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"Foreclosure Prevention: Is the Home Affordable Modification Program Preserving Homeownership?"

Chairman Towns, Ranking Member Issa and members of the Committee, thank you for the opportunity to testify today on the Administration's comprehensive initiatives to stabilize the U.S. housing market and support homeowners.

The Home Affordable Modification Program is Promoting Affordability
As the Obama Administration came into office last year, the country faced extraordinary economic and housing market conditions that required the rapid introduction of unprecedented housing policies designed to stabilize the housing market. On February 18, 2009, President Obama announced a comprehensive Homeowner Affordability and Stability Plan, which sought to address the issue of mortgage affordability for millions of struggling homeowners in America.

The Home Affordable Modification Program (HAMP) is a critical piece of this plan. When it was announced last year, the President said the program would "enable as many as 3 to 4 million homeowners to modify the terms of their mortgages" over the four-year life of the program, enabling these homeowners to modify their mortgages and helping them avoid foreclosure. Now, just a year after program guidelines were first put forward, 1.1 million homeowners have entered into a trial period plan that comes with real and immediate relief in the form of lower mortgage payments. For most of the period since June 2009, approximately 20,000 to 25,000 new homeowners began a trial plan each week. At this rate, HAMP is on track to have actual trial modifications for up to 3 to 4 million homeowners by 2012.

Since the programs began, the Administration has consistently strived to not only offer assistance to struggling homeowners but to translate this initial help into sustainable outcomes for borrowers that allow families to remain in their homes or avoid foreclosure. In many cases, the best sustainable outcome for a homeowner is in the form of a permanent HAMP modification, though some borrowers may be better suited for a modification outside our program, or a dignified transition to other housing through alternatives such as the Home Affordable Foreclosure Alternatives Program (HAFA). We believe that the most significant measures of success are not just how many borrowers start trial modifications or even permanent modifications, but whether families are able to avoid foreclosure and how effective the program is in stabilizing the housing market. The Administration has made substantial progress in implementation and has seen initial signs of housing stability, but a number of critical challenges remain.

The Administration's Response Addresses the Major Components of the Housing Crisis
The Administration has taken a broad set of aggressive actions to stabilize the housing market and help American homeowners. These efforts are having an impact on our housing markets and we are seeing signs of stabilization. Looking back to over a year ago, stress in the financial system had severely reduced the supply of mortgage credit, limiting the ability of Americans to buy homes or refinance mortgages. Millions of responsible families who make their monthly payments and fulfill their obligations saw their property values fall, and found themselves unable to refinance at lower mortgage rates.

In response to the dire state of the housing market, the Administration announced a comprehensive set of programs to strengthen the housing market and provide relief to struggling homeowners:

Actions Supporting Market Stability and Access to Affordable Mortgage Credit

- Provided strong support to Fannie Mae and Freddie Mac to ensure continued access to affordable mortgage credit across the market;
- Together, the Treasury and the Federal Reserve mortgage-backed securities (MBS) purchase programs have purchased over $1.4 trillion in agency MBS helping to keep interest rates at historic lows so homeowners can access credit to purchase new homes and refinance into more affordable monthly payments; and
- The Federal Housing Administration (FHA) has played an important counter-cyclical role, providing liquidity for housing purchases at a time when private lending declined.

Actions Helping Homeowners Purchase Homes, Refinance and Modify Mortgages to More Affordable Payments, Prevent Foreclosures and Stabilize Communities

- Launched a modification initiative to help homeowners reduce mortgage payments to affordable levels and prevent avoidable foreclosures;
- Supported extending the temporary loan limits of $729,750 for Government Sponsored Enterprise (GSE) loans and FHA loans;
- Expanded refinancing flexibilities for the GSEs, particularly for borrowers with negative equity, to allow more Americans to refinance;
- Launched a $23.5 billion Housing Finance Agencies Initiative which is helping over 90 state and local housing finance agencies across 49 states provide sustainable homeownership and rental resources for American families;
- Supported the First Time Homebuyer Tax Credit that has helped hundreds of thousands of responsible Americans purchase homes;
- The Recovery Act is providing over $5 billion in support for affordable rental housing through low income housing tax credit programs and $2 billion in support for the Neighborhood Stabilization Program to restore neighborhoods hardest hit by concentrated foreclosures; and
- On February 19, 2010, the Administration announced the $1.5 billion Hardest Hit Fund for state housing finance agencies in the nation's hardest hit housing markets to design innovative, locally targeted foreclosure prevention programs.

