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Written Testimony

Stabilizing the Housing Market

Chairman Dodd, Ranking Member Shelby 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 for our economic recovery. It is a fundamental source of wealth and well-being for individual families and communities and plays a key role in our financial system. 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 address this crisis, help millions of homeowners and lay the foundation for economic recovery and financial stability.

This crisis took years in the making and as a result, millions of homeowners have mortgage payments they are unable to afford. The rapid decline in home prices of 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. Many analysts project that more than 6 million families could face foreclosure in the next three years if effective actions are not taken.

The Administration's Efforts

This Administration has moved with great speed to aggressively confront the economic challenges facing our economy and housing market by announcing and implementing an unprecedented mortgage modification program.

Within a month of taking office, on February 18th, President Obama and Secretary Geithner 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.

An initiative of this scale has never been previously attempted. Just two weeks after the President announced the program, the Administration, working with the banking regulators, HUD, and the Federal Housing Finance Agency, published detailed program guidelines for MHA's Home Affordable Modification Program℠ (HAMP℠). On April 6th, we issued detailed servicer guidance. Today, we have 27 servicers signed up to participate in MHA. Between loans covered by those servicers and the GSEs, more than 85 percent of all mortgage loans in the country are now covered by the program.

The initiative includes the following 3 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 has sunk below that of their existing mortgages.

Initially, the program was able to help homeowners whose existing mortgages were up to 105 percent of their current home value. However, we moved to expand it to help those with mortgages up to 125 percent of current home value.

(2) **TheHome Affordable Modification Program (HAMP**): HAMP will provide up to $75 billion dollars, including $50 billion of funds from the Troubled Assets Relief Program (TARP), to encourage loan modifications that will provide sustainably affordable mortgage payments for borrowers. Importantly, HAMP offers incentives to investors, lenders, servicers, and homeowners to encourage mortgage modifications.

(3) **Support to the GSEs**: 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.

In addition, we have also announced the following additional HAMP measures:

· On April 28th, 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 HOPE for Homeowners Program, which provides additional relief for borrowers with mortgage balances greater than the current value of their homes.

· On May 14 th, 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 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.

HAMP Design – Key Principles

Now, I will discuss these programs in greater detail.

Our initiatives are 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 borrowers' gross monthly 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 Program establishes detailed guidelines for the industry to use in making loan modifications with the goal of encouraging the mortgage industry to adopt a standard that better suits borrowers and lenders, both in and out of MHA.

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. Driving the industry towards standardized modifications based on HAMP should help increase the number of modifications.

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

HAMP Design – Eligibility Criteria

Next, I will discuss the eligibility criteria for the modification program, designed specifically to help responsible American homeowners with the greatest need for assistance and to provide that assistance at the least 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 incentives for the modification of loans where borrowers are current on their payments, but can demonstrate financial hardship or imminent risk of default.

HAMP Design – Modification Process

Next, I will discuss the 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 is 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.

HAMP Design – "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 27 servicers, including the five largest. Between loans covered by these servicers and loans owned or guaranteed by the GSEs, more than 80 percent of all mortgage loans in the country are now covered by the program.

· 325,000 trial modifications have been offered under the program. Tens of thousands of trial modifications are underway.

At this early date, MHA 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 MHA. I highlight some key measures below:

One, we are also 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

Two, just last week, 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 requests 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. Treasury also requested that each servicer detail the specific steps that the servicer will take towards effective implementation and compliance.

Three, we are taking additional steps to expedite implementation, including more standardization of documentation and 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 are planning to take three additional concrete steps in conjunction with the servicer liaison meeting to enhance transparency in the program:

One, by August 4 th, we will begin publicly reporting servicer-specific results on a monthly basis. These reports will 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 will work 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 are also planning to deploy a data reporting tool that will contain over 130 data elements and will be able to provide a comprehensive assessment of the program at the loan, servicer, and mortgage market levels. This will enable the program to be effectively measured against specific performance benchmarks.

Finally, we have 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 will be designed to minimize the likelihood that borrower applications are overlooked or that applicants are inadvertently denied a modification.

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 22 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 MHA program.

- Working closely with Fannie Mae, we have also launched an effort to hold foreclosure prevention workshops and borrower education events in cities facing high foreclosure rates. The first such outreach event was held in Miami in June.

Much more has to be done and we will continue to work with other agencies 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 result 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 five months, including the initial start-up phase, HAMP has accomplished a great deal and helped homeowners across the country. But we know that more is required to help American families during this crisis and will aggressively continue to build on this progress. For example, we are taking additional steps to implement programs including:

1. the Second Lien Program;
2. the Foreclosure Alternatives Program;
3. Home Price Decline Protection incentives; and
4. strengthening of HOPE for Homeowners.

Each of these supplemental programs is designed to increase the effectiveness and take-up of the basic 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.

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