Helping Homeowners Harmed by Foreclosures:
Ensuring Accountability and Transparency in Foreclosure Reviews, Part II

Written Testimony of

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Chairman Menendez, Ranking Member Moran, and members of the Subcommittee, my name is Debby Goldberg, and I am a special project director with the National Fair Housing Alliance (NFHA). Founded in 1988 and headquartered in Washington, DC, the National Fair Housing Alliance is a consortium of more than 220 private, non-profit fair housing organizations, state and local civil rights agencies, and individuals from throughout the United States. Through comprehensive education, advocacy and enforcement programs, NFHA protects and promotes residential integration and equal access to apartments, houses, mortgage loans and insurance policies for all residents of the nation.

I want to thank you for the opportunity to testify here today about the Independent Foreclosure Review (IFR). The IFR was one component of consent orders that the Office of the Comptroller of the Currency and the Federal Reserve Board signed two years ago with 14 mortgage servicers, later expanded to 16 companies. Those consent orders were intended to address widespread failures in those companies' mortgage servicing and loss mitigation systems, as identified in the "horizontal review" that the regulators conducted in the wake of the so-called "robo-signing" scandal.

NFHA and many other civil rights and consumer organizations welcomed the announcement that the regulators had entered into consent orders with these servicers and supported the dual goal of the orders: to ensure that the servicers made changes to their staffing, systems and oversight that would prevent future borrowers from experiencing the kinds of problems that could lead to unnecessary foreclosures; and to identify borrowers whose servicers acted improperly in the foreclosure process and the events leading up to it, and compensate those borrowers for the financial harm they suffered. We only wish that the announcement had come much sooner, so that some of the four million or more homes that have been lost to foreclosure since 2008 might have been saved.[1]

The Negative Impact of the Foreclosure Crisis on Communities of Color

For NFHA, the 2011 consent orders represented an important regulatory milestone. Four years earlier, in 2007, we and four other national civil rights

[1] CoreLogic, "CoreLogic Reports 767,000 Completed Foreclosures in 2012," February 1, 2013, available at http://www.corelogic.com/research/national-foreclosure-report-december-2012.pdf.

organizations called for a national moratorium on foreclosures. We did so because we were hearing from our members and others about the massive level of foreclosure activity occurring in communities of color all across the country. The situation had reached crisis proportions and called for a national response. In previous years, communities of color had been flooded with subprime and other unsustainable mortgages. African-American borrowers were 3 times more likely, and Latino borrowers were 2.5 times more likely to be placed in subprime loans than their white counterparts.[2] Research indicated that significant numbers of these borrowers had credit that was good enough to qualify them for safer, less costly prime loans.[3] Recent settlements between the U.S. Department of Justice and several major mortgage lenders illustrate how financial incentives encouraged mortgage brokers and loan officers to charge higher fees to hundreds of thousand of African-American and Latino borrowers. These incentives also encouraged lenders to steer tens of thousands of borrowers who qualified for prime loans into subprime mortgages that were more profitable for the loan originators, but proved to be disastrous for the borrowers, their communities and our economy as a whole.

While the foreclosure crisis has affected a great many borrowers and communities, some have been hit harder than others. According to research by the Center for Responsible Lending (CRL), by early 2011, 25% of all African-American and Latino homeowners who had mortgages originated between 2004 and 2008 had either lost their homes to foreclosure or were seriously delinquent, a rate twice that of white borrowers. The impact of these foreclosures has been devastating, not only for the families who have lost their homes, but also for their neighbors whose lives and communities and property values have all be affected. CRL's research indicates that $2 trillion of wealth has been lost as a result of the foreclosure crisis. Half of that amount, $1 trillion, has been lost by communities of color.[4] It may be a full generation or more before this lost wealth is regained, and the implications of this loss for our country are profound.

