rate Freeze	11,341	3,512	2,407	2,901	11,554	298.3%	1.9%
Term Extension	65,218	62,156	56,321	105,957	140,568	32.7%	115.5%
Principal Reduction	14,194	17,090	8,435	4,464	5,865	31.4%	-58.7%
Principal Deferral	3,496	4,040	7,205	23,518	30,027	27.7%	758.9%
Unknown*	8,326	2,447	1,516	2,413	1,339	-44.5%	-83.9%

*Processing constraints at some servicers prevented them from aggregating and reporting specific modified term(s).

Changes to Monthly Payments Resulting from Modifications

In addition to providing data on the types of loan modifications, the Mortgage Metrics Reports include information on the changes to monthly principal and interest payments resulting from the modifications.

Mortgage modifications that lowered monthly principal and interest payments increased to over 90 percent of all modifications during the second quarter 2010. Modifications that reduced payments by more than 20 percent continued to increase, to 56 percent, up from 55 percent the previous quarter. This increase in modifications that reduce the borrowers' monthly mortgage payments continued over the last several quarters as servicers focused on more sustainable modifications.

Table 3. **Changes in Monthly Principal and Interest Payments Resulting from Modifications**							
(Percentage of Modifications)*							
	6/30/09	9/30/09	12/31/09	3/31/10	6/30/10	1Q %Change	1Y %Change
Decreased by 20% or More	38.8%	37.0%	41.8%	54.9%	56.4%	2.9%	45.5%
Decreased by 10% to Less than 20%	19.6%	18.3%	19.1%	17.7%	17.6%	-0.4%	-10.2%
Decreased Less than 10%	19.9%	24.4%	21.1%	14.9%	16.1%	8.1%	-19.3%
Subtotal for Decreased	**78.3%**	**79.7%**	**82.0%**	**87.4%**	**90.1%**	**3.1%**	**15.1%**
Unchanged	4.3%	3.6%	4.8%	2.7%	1.9%	-30.8%	-55.8%
Increased	17.4%	16.8%	13.2%	9.9%	8.0%	-18.9%	-54.0%
Subtotal for Unchanged and Increased	**21.7%**	**20.3%**	**18.0%**	**12.6%**	**9.9%**	**-21.4%**	**-54.4%**
Total	100.0%	100.0%	100.0%	100.0%	100.0%		
(Number of Modifications)							
Decreased by 20% or More	54,860	48,151	51,036	126,379	153,730	21.6%	180.2%
Decreased by 10% to Less than 20%	27,691	23,786	23,338	40,663	47,875	17.7%	72.9%
Decreased Less than 10%	28,213	31,707	25,748	34,271	43,827	27.9%	55.3%
Subtotal for Decreased	110,764	**103,644**	100,122	201,313	245,432	21.9%	121.6%
Unchanged	6,038	4,630	5,822	6,273	5,136	-18.1%	-14.9%
Increased	24,665	21,829	16,142	22,750	21,831	-4.0%	-11.5%
Subtotal for Unchanged and Increased	30,703	**26,459**	21,964	29,023	26,967	-7.1%	-12.2%
Total	141,467	130,103	122,086	230,336	272,399	18.3%	92.6%

*Payment change information was not reported on 895 modifications in the second quarter of 2009; 1,144 in the third quarter of 2009; 2,210 in the fourth quarter of 2009; 1,140 in the first quarter of 2010 and 1,020 in the second quarter of 2010.

Modifications made during the second quarter of 2010 reduced monthly payments by an average of $427. HAMP modifications made during the quarter reduced payments by an average of $608, compared with other modifications that reduced average monthly payments by $307 overall. The emphasis on payment affordability and sustainability has resulted in a 62 percent reduction in the average monthly payment from a year ago.

Status of Mortgages Modified in 2008-2010

Since the beginning of 2008, servicers have modified 1,239,896 loans. At the end of the second quarter of 2010, 46 percent of these modifications remained current or were paid off and another 10 percent were 30 to 59 days delinquent. More than 26 percent of the modifications were seriously delinquent, nine percent were in the process of foreclosure, and four percent had completed the foreclosure process.