Historically low interest rates along with expanded refinancing flexibilities for Fannie Mae and Freddie Mac conforming and GSE loans have helped over four million American homeowners with Fannie Mae and Freddie Mac loans to refinance, saving each homeowner an estimated $150 per month on average and more than $7 billion in total. HAMP has provided over 1 million struggling homeowners a second chance to stay in their homes. Furthermore, each homeowner in a HAMP modification receives a median payment reduction of around $500 per month.

HAMP Is Helping Struggling Homeowners Today

HAMP is providing immediate relief in the lives of homeowners who are affected by the mortgage crisis. The prospect of losing one's home is extremely emotional and personal. And we recognize that HAMP, designed to keep eligible homeowners in their homes with long-term affordable mortgages, took a while to ramp up and adapt to borrower needs. As the first program of this scope and complexity, implementation could not happen overnight.

Servicers have had to ramp up capacity and make significant changes to their businesses to implement the program. The servicing industry has been profoundly transformed. Previously, servicers were essentially operations to process payments and perform loss mitigation for a small number of their borrowers. Today, the financial crisis and the HAMP program have pushed them to modify mortgages, offer customer service at an unprecedented scale, and consider other alternative approaches to keeping borrowers out of foreclosure. Throughout this process, Treasury has issued guidance and clarifications designed to streamline the modification process and to improve the borrower experience. Yesterday, Treasury released additional guidance to further improve borrowers' experience by setting standards around servicer solicitation, evaluation of borrowers in bankruptcy, and clarifying the foreclosure process around HAMP-eligible borrowers.

HAMP is a Critical Component of the Administration's Broader Stability Initiatives

Whom Does HAMP Help?

HAMP has been designed for homeowners who are at risk of foreclosure and can benefit from a reduced monthly mortgage payment. HAMP was not designed to help every borrower. Borrowers who purchase investment properties, second homes or vacation homes, for example, we never intended to be assisted under this program.

To be eligible for HAMP, borrowers must meet these criteria:

- own and occupy the home as their primary residence,
- have a loan balance less than $729,750,
- received their mortgage on or before January 1, 2009,
- have a contractual mortgage payment greater than 31 percent of their gross monthly income,
- can afford to make the payment on a modified mortgage, and
- want to remain in their homes and are willing to stay current on their payments and comply with program terms.

Participating servicers are required to evaluate for HAMP every eligible seriously delinquent loan, defined as 60 days late. Part of this evaluation includes using a standard Net Present Value

(NPV) test to determine if the modification – including any government incentive – is economical from the lender’s perspective. Every loan that tests NPV positive for a modification is required to be modified. This requirement both ensures that modifications are economically beneficial and ensures that every at-risk borrower gets a fair evaluation for a modification.

How Do Borrowers Benefit from HAMP?
HAMP supports meaningful modifications with payments to servicers, investors and homeowners. Every modification under the program must lower the borrower's monthly mortgage payment to 31 percent of the borrower's monthly gross income. The borrower’s modified monthly payment of 31 percent debt to income (DTI) will remain in place for five years, provided the borrower remains current. After the first five years, the interest rate gradually steps up to the prevailing Primary Mortgage Market Survey rate in place at the time of permanent modification, locking in a rate that is currently historically low – around 5 percent - for the life of the loan. Borrowers in permanent modifications are experiencing median payment reductions of over $500 per month, or over $30,000 over the first five years, plus up to $5,000 in homeowner incentives for on-time payment performance that reduce the principal balance.

How Does HAMP Protect Taxpayers?
HAMP protects taxpayers with an innovative pay-for-success framework. While trial modifications provide the borrower an immediate reduction in payments to a sustainable level at 31percent of income, the taxpayer doesn't pay a penny for trial modifications where the borrower doesn't complete the trial. After the trial period, the payment of servicer, investor and homeowner incentive payments are contingent on continued performance in the modification.

HAMP is Transforming the Mortgage Servicing Industry
HAMP is the first national, standardized modification program—one that has led the way in setting an industry standard for affordable and sustainable mortgage modification. HAMP has been a catalyst for change by incentivizing servicers to develop the capacity and resources necessary to execute modifications on a large scale. HAMP defines a standard for an affordable and sustainable modification across the industry, set at 31 percent of gross monthly income. Until HAMP, the industry did not have a standard process for mortgage modifications, an affordability standard, or standard timelines by which modifications would be processed. HAMP has begun to systematize across servicers the method and process for modifying loans by setting affordability standards, requiring sound underwriting guidelines, and establishing a specific modification protocol and a defined timeframe for responding to modification requests. This has brought more efficiency and transparency to modifications, though challenges clearly remain.