NFHA's own work shows that the negative impact of foreclosures lasts far beyond the event itself. We have investigated the practices of mortgage servicers with respect to maintenance, management and marketing of the homes they have

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[2] Bocian, Debbie Gruenstein, Wei Li, Carolina Reid and Roberto G. Quercia, "Lost Ground, 2011: Disparities in Mortgage Lending and Foreclosures." Center for Responsible Lending, November 2011.
[3] Brooks, Rick and Ruth Simon, "Subprime Debacle Traps Even Very Creditworthy." Wall Street Journal, December 3, 2007.
[4] Bocian, Debbie Gruenstein, Peter Smith and Wei Li, "Collateral Damage: The Spillover Costs of Foreclosures." Center for Responsible Lending, October 24, 2012.

taken back through foreclosure (i.e. their real-estate owned or REO properties). We have found that, compared to REO homes in white communities, REOs in communities of color are many times more likely to have multiple problems with respect to their physical condition, such as leaking roofs, broken windows, unsecured doors, trash in the yard, poorly maintained yards, and the like. They are less likely to be marketed effectively, are more likely to linger on the market longer, and are more likely to be bought by an investor rather than an owner-occupant.[5] All of creates eyesores and hazards and depresses property values for the homeowners who remain.

In sum, the foreclosure crisis has had a significant impact on people and communities of color. For us at NFHA, addressing the sources of these problems and protecting against their recurrence have been a high priority, and one that we see as consistent with our civil rights mission. We were pleased when the OCC and the Federal Reserve announced their consent orders, and were hopeful that the effort to identify and compensate aggrieved borrowers would be an important step towards mitigating some of the damage done by servicers' abuses. We also hoped that the servicing provisions of the consent orders and the regulators' increased focus on servicing practices would result in better loss mitigation so that more borrowers would receive the loan modifications for which they were eligible and be able to stay in their homes.

Importance of the Independent Foreclosure Review and Consent Orders

The 2011 OCC/FRB consent orders, with their provisions requiring the servicers to conduct independent foreclosure reviews, were one of several efforts under way in recent years to address the foreclosure crisis. In 2009, Making Home Affordable was launched, with its HAMP, HARP and Hardest Hit Funds programs. In February, 2012, 49 state attorneys general and several federal agencies reached an agreement with five major mortgage servicers[6], the National Mortgage Settlement (NMS). These efforts are aimed at preventing further foreclosures, by reforming mortgage servicing practices, standardizing loan modification terms and conditions, increasing the use of principal reduction in loan modifications, and making it possible for homeowners who were current on

[5] National Fair Housing Alliance, "The Banks are Back, Our Neighborhoods are Not: Discrimination in the Maintenance and Marketing of REO Properties." April 4, 2012.

[6] The servicers covered by the National Mortgage Settlement include Bank of America, Citi, JP Morgan Chase, Wells Fargo and GMAC/Ally (see www.nationalmortgagesettlement.org for further details). All of these servicers also entered into consent orders with OCC and/or the Federal Reserve Board in April, 2011 and were subject to the requirements of the IFR.

their mortgages but underwater to refinance into loans with lower interest rates. What sets the IFR apart from these other efforts is its emphasis on identifying and compensating borrowers who were harmed by problems in the way their servicer handled their mortgages and their requests for assistance when they could no longer make their payments.

This approach is particularly important from a civil rights perspective. As noted above, a disproportionate number of unsustainable subprime loans were made to African-American and Latino borrowers. Many of these loans became unaffordable and unsustainable, forcing the borrowers into default, in the earliest waves of foreclosures. By the time the consent orders were signed, many of these borrowers may have already lost their homes. However, even if it was too late to help these borrowers save their homes, it was not too late to find them and compensate them, at least in part, for the harm they suffered. For this reason, NFHA has taken a particular interest in the implementation of the IFR process.

Concerns with the Independent Foreclosure Review

The IFR had two components. One of these was the "look-back" process, for which the independent consultants (ICs) that the servicers were required to hire would review samples of files, and where a certain level of errors was found, expand those samples to capture all of the files of borrowers with similar characteristics. The second component was the Request for Review (RFR) process, which provided an opportunity for borrowers who believed they had been harmed to request a review of their particular file, whether or not it was also captured in one of the samples reviewed by the ICs.