***Table 4.* Status of Mortgages Modified in 2008-2010**								
	Total	Current	30–59 Days Delinquent	Seriously Delinquent	Foreclosures in Process	Completed Foreclosures	Paid Off	No Longer in the Portfolio*
2008	421,322	26.8%	7.8%	32.2%	13.6%	8.8%	2.3%	8.4%
2009	587,098	46.8%	10.6%	28.2%	8.9%	2.1%	0.7%	2.7%
First Quarter 2010	231,476	73.7%	12.7%	11.6%	1.4%	0.1%	0.1%	0.5%
Total	1,239,896	45.0%	10.0%	26.5%	9.1%	4.0%	1.1%	4.2%
Modifications that Reduced Payments by 10 Percent or More								
	Total	Current	30-59 Days Delinquent	Seriously Delinquent	Foreclosures in Process	Completed Foreclosures	Paid Off	No Longer in the Portfolio
Modifications that Reduced Payments by 10% or More	596,796	57.8%	10.3%	19.2%	6.3%	2.0%	0.6%	3.8%
Modifications that Reduced Payments by Less than 10 Percent								
	Total	Current	30–59 Days Delinquent	Seriously Delinquent	Foreclosures in Process	Completed Foreclosures	Paid Off	No Longer in the Portfolio
Modifications that Reduced Payments by Less than 10%	643,100	33.3%	9.8%	33.2%	11.6%	5.9%	1.6%	4.6%

*Processing constraints at some servicers prevented them from reporting the reason for removal from the portfolio.

<u>OCC Re-default Reporting Methodology</u>

A re-default occurs when a modified loan becomes delinquent on contractually required payments subsequent to the modification. Re-default is a useful metric to gauge payment sustainability of loan modifications, identify unsafe and unsound loan mitigation practice such as loss deferral, and determine loan loss reserves.

Our reports show re-defaults in a variety of ways to more comprehensively reflect the severity of the delinquency and the amount of time that has elapsed after the modification. Among the measures we report are the number and percentage of modified loans that are 30, 60, or 90 days delinquent or in process of foreclosure at several time periods after the modification, including three, six, nine, and twelve months post-modification. These measures enable us to assess the sustainability of a modification over time. We also report on the comparative performance of modifications implemented during specific calendar quarters to gauge the effectiveness of changes in modification actions or criteria.

The re-default rate refers to the percentage of modified loans that subsequently re-default relative to the total number of modified loans. Our Mortgage Metrics Reports show re-default rates based on the number of modified loans that remain in effect at the measurement date (e.g., the number of modified loans that are 60 or more days delinquent or in the process of foreclosure at six months after the modification as a percentage of all modified loans still in effect six months after the modification).[5]

Performance of Modified Loans

More recent modifications have performed better than earlier modifications every quarter since the end of the first quarter of 2009. At six months after modification, nearly 21 percent of the modifications made in the fourth quarter of 2009 were seriously delinquent, compared with 43 percent of the modifications made during the first quarter of 2009. This trend of lower delinquency rates following modification corresponds with the increasing emphasis on repayment sustainability through reduction of the borrower's monthly payment.

[5] All modified loans that have been repaid in full, refinanced, sold, or have completed the foreclosure process after the modification are removed from the calculation. Re-default rates reported by other sources may be based on the total, unadjusted number of modified loans.

Table 5. Modified Loans 60 or More Days Delinquent				
Modification Date	3 Months after Modification	6 Months after Modification	9 Months after Modification	12 Months after Modification*
First Quarter 2009	30.8%	42.8%	51.5%	55.0%
Second Quarter 2009	18.7%	33.5%	40.9%	43.2%
Third Quarter 2009	14.7%	27.7%	32.7%	--
Fourth Quarter 2009	11.4%	20.7%	--	--
First Quarter 2010	11.1%	--	--	--

*All re-default data are based on modified loans that remain in effect at the specified amount of time after the modification. All loans that have been repaid in full, refinanced, sold, or completed the foreclosure process are removed from the calculation. Data include only modifications that have had time to age the indicated number of months.

