NATIONAL CONSUMER LAW CENTER

NACA

November 20, 2008

VIA FACSIMILE AND FIRST CLASS MAIL
Secretary Henry Paulson
United States Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, D.C. 202202

Dear Secretary Paulson:

Preserving homeownership and protecting home values are among the central purposes of the Emergency Economic Stabilization Act of 2008, which authorized the Trouble Assets Relief Program ("TARP"). As voluntary measures have made such limited progress, greater efforts from government are essential to stem the wave of mortgage defaults and foreclosures. The new streamlined modification program and other measures available through HUD and HOPE NOW simply will not effectively address the need. Moreover, refinancings will not be available to borrowers who are underwater. The National Consumer Law Center,[1] on behalf of its low-income clients, and the National Association of Consumer Advocates[2] urge Treasury to take more direct action.

Treasury should use the broad powers provided by TARP to mandate affordable modifications through every available means. Treasury should –

- develop a loan modification program that can be routinized and applied on a large-scale basis;
- condition any purchase of an equity interest in a financial institution on a rigorous loan modification plan;
- provide guarantees only for *affordable* loan modifications; and

[1] The **National Consumer Law Center, Inc. (NCLC)** is a non-profit Massachusetts Corporation, founded in 1969, specializing in low-income consumer issues, with an emphasis on consumer credit. On a daily basis, NCLC provides legal and technical consulting and assistance on consumer law issues to legal services, government, and private attorneys representing low-income consumers across the country. NCLC publishes a series of sixteen practice treatises and annual supplements on consumer credit laws. NCLC advocates on behalf of its low-income clients and its attorneys have been closely involved with the enactment of the all federal laws affecting consumer credit since the 1970s, and regularly provide extensive comments to the federal agencies on the regulations under these laws.

[2] The **National Association of Consumer Advocates (NACA)** is a non-profit corporation whose members are private and public sector attorneys, legal services attorneys, law professors, and law students, whose primary focus involves the protection and representation of consumers. NACA's mission is to promote justice for all consumers.

- purchase a sufficient stake in assets to enable the implementation of an aggressive modification program through the purchase of whole loans, second mortgages, securities, or servicing rights.

The basic structure of the servicing industry prevents it from leading the way out of this foreclosure nightmare. Despite the important functions of mortgage servicers, there are no market or statutory incentives to ensure that loan modifications are appropriately considered before foreclosures are initiated. Rather, in the interest of maximizing profits, servicers have engaged in a laundry list of bad behavior, *which has considerably exacerbated foreclosure rates*. Loan servicing abuses typically include misapplication of payments, failure to make timely escrow disbursements, and cascading fees imposed upon homeowners in default. Mortgage servicers have no market deterrents against this behavior. The malfunctions in the servicer industry require a systemic *government sponsored* loan modification program.

An effective TARP program for homeowners lies in the mechanics of the loan modification program. The following principles should be the basis for any federal loan modification program under TARP:

1. **A mechanized program.** A one size fits all approach should be the default program applied to all homeowners, while those with special circumstances are still able to have their needs addressed. The modifications also need to be permanent and sustainable, to ensure that the foreclosure is not simply postponed to a later day.

2. **Objective and flexible affordability analysis.** Loan modifications should be oriented toward an affordable debt to income ("DTI") ratio, such as 38% including taxes and home-related insurance.

3. **Principal reductions to 95% LTV.** Without principal reductions, homeowners will not, if circumstances require, be able to refinance loans which are for more than the home value, make needed repairs, obtain a reverse mortgage, or relocate.

4. **Second liens cannot be ignored.** Loan modifications that address first liens but omit any treatment of second liens simply are setting up homeowners for foreclosure and thousands of dollars in lost equity. The holder of a sleeping second mortgage lien could, after years of good faith payments on the modified first mortgage, seek to collect on the lien, robbing the homeowner of any homeownership gains acquired through the loan modification process. Second liens should be bought out at a nominal price.

5. **Loan modifications available to homeowners whose default is reasonably foreseeable.** Many homeowners are scraping by on their payments – borrowing money from family members, draining savings,

foregoing payment on other debt or utilities, running up their credit cards. These families also should have a chance to obtain sustainable loan terms and regain financial stability.

6. **Fees waived.** Late fees and all default servicing fees should always be waived in loan modifications. As servicers profit enormously from such fees, they often are out of proportion to the loan balance. When fees are capitalized into the loan balance, the loan principal increases substantially. Neither servicers nor homeowners benefit from a system that requires homeowners to challenge the legitimacy of default servicing fees in court proceedings in order to receive a sustainable and affordable loan modification.

7. **Shared loss guarantees should favor the most-needed loan modifications**. Loan modification guarantees should be based on the degree of concessions offered, with greater concessions leading to more significant guarantees.

We hope Treasury will reconsider its approach to administering the TARP program and will focus efforts on addressing the root cause of the crisis—unsustainable loans and the resulting defaults and foreclosures decimating communities across the country. Implementation of a guarantee program would be an important step in the right direction. Should you want to discuss this further, please contact Alys Cohen in NCLC's Washington Office at (202) 452-6252 or Ira Rheingold at NACA at (202) 452-1989.

Sincerely,

Willard P. Ogburn

Will Ogburn, Executive Director
National Consumer Law Center

Ira Rheingold, Executive Director
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cc: Chairman Sheila Bair, FDIC