Reviewing the files of 4.4 million borrowers who faced foreclosure to determine whether their servicers acted properly, whether the borrowers suffered financial harm, and quantifying that harm is a big, complex undertaking. For NFHA and the civil rights and consumer advocates with whom we work, it was important for the reviews to be:

- conducted in a timely and transparent manner,
- thorough while focusing in on the problems experienced most frequently by borrowers,
- fair and even-handed by capturing the borrower's side of the story, and
- consistent, resulting in comparable outcomes for similarly situated borrowers with different servicers.

Transparency, consistency and fairness have all proven problematic in the IFR process, as is evident in the record compiled by this Committee through its earlier hearings, and in the two reports published by the Government Accountability Office (GAO). With respect to the look-back process, NFHA and other advocates raised several key concerns.

Our first concern was the ***lack of transparency*** due to the regulators' reluctance to make public the rulebook for this undertaking. Despite numerous requests, the regulators never released the guidance they provided the ICs about how to implement the reviews and how to resolve any issues that arose. This lack of transparency undermined public confidence in the process and made it difficult to have confidence that the ICs knew what to look for in the files or how to interpret what they found (or didn't find). This lack of transparency also undermined public confidence that the outcomes would be consistent across servicers.

Further, the ***process did not allow for input from the borrower*** about his or her interactions with the servicer. This was necessary to identify cases where borrowers were given incorrect, inconsistent or conflicting information by their servicers, and to shed light on the many instances in which borrowers submitted the documents required to be considered for a loan modification or other loss mitigation options – often several times – but servicers claimed never to have received them. For many borrowers, this had caused significant and costly delays in the processing of their loan modification applications. In some cases, the mounting arrearages made them ineligible for the modification they requested.

The Request for Review (RFR) process also raised many concerns. Again, the GAO report on the subject lays them out clearly. Many of these problems stemmed from the ***failure to provide for the kind of outreach necessary*** for the RFR process to be successful. This was a problem in the consent orders themselves. No resources were allocated for outreach; no organizations that work closely with borrowers, such as housing counseling agencies or legal services offices, were consulted about the best way to reach borrowers or what role they might play in doing so; no provisions were made for developing effective outreach materials; and no consideration was given to a reasonable timetable for such an effort.

A second, more targeted outreach effort was conducted during the last six weeks or so before the final application deadline. This resulted in a substantial increase

in the number of borrowers who filed an RFR, but in the end only some 11 percent of eligible borrowers made such a request. Many borrowers may not have been in a position to submit an RFR, others may have lacked confidence that the outcome would justify the effort required, and a great many others may simply never have known that the IFR process existed and they could file a request to have their file reviewed. These are just a few of the concerns about the RFR process. Others were detailed in the testimony provided to this Committee by Alys Cohen, of the National Consumer Law Center, on December 13, 2011.[7]

Concerns with the January, 2013 IFR Settlement

On January 7, 2013, the regulators announced that they had reached a settlement with 13 of the IFR servicers, were halting the IFR process at those companies and replacing it with a combination of direct payments to borrowers and other forms of mortgage assistance. The settlement was valued at $9.3 billion, including $3.6 billion in direct payments to 4.2 million borrowers, and $5.7 billion in other assistance. The agencies expressed concern about the slow pace of the IFR process and the substantial cost of the Independent Consultants, already reported to be $2 billion, and stated their belief that the new settlement would put more money in the hands of more borrowers more quickly.