Understanding HAMP’s Impact on Foreclosures
There is a great deal of confusion around whether and how HAMP is helping borrowers avoid foreclosure. The first step in resolving this confusion is clearly defining foreclosure and the process of foreclosure referral.

We seek to minimize the number of eligible homeowners who lose their homes in a completed foreclosure process. Although all stages of foreclosure are unpleasant, forced sale through foreclosure is the stage of the process that dislocates the family, disrupts the community, and destabilizes the local housing market.

Importantly, this measure is rarely the focus of public discussion. Most attention is given to the number of foreclosure “starts” or to the total number of foreclosure referral notices sent to borrowers. In any given year, foreclosure starts greatly outnumber foreclosure sales. HOPE Now data indicates that between April 2009 – the beginning of HAMP – and November 2009, over 1.9 million loans started the foreclosure process but significantly fewer – 666,476 loans – completed the foreclosure sale process.

In the context of current policy, which focuses foreclosure avoidance efforts along the entire foreclosure process even if the foreclosure process has begun, foreclosure starts have become less relevant predictors of future foreclosure sales. Though foreclosure starts may remain a useful indicator of housing market and economic stress, evaluating the HAMP program against its goals of helping eligible homeowners avoid foreclosure requires that we focus on completed foreclosure sales within the eligible population. While it is early in this process, we believe that HAMP is, in fact, effectively reducing the number of foreclosure sales.

HAMP-participating servicers have reported informally that, since April 2009, the overwhelming majority of their foreclosure sales were borrowers who failed to respond to solicitations and loans that HAMP was not designed to address —properties that were vacant, investor or vacation homes, and loans that were originated very recently or were excessively large. Though information from HAMP servicers alone does not capture the entire universe of foreclosures, it does provide some useful insights into the characteristics of loans going to foreclosure sale among HAMP servicers.

As the conversion process continues, we expect that the number of borrowers who do not successfully transition to permanent modifications and who ultimately transition to other forms of assistance will grow. Even for this population, we expect that HAMP can continue to successfully assist homeowners avoid foreclosures by requiring servicers to consider borrowers with cancelled trial modifications for other foreclosure prevention options. The Home Affordable Foreclosure Alternatives program will be a critical component of this effort.

HAMP Performance in Context

At the time we launched HAMP in March 2009, President Obama said that the program would "enable as many as 3 to 4 million homeowners to modify the terms of their mortgages." Since the way we get to the 3 to 4 million homeowners by the end of 2012 has generated some confusion, let me offer the following points:

- The count applies to the modifications in both the TARP-funded first lien program and the companion GSE programs.

- The President’s statement about “enabling” modifications is the reason that we have continued to report offers of trial modifications - the offer is when a homeowner is able to get a modification, and 1.4 millions offers have been extended in the first twelve months.

- A very similar picture of progress arises from the number of actual trial modifications begun, over 1.1 million in twelve months. Actual trial modifications are the point at which homeowners begin a lower mortgage payment -- an average reduction of around $500 per month.

- In a program scheduled to last nearly four years (March 2009 until the end of 2012), either the 1.1 million or 1.4 million in the first year places the program well on schedule to the goal announced by President Obama.

- The Administration has never said that the program would implement 3 to 4 million permanent modifications, which take place only after the homeowner has been offered a trial modification, has performed for at least three months in a trial modification, and has met the full documentation requirements for the permanent modification. One important reason for having permanent modifications in the first place was a recognition that not all trial modifications would become permanent, such as when a borrower does not make the three payments needed to receive a permanent modification.

- For lending involving borrowers who were already at risk of default, we have also always understood that loan modifications have redefaults. Even for permanent modifications, a significant number will redefault, so it is clear that our goal was never to see who would make every payment for the life of the mortgage. The President's announced goal -- to enable modifications for 3 to 4 million homeowners -- clearly addresses the modification process rather than the smaller number of those who never experience subsequent difficulties. In fact, we designed our program specifically to protect the taxpayer in cases where redefault occurs -- payments to servicers, investors, and borrowers are based on actual performance over time.

- The projection was based on our best estimate, at the time, of the number of HAMP-eligible households that were likely to require assistance during the four-year program. The number of households that actually require assistance from HAMP during the remaining three years may diverge from our expectations if economic conditions or home prices evolve differently than projected.

HAMP is on track toward its goals: 1.1 million borrowers have started HAMP modifications…
Nearly 1.4 million borrowers have been extended a modification offer, with 1.1 million of these approved offers resulting in modification trials. For most of the period since June, the run rate of eligible borrowers approved for and starting modifications has been approximately 20,000 to 25,000 per week. The 1.1 million homeowners who have started modifications have had their payments reduced substantially. Even for those borrowers who do not obtain a permanent modification (for example, those who do not complete a trial modification but instead pursue a foreclosure alternative such as a short sale), they still benefit from reduced payments during the trial phase.

