

June 29, 2011

Acting Director Edward DeMarco  
Federal Housing Finance Agency  
1700 G Street, NW, 4th Floor  
Washington, DC 20552

Dear Acting Director DeMarco,

On April 28, 2011, the Federal Housing Finance Agency (FHFA) announced a new initiative to align the servicing models of both GSEs. The updated framework is intended to establish uniform servicing requirements as well as monetary incentives and penalties for servicer performance. We appreciate the progress made by these steps, especially on modification reviews prior to foreclosure; however substantial gaps remain. Several of the key pillars of the new servicing policy—features that were not announced to the public but were shared on a conference call with stakeholders—raise serious concerns about the limits of the new GSE modification program and should be reconsidered. Moreover, these developments also highlight ongoing concerns regarding GSE policies on dual track, principal reduction and forbearance for unemployed homeowners. Fannie and Freddie (the Enterprises) are estimated to have received \$154 billion of taxpayer investment, and the figure could swell to \$259 billion if we dip into a second recession. FHFA should compel the Enterprises to act in the interest of taxpayers by preventing avoidable foreclosures.

The new articulation of a requirement to review a homeowner for a modification prior to foreclosure, and to actively seek out the homeowner for such a review, is an important step forward. Yet there do not appear to be any similar protections for homeowners who seek a modification after foreclosure has been initiated.

- **The end of dual track should include homeowners currently in foreclosure.** A stop to foreclosure initiation as well as any existing foreclosure during loan modification reviews will better limit avoidable foreclosures, provide a greater maximization of net present value, and stabilize the housing market and communities. While sales should be cancelled during modification review, any continuing need to postpone sale dates should be delegated by the Enterprises. Postponement requests are a burden for the homeowner, the housing counselor, the servicer, and the GSEs, and a source of some of the most troubling mistaken foreclosures.

The standards of the new 5480 modification program will determine whether this new program will be able to provide sustainable modifications to distressed homeowners, or whether it will simply be another underutilized program that misses an opportunity to reform how servicers do business. The contours of this program are of heightened importance because GSE standards have effectively become the industry standards for acceptable servicer behavior.

We recognize the value in the new rules on communication and outreach with borrowers; however, some ambiguities remain. In particular, how will it be determined whether a homeowner and servicer are in good faith modification negotiations and thus that the foreclosure-filing deadline will be extended? Clarifying these issues is essential to ensuring that, where possible, modification reviews occur prior to the initiation of foreclosure.

- **Servicer paperwork lapses should not be considered an end to good faith negotiations.** If a homeowner has submitted paperwork but the servicer has lost it (perhaps repeatedly, which is not uncommon), the servicer's lapse should not result in the homeowner's foreclosure **or the accrual of any additional interest.** The record of servicers losing homeowner documentation or wrongfully denying modifications makes it imperative that the pre-foreclosure review and subsequent foreclosure initiation for failed modification efforts be a rigorous process.
- **The foreclosure filing should be halted until the homeowner has had an opportunity to challenge a denial.** A modification denial should not trigger the initiation of the foreclosure until the escalation process has completed. It is well known that servicers often wrongfully deny homeowners for modifications. The lack of responsible data reporting from servicers on turndown reasons emphasizes this point. Moreover, denials should be accompanied by full documentation of the servicer's reasoning, including NPV inputs and outputs and any relevant investor restrictions and efforts to obtain an exception to such restrictions.
- **Homeowners facing wrongful denials or other servicing challenges should be able to access a functional escalations team at the relevant Enterprise.** Many homeowners seeking GSE modifications now face problems with their servicer and have not been able to receive adequate assistance from the Enterprises themselves. Any new system must include an efficient means for the GSEs to handle escalated cases.

A central issue for struggling homeowners is what the structure of the new modification will be. GSE modification standards should ensure that modifications provide long-term solutions for homeowners and communities.