Questions about the Cash Distribution

Borrowers and their advocates certainly shared the regulators' frustration over the pace and cost of the reviews. Whether the new settlement provides a more equitable distribution of relief, however, is a different matter. Last week the regulators released a chart that details how payments will be allocated among 3.9 million borrowers (payment details have yet to be released for borrowers whose loans were serviced by Goldman Sachs and Morgan Stanley). They range from $300 to $125,000. At the top end of the scale, 2,041 borrowers will receive $125,000. These are borrowers who were protected under the provisions of the Servicemembers Civil Relief Act (SCRA), but whose servicers foreclosed on their homes anyway. Another 98 borrowers who were never in default but still lost their homes to foreclosure will also receive $125,000. At the bottom end of the scale, 2,358,441 borrowers whose servicers brought foreclosure actions against them after approving their request for a loan modification, whose servicers never

[7] Cohen, Alys, "Helping Homeowners Harmed by Foreclosures: Ensuring Accountability and Transparency in the Foreclosure Reviews," Testimony before the United States Senate Subcommittee on Housing, Transportation and Community Development of the United States Senate Committee on Banking, Housing and Urban Affairs, December 13, 2011.

reached out to them to offer assistance, or who fall into an "other" category will receive $300 apiece. None of these borrowers filed an RFR. Their 260,623 counterparts in the same categories who did file an RFR will receive either $500 or $600.

The chart raises more questions than answers. For example, it is not clear why responsibility for "slotting" borrowers into specific categories was given to the servicers and why their record systems, which are known to be seriously flawed, were used as the basis for the slotting process. Nor is it clear why certain categories of borrowers were awarded one amount of money and other categories were awarded a different amount. In the end, no determinations were made about which borrowers experienced financial harm. With the exception of the SCRA violations and the borrowers who were never in default, the fact that a borrower falls into a category higher on the chart is no indication that he or she actually experienced harm. Similarly, the fact that a borrower is slotted into a category lower on the chart is no indication that he or she did not experience harm. Given this, it is not clear why there are so many different categories of borrowers and awards, or even any categories at all. And given the likelihood that a great many borrowers never knew about the IFR at all, let alone that they could file a request for review, and the fact that no borrowers knew that doing so would affect the amount of compensation they would receive, it is not clear why borrowers who filed an RFR were awarded so much more compensation than their counterparts who did not file such a request.

These questions are confusing and distressing to borrowers, and I suspect many of the members of this Committee are hearing from your constituents with these and other concerns about how this process has played out.

Advocates have many concerns about the payment process itself. As with the initial RFR process, no resources were allocated for outreach to borrowers to let them know about the change in plans and the fact that checks will be coming their way. Postcards from the payment agent, Rust Consulting, were mailed to borrowers, but these postcards are subject to the same critiques that GAO cited in its report on the previous IFR outreach process. We are already hearing reports that borrowers are confused about the postcards, believe they may come from scam artists, or are simply throwing them out as junk mail.

This, in turn, raises concerns about whether, when the IFR checks are mailed, borrowers will actually open the letters and cash the checks. It is critical for the regulators to track returned mail and cashed checks to determine whether the

funds are not getting through in certain geographic areas or to groups of borrowers, particularly those who may not be proficient in English and may not fully understand the letter of explanation accompanying the checks. Despite advocates' recommendation, the regulators did not send postcards or letters in both English and Spanish, let alone any other languages. If gaps are identified among those borrowers cashing the checks, the regulators should take additional steps to ensure that they have the correct address for borrowers. They should also conduct additional, and where appropriate language specific, outreach in those communities to ensure that borrowers actually receive the funds to which they are entitled.

In addition, it is inevitable that some funds will go unclaimed. The regulators have not announced what will be done with such funds. After every effort is made to locate those borrowers who did not cash their checks and encourage them to do so, we recommend that remaining funds be earmarked to support housing counseling, legal services and other foreclosure prevention services.

Questions about the Other Forms of Assistance to Borrowers

There are also many questions and concerns about the provisions of the settlement relating to non-monetary assistance to borrowers, the so-called "soft dollar" side of the settlement. The $5.7 billion worth of assistance will be provided to borrowers in the form of loan modifications, short sales, deficiency waivers and the like. The servicers themselves will determine which borrowers will receive assistance, how much, and in what form. The structure of this side of the settlement resembles the structure of the National Mortgage Settlement (NMS), in that servicers will receive credit towards their targeted level of borrower assistance for the specified activities.