As of the end of February 2010, 822,000 homeowners had been in the trial phase of the modification process for more than three months and could be eligible for conversion subject to submitting all necessary documents, remaining current on payments and meeting other technical requirements. Of those homeowners, 32 percent had received permanent modifications or had been approved for permanent modification (170,000 permanent and another almost 92,000 approved for permanent). This conversion rate from trial to permanent modifications has been improving but is still below desired or anticipated program levels. The overall number of borrowers in permanent modifications has been rising substantially in recent months and should continue to do so. In February alone, 53,000 borrowers in modifications received permanent status. However, the conversion rate and overall number of conversions remain a critical focus of attention.

…. Yet conversions remain a challenge

The process of converting trial modifications to permanent has been much more challenging than officials originally anticipated. This is due to several factors, including insufficient capacity and execution at most servicers, a lack of willingness or ability to provide necessary documentation on the part of some borrowers, frequent inconsistencies between verbal and verified income that result in a borrower being deemed ineligible for the program, and a process that has proven more complex administratively than originally conceived. At the start of the program, servicers were provided flexibility to approve borrowers for trial modifications based on what fit best with their existing business practices – either starting a trial modification and then collecting documentation or collecting documentation upfront before the trial modification started. When the program launched, there were a large number of borrowers who needed immediate relief and could not wait for servicers to fully ramp up. This created a substantial backlog for servicers to process when borrowers reached the end of their trial period. To address many of these challenges, the Administration recently issued new guidance requiring servicers to begin offering trial modifications based on verified documentation at the front end of the process.

On November 30, 2009, Treasury launched a comprehensive conversion campaign focused on reaching homeowners who are eligible for permanent mortgage modifications. We required the seven largest HAMP servicers to submit conversion plans and required all HAMP servicers to submit their strategy for obtaining documentation from borrowers. We also enhanced communication tools for borrowers on our website to make conversion easier, including an instructional video, links to all of the required documents, and an income verification checklist, and a conversion guide for borrowers. As a result of these efforts, the number of borrowers entering into permanent modifications almost quadrupled from just over 30,000 at the beginning of December to over 170,000 permanent modifications and 91,000 pending permanent modifications at the end of February.

Program Improvements

Enhancing Borrower Protections

Yesterday, Treasury released guidance (Supplemental Directive 10-02) that will provide borrowers with a number of new protections in the HAMP evaluation process to help address some of the confusion and anxiety that some borrowers reported surrounding their rights during the evaluation process

The guidance addresses borrower solicitation, borrower response timelines, the foreclosure process, and bankruptcy changes. Supplemental Directive 10-02 requires and defines reasonable outreach efforts to homeowners by servicers and establishes a timeframe for borrowers to respond to these efforts. This guidance also clarifies that servicers must consider borrowers in active bankruptcy for HAMP if a request for modification is received.

Supplemental Directive 10-02 also addresses the HAMP evaluation process with respect to foreclosure. Currently, servicers may not refer a mortgage to foreclosure if the borrower is in a trial modification. The guidance would prohibit foreclosure referral for all potentially eligible loans unless the borrower does not respond to solicitation, was not approved for HAMP, or failed to make their trial modification payments. Servicers will be required to provide borrowers with clear written communications explaining the concurrent foreclosure/modification processes and stating that a foreclosure sale will not take place during the trial period. If a borrower is found ineligible for HAMP, a foreclosure sale cannot be scheduled sooner than 30 days after the date of a Non-Approval Notice so that the borrower has a chance to respond. Servicers must also certify to their foreclosure attorneys that a borrower is not eligible for HAMP before a sale may be conducted.

Addressing Second Liens

The Second Lien Modification Program creates a comprehensive solution to help borrowers achieve greater affordability by lowering payments on both first lien and second lien mortgage loans. In addition to providing the basis for lien holders to share the cost of modifications, this program also supports efforts to reduce total borrower indebtedness by providing the option for second lien holders to receive lump sum payments to extinguish liens entirely. To date, Bank of America, Citi, JPMorgan Chase and Wells Fargo Bank have committed to participate in the program. Together, these four servicers account for just over half of second lien loans and we expect more servicer participation in the future.