Re-Default Rates by Change in Payment

Modifications that reduced payments by 10 percent or more performed better than modifications that reduced payments by less than 10 percent, increased, or left the payment unchanged. At the end of the second quarter, 58 percent of modifications that reduced payments by 10 percent or more were current and performing, compared with the 33 percent of modifications that reduced payments by less than 10 percent.

Our data also show that modifications that result in lower monthly payments consistently perform better over time than those that increase payments or leave payments unchanged, with better performance directly correlating to the amount of payment reduction.

The following tables present re-default rates, measured as 60 or more days delinquent, for modifications made since January 1, 2008. Data show re-default rates decreased as reduction in monthly principal and interest payments increased, and the re-default rates were lower among modifications made in 2009 and 2010, compared with 2008 modifications.

The better performance of more recent modifications corresponds with the on-going emphasis on lowering monthly payments and improving payment sustainability.

HAMP, as well as an increasing number of other modification programs, also attempt to increase sustainability by not only reducing payments, but also targeting monthly payments relative to the borrowers' income and ability to repay the loan.

***Table 6.* Re-Default Rates of Loans Modified in 2008 by Change in Payment** (60 or More Days Delinquent)*				
	3 Months after Modification	6 Months after Modification	9 Months after Modification	12 Months after Modification
Decreased by 20% or More	15.8%	26.0%	33.3%	39.4%
Decreased by 10% to Less than 20%	20.7%	33.0%	41.4%	48.1%
Decreased by Less than 10%	23.9%	40.0%	49.4%	55.1%
Unchanged	48.3%	57.9%	63.7%	67.0%
Increased	35.2%	54.3%	63.3%	68.5%
Total	31.6%	45.2%	53.0%	58.1%

***Table 7.* Re-Default Rates of Loans Modified in 2009 by Change in Payment** (60 or More Days Delinquent)*				
	3 Months after Modification	6 Months after Modification	9 Months after Modification	12 Months after Modification
Decreased by 20% or More	11.1%	19.6%	28.4%	34.7%
Decreased by 10% to Less than 20%	16.1%	29.8%	40.2%	46.0%
Decreased by Less than 10%	17.8%	34.2%	44.6%	51.7%
Unchanged	46.7%	51.5%	60.2%	63.9%
Increased	26.7%	46.7%	57.9%	65.4%
Total	19.9%	32.3%	42.7%	49.7%

Table 8 **Re-Default Rates of Loans Modified in 2010 by Change in Payment** (60 or More Days Delinquent)*				
	3 Months after Modification	6 Months after Modification	9 Months after Modification	12 Months after Modification
Decreased by 20% or More	8.2%	--	--	--
Decreased by 10% to Less than 20%	10.2%	--	--	--
Decreased by Less than 10%	13.5%	--	--	--
Unchanged	31.2%	--	--	--
Increased	20.0%	--	--	--
Total	11.1%	--	--	--

*Data include all modifications implemented during 2010 that have aged the indicated number of months. Data do not include modifications for which payment change data was not reported.

Conclusion

Since the mortgage crisis began, mortgage servicers have been confronted with an unprecedented number of borrowers facing difficulties in meeting their mortgage obligations. This has required servicers to make substantial investments in their operations and fundamental changes in the types of modifications being offered. While much has been done, much more still needs to be accomplished. The OCC and OTS Mortgage Metrics Reports have helped to fill a critical void in monitoring and measuring loan modification activities and post modification loan performance.

Our data show that servicers are adjusting their programs to use a combination of factors to provide meaningful reductions in borrowers' monthly mortgage payments, resulting in more sustainable modifications. The result of these efforts is demonstrated in the improved longer-term performance that we are seeing in more recent mortgage modifications that have emphasized lower and more sustainable monthly payments for borrowers.