There are some significant differences between the IFR settlement and the NMS, however, and many of these are cause for concern because they undermine the regulators' stated goal for this part of the settlement, which is to help save people's homes.

Our greatest concern is that, unlike the NMS, the IFR settlement bases the amount of credit the servicer receives on the unpaid balance of the loan, rather than the amount of assistance provided to the borrower. In other words, if a servicer forgives $50,000 worth of principal on a $500,000 loan, it receives soft-dollar credit not for $50,000 but for $500,000. This severely inflates the amount of

credit the servicer receives, and dramatically reduces the number of borrowers who are likely to receive assistance through this program.

An equally alarming aspect of this approach is that it creates an incentive for servicers to focus their efforts on higher-priced homes with larger unpaid loan balances. On a loan with an unpaid principal balance of $500,000, a loan modification that provides any amount of principal reduction – be that $1,000, $10,000, or $100,000 - will yield $500,000 worth of credit for the servicer. A modification that provides the same amount of principal reduction on a loan with an unpaid principal balance of $150,000 will only yield $150,000 worth of credit.

This crediting structure encourages servicers to focus their efforts on large-balance loans. It is likely to disadvantage borrowers in communities of color, where home prices and therefore loan balances are systematically lower than those of comparable homes in predominantly white communities. Thus a process that initially held promise for remediating some of harm suffered by borrowers in communities of color may instead leave those borrowers out in the cold.

In another contrast to the NMS, the IFR settlement places loan modifications – which have the real potential to save the borrower's home – on equal footing with short sales, in which the borrower loses the home. Both receive dollar for dollar credit under the IFR settlement. Unlike the NMS, the IFR settlement places no cap on the amount of credit that servicers can receive for short sales, so if they choose, servicers can meet their entire soft-dollar goals through short sales. Nor does the IFR settlement make any provision for resources to support outreach to borrowers and counseling or legal assistance. Funding for these efforts, which is strictly left to the discretion of individual servicers, will come out of the soft-dollar side of the settlement.

Ways in Which the IFR Settlement Could Still be Helpful

The results of the 2011 consent orders and the IFR process to date have been extremely disappointing. They have failed to identify borrowers who were harmed by the actions or inactions of their servicers, and the checks that are being sent to borrowers will not adequately compensate those who were harmed. Nonetheless, the orders still provide the regulators with two key opportunities to help keep borrowers in their homes, if they choose to use them. These are

through reforming servicing practices and ensuring that help goes to those borrowers and communities that have been hardest hit.

Servicing Reforms Needed

Servicing abuses remain widespread, and too often, servicers still are not providing borrowers with the loan modifications for which they are eligible. This is a problem that the 2011 consent orders were intended to fix, although this component of the orders has received little attention from the regulators, who have been focused on the IFR. While the regulators report that more than half of the more than 4 million homeowners who were in scope for the IFR process have subsequently lost their homes to foreclosure, as many as two million have not. For these and other at-risk homeowners, it is critical that the regulators step up their focus on loss mitigation and servicing reforms.

In addition to the servicing reforms spelled out in the consent orders, the regulators have broad supervisory authority to ensure that servicers comply with other contractual and programmatic requirements. If the regulators were to put more emphasis on servicing reforms in their compliance reviews, borrowers would benefit tremendously. To do this, they must bring their examination teams up to speed on what servicers should be doing, and get input from the field about how servicers are actually performing.