Foreclosure Alternatives: For Those Borrowers Unable to Complete a Modification

The Administration is in the final stages of implementation of the HAFA program which will help to prevent costly foreclosures. As noted, the Administration has recognized from the start that not all homeowners can be successfully reached through a HAMP modification or another modification offered by the servicer. A short sale or a deed-in-lieu under HAFA helps borrowers avoid foreclosure, and transition to other sustainable housing in a more dignified way. The Administration expects that many homeowners will avoid foreclosures through HAFA, including borrowers who originally were helped through a trial modification. We also anticipate that HAFA could help establish standard practices that will ease the use of short sales, which are often much better for a family than a foreclosure sale, just as HAMP has helped establish standards for mortgage modifications. HAFA is critical to helping families maintain mobility in the labor force, which has broader economic benefits as well.

Transparency & Servicer Accountability

Over the past year, the Administration has refined the HAMP program to address new challenges.

First, Treasury has taken steps through its compliance activities (on-site field reviews, loan file reviews and targeted reviews) to identify areas of improvement for servicers. We instituted a number of measures to ensure that servicers were improving their responsiveness with homeowners, including a streamlined evaluation process and Borrower Notices for those borrowers who were not approved for a HAMP modification. While servicers have substantially improved their capacity and implementation since program launch and measures of borrower issues like the percentage of servicer-related complaints to the Homeowner's HOPE Hotline have dropped materially, the Administration is still working hard to improve the program in this area.

Second, the Administration continues to augment its reporting to provide meaningful information to the public about the program. In addition to the monthly report, which continues to expand with every installment (e.g., the addition of conversion metrics, eligibility estimates, modification characteristics, geographical data), the Administration recently issued a summary report on HAMP call center activity and will continue to do so quarterly. Treasury will also begin issuing reports on compliance activities in the near future. The Administration will continue to enhance reporting, while balancing the need to protect confidential information and provide only statistically reliable data.

Understanding HAMP Expenditures and Budget

Treasury set aside $50 billion in TARP funds for HAMP. We remain committed to stabilizing the housing market and using the full $50 billion budget to reach and assist at-risk homeowners. The $50 billion allocation included budgets for first-lien HAMP modifications, including Home Price Decline Payments, second lien modifications, HAFA, and other program elements. As the program progresses, we will re-evaluate whether expenditures in these categories are likely to meet the original budget targets. As we determine we can implement productive innovation, we will move aggressively to implement program changes and expansions to assist at-risk homeowners both inside and outside the HAMP program.

Despite the rapidly expanding number of trial modifications and conversions to permanent modifications, so far, HAMP has paid a very small share of long-term expected program costs. HAMP is designed to protect taxpayers with an innovative pay-for-success framework, which means that the taxpayer doesn't pay a penny for trial modifications where the borrower doesn't complete the trial and even after the trial period, continued servicer, investor and homeowner incentive payments are contingent on continued borrower payment performance over the 5 year modification.

As a result of this back-loaded payment structure, to date, only a small amount of incentives has been paid to servicers and investors. To understand how the pay-for-success structure results in back-loaded expenditures, consider expenditures paid to date on permanent modifications. Through February, expenditures were only $57 million, primarily representing up-front servicer payments. However, over the five-year life of these *same* modifications, we will pay out up to $775 million in additional homeowner, investor and servicer incentives.

As discussed, we have made important progress in converting additional modifications to permanent modification over the past few months and we are confident that the number of permanent modifications will continue to increase.

Conclusion
HAMP is the largest mortgage modification program our nation has seen, in size, scope and impact on affordability. In addition to the relief it provides directly, it has impacted the broader industry by forcing mortgage servicers to build up systems to meet unprecedented demand and streamlining and standardizing modification processes across the industry. While significant progress has been made in the first year of program implementation, the Administration continues to work closely with homeowners, mortgage servicers, housing counselors, elected officials, and other key stakeholders to strengthen program implementation and broaden the program's impact.

In addition to the program improvements outlined here, the Administration remains committed to the many other housing market stabilization efforts that work in concert with HAMP, including substantial support for the housing markets through support of Fannie Mae and Freddie Mac to help keep mortgage rates affordable; refinancing opportunities that have allowed more than 4 million borrowers to refinance since the launch of HAMP; an initiative to provide support and financing to state and local housing finance agencies which in turn provide tens of thousands of affordable mortgages to first-time homebuyers and help develop tens of thousands of affordable rental units for working families, including those displaced by the housing crisis and foreclosures.

The Administration is on track to meet the stated program goals and – most importantly – to help prevent avoidable foreclosures for as many eligible American families as possible.

Substantial progress has been made in implementation but the Administration recognizes that real and complex challenges to achieving these important goals remain. For HAMP to reach its potential, implementation must continue to be improved, servicers must recommit to a better borrower experience and outcomes, and program enhancements must continue.