- **Interest rate reductions should be prioritized over term extensions.** Interest rate reductions favor the accrual of home equity—a core requirement for stable neighborhoods and fewer defaults. Moreover, a waterfall that emphasizes extensions plus forbearance, with severe limitations on interest rate reductions, as discussed below, is likely to result in modifications that rely substantially on balloon payments.
- **Interest rate reductions should go below 5%.** Interest rates should be allowed to move down to as low as the HAMP rates of 2%, if needed to produce an affordable payment and if the ensuing modification returns a net present value over a foreclosure for taxpayers, the ultimate investors in GSE loans. An arbitrary cutoff guarantees that unnecessary and expensive foreclosures will happen, at a high cost to homeowners who are experiencing severe financial hardship and investors who would have profited from a loan modification.
- **Principal reduction, and not just forbearance, should be available.** Principal reductions often significantly improve the sustainability of modifications. The GSEs should include principal reductions **in the waterfall, and, more generally, the GSEs should be** providing principal reductions when they increase the return to taxpayers. **As an immediate step, the GSEs should actively participate in state Hardest Hit Fund and related programs that promote principal reduction.**
- **Loan to value ratios should not limit modifications.** Homeowners should not be required to meet an LTV floor in order to qualify for a modification. Seniors, in

particular, will often have accumulated equity in their homes. They should not be denied a loan modification and forced to seek a refinancing or a reverse mortgage just because they have a significant level of equity in their home. They may be forced to a refinancing or reverse mortgage by the exigencies of the net present value test, which will value the foreclosure option more highly than a modification when there is significant equity, but that is no reason to create an absolute bar.

- **Modifications should be available to homeowners facing imminent default.** The risk of imminent default should include a broad understanding of the factors that can push a family into default, including reduction in family income, death or illness of a family member, or predatory lending.
- **Meaningful forbearance should be available to unemployed homeowners.** The current foreclosure crisis, combined with high unemployment, makes clear that loss mitigation programs do not adequately provide for homeowners facing temporary unemployment. A 12-month period of forbearance with reasonable repayment rules should be established. Homeowners then should be able to seek a modification after the forbearance is exhausted.
- **Any use of trial modifications should include automatic conversions.** Homeowners with HAMP trial modifications more often than not have faced many extra months of waiting before a permanent modification has been provided, if at all. Most of these delays have been caused by servicer delay or wrongful denial of permanent modifications even where the homeowner has met all the trial payment requirements. Automatic conversions to permanent modifications upon payment of the trial period payments must be adopted, with backdating of the permanent modification so that interest arrearages do not accrue during the trial period. Homeowners who fail any trial modification should be given a chance to repay the arrearages through a term extension rather than through a lump sum payment.
- **Improvements in the modification process should apply to the homeowners who are currently in the GSE backlogs.** The new alignment appears to apply only to new delinquency cases coming into the system. The homeowners in the backlog need an equitable and timely solution, which will in turn provide a better return to the GSE balance sheets.
- **The GSEs should pay housing counseling agencies for housing counseling services delivered to their borrowers.** Housing counselors deliver complete borrower packages with documentation, assist homeowners through the difficult modification process, obtain more sustainable modifications, and have better payment histories for their clients. GSEs should work with HUD approved housing counseling agencies to make loan modification more efficient and provide sustainable funding for their services.

We appreciate FHFA's efforts to standardize the servicing practices of the GSEs and hope you will consider these significant concerns in drafting the details of the alignment and GSE policy in general. Any implementation of a protocol also will require substantially increased compliance oversight so that the intended benefits of the program materialize.

Sincerely,

AFL-CIO

Affordable Housing Centers of America  
Alliance for a Just Society  
Americans for Financial Reform  
California Reinvestment Coalition  
Center for NYC Neighborhoods  
Center for Responsible Lending  
Consumer Action  
Empire Justice Center  
National Association of Consumer Advocates  
National Community Reinvestment Coalition  
National Consumer Law Center  
National Council of La Raza  
National Fair Housing Alliance  
National People's Action  
Neighborhood Economic Development Advocacy Project (NEDAP)  
PICO National Network  
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