The on-going servicing problems are illustrated by a survey of housing counselors in California, released earlier this month by the California Reinvestment Coalition.[8] The survey focused on the provisions of the NMS and the servicers to which it applies, but the results are indicative of more widespread problems in the industry. Seventy percent of the counselors who responded to the survey reported that the single point of contact provided to borrowers by their servicer to manage and assist in their request for a loan modification was never, rarely, or only sometimes accessible, consistent or knowledgeable. More than sixty percent of counselors reported that the servicers always, often or sometimes pursue foreclosure while the borrower is still under review for a loan modification. Sixty percent or more of counselors reported that servicers never or rarely make decisions about loan modifications within 30 days of receiving a completed modification, and a majority of counselors reported that servicers rarely or never acknowledge receipt of

[8] California Reinvestment Coalition, "Chasm Between Words and Deeds IX: Bank Violations Hurt Hardest Hit Communities." April, 2013. Available at www.calreinvest.org/.

applications in a timely manner or notify borrowers of documents needed to complete their applications. Counselors also reported problems with servicers giving borrowers enough time to supply missing documents, losing documents, and improperly denying loan modifications to borrowers who appear to be qualified for them.

Through aggressive use of their authority under the provisions of the consent orders, as well as their broader supervisory authority, the OCC and the Federal Reserve could help to bring about much-needed changes in servicing practices and help homeowners keep their homes. Advocates have recommended that the regulators take some specific steps to accomplish this:

1. The regulators should increase their oversight of loss mitigation practices and the servicers' compliance with contract, regulatory and programmatic standards.
2. The regulators should require those servicers covered by the consent orders to certify that they have properly reviewed borrowers for loan modifications or other loss mitigation options before moving forward with any action that results in the loss of a home.
3. The regulators should establish a separate appeals or complaint process for IFR borrowers who believe their servicer has acted improperly, and inform those borrowers of this channel for an outside review of their case. Foreclosures should be halted until any such complaints are resolved.
4. In cases where servicers consistently break the rules, the regulators should impose significant penalties.

These four steps could make a big difference for millions of homeowners seeking to stay in their homes.

Ensuring that Help Goes to Those Most in Need

While the consent orders and recent settlement agreements provide the regulators with few tools to ensure that help goes to those most in need, they do allow for the regulators to collect detailed information on the actions that servicers take to meet their soft-dollar crediting targets. Servicers will submit reports to the regulators every 45 days. The regulators should make this information available to the public at a granular level to establish some accountability for the servicers.

Advocates have recommended that the regulators collect and disclose the detailed information by servicer and census tract. The data collected should include, at a minimum:

- the number of borrowers still in their homes,
- the number who have applied for loan modifications,
- the number of modifications approved for both first and second liens(linked where possible),
- the terms of the modification (interest rate reduction, principal reduction, change in payment amount, etc.),
- the number of modifications denied and the reasons for denial,
- the number and dollar value of short sales, deeds in lieu of foreclosure and associated deficiency waivers, and
- the dollars allocated for housing counseling services.

It is critical for these data to be reported at the census tract level. This is the only way to determine whether the allocation of the IFR's soft dollar assistance is going to communities most in need. The lack of such data under the NMS has been a major source of frustration for civil rights groups, community organizations and counseling/legal services agencies. Many of these groups report that their clients and constituents are not receiving offers of assistance under that settlement, and wonder where the help is going. The OCC and Federal Reserve have the opportunity to do a better job of tracking the funds, and we hope Congress will encourage them to do so.

Conclusion

Congress has a crucial role to play in making sure that the federal regulatory agencies responsible for policing the nation's mortgage market do their jobs. Unfortunately, we are not yet at the point where either Congress or the public can have confidence that mortgage servicers are in compliance with their obligations under various enforcement actions, program guidelines or their contractual with their investors. The problems are widespread and long-lasting, with millions of homeowners still at risk of foreclosure, it is important that servicers correct these problems in order to prevent unnecessary foreclosures and speed our economic recovery.

Looking ahead, NFHA is concerned about gaps in the existing servicing standards and those that will go into effect next year. Among other things, these gaps leave borrowers with disabilities, those with limited English proficiency, and the widows and heirs of deceased borrowers without the protections they

need to get the help they deserve from their mortgage servicers. We look forward to working with you to address these gaps in the servicing standards and to make it possible for the greatest possible number of vulnerable borrowers to keep their homes.

Thank you for the opportunity to testify here today, and for your on-going oversight of the Independent Foreclosure Review process. I will be happy to answer any questions you may have.