Testimony of Alys Cohen

National Consumer Law Center

and the National Association of Consumer Advocates

On

Housing Finance Reform: Essentials of a Functioning Housing Finance System for Consumers

Before the United States Senate Committee on

Banking, Housing and Urban Affairs

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Chairman Johnson, Ranking Member Crapo, and Members of the Committee, thank you for the opportunity to testify today on the key components of housing finance reform for consumers.

I am a staff attorney at the National Consumer Law Center (NCLC).[1] In my work at NCLC, I provide training and technical assistance to attorneys across the country representing homeowners who are facing foreclosure, and I also lead the Center's Washington mortgage policy work. Prior to my work at the National Consumer Law Center, I focused on mortgage lending issues as an attorney at the Federal Trade Commission's consumer protection bureau, where I was involved in investigations and litigation regarding lending abuses, and where I drafted the Commission's first testimony regarding predatory mortgage lending in the late 1990s. For over 15 years I have worked to address the harms caused by predatory mortgage lending and have seen firsthand the harms caused in communities nationwide. I testify here today on behalf of the National Consumer Law Center's low income clients and the National Association of Consumer Advocates.[2] On a daily basis, NCLC provides legal and technical assistance on consumer law issues to legal services, government and private attorneys representing low-income consumers across the country.

Congress and the nation face an important crossroads in the life of the housing finance system. At a moment when many communities are still devastated from high foreclosure rates and when access to credit remains too scarce, the contours of a new housing finance system will determine the future of homeownership—who gets it, who doesn't, and how fairly it is distributed. Homeownership and housing finance contribute to family stability, stronger neighborhoods and economic growth. The new system must incorporate mechanisms to assure access and affordability for a wide array of homeowners, including those hardest hit in the recent foreclosure crisis and currently marginalized in today's lending market—communities of color, low-income homeowners, and residents of rural areas. This sustainability must apply to the entire life cycle of a loan, including loss mitigation available during periods of hardship.

My testimony today will provide a brief overview of the state of the housing market and the essential components of a new housing system's approach to lending to consumers while focusing primarily on one key aspect of housing refinance reform, mortgage servicing.

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[1] Since 1969, the nonprofit **National Consumer Law Center® (NCLC®)** has used its expertise in consumer law and energy policy to work for consumer justice and economic security for low-income and other disadvantaged people, including older adults, in the United States. NCLC's expertise includes policy analysis and advocacy; consumer law and energy publications; litigation; expert witness services, and training and advice for advocates. NCLC works with nonprofit and legal services organizations, private attorneys, policymakers, and federal and state government and courts across the nation to stop exploitive practices, help financially stressed families build and retain wealth, and advance economic fairness. NCLC publishes a series of consumer law treatises including Mortgage Lending, Truth in Lending and Foreclosures. NCLC attorneys provide assistance on a daily basis to the attorneys and housing counselors working with distressed homeowners across the country. This testimony is based on the field experience of these advocates as well as our knowledge and expertise in mortgage origination and servicing.

[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.

I. Current Trends Highlight The Need for Better Access and Affordability Throughout the Loan Cycle

While the housing market has improved somewhat from the height of the crisis, more needs to be done to restore a functioning and fair housing market. Approximately two-thirds of mortgage originations in the second quarter of 2013 were for refinancing, not home purchases.[3] The percentage of home purchases by investors has increased substantially. While investor purchases may support housing prices and perhaps even inflate them,[4] it is not a structure that builds a sound and broadly accessible housing finance system. Moreover, the wealth gap between whites and both Latinos and African Americans is larger than it has been since data on the size of the gap were first collected, nearly 30 years ago.[5] The wealth of an entire generation has been eliminated. As these communities begin to rebuild their wealth, homeownership is likely to continue to be a cornerstone of their wealth acquisition.

While much of the discussion has moved to restoration of the lending market, many homeowners are still facing foreclosure. In the second quarter of 2013, 2.13% of prime loans and 11.01% of subprime loans were in foreclosure.[6] These rates are still higher than the percent of loans in foreclosure at the onset of the economic collapse in 2008,[7] a year into the subprime mortgage meltdown,[8] and are much higher than any we have seen since before the turn of the current century.[9]

Moreover, most homeowners with access to loss mitigation still do not get the best modifications available to them, and many who qualify get no modification at all. While HAMP loan modifications have the best results, with post-modification delinquency rates at half of other modifications, [10] most homeowners receive either a proprietary modification with less advantageous terms or no modification at all. In fact, 3% of delinquent homeowners in the second quarter of 2013 received non-HAMP modifications, while only 1% received HAMP trial modifications and another

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[3] Julia Gordon, Testimony Before the Senate Committee on Banking, Housing and Urban Affairs (Sept. 12, 2013), *citing* US Department of Housing and Urban Development and US Department of Treasury, "The Obama Administration's Efforts to Stabilize the Housing Market and Help American Homeowners," (2013), *available at* http://portal.hud.gov/hudportal/documents/huddoc?id=hudjulynat2013scd.pdf.

[4] Julia Gordon, Testimony Before the Senate Committee on Banking, Housing and Urban Affairs (Sept. 12, 2013), *citing* Susan Berfield, "A Phoenix Housing Boom Forms, in Hint of U.S. Recovery," *Bloomberg Businessweek*, February 21, 2013, *available at* http://www.businessweek.com/articles/2013-02-21/a-phoenix-housing-boom-forms-in-hint-of-u-dot-s-dot-recovery.

[5] R. Kochhar, et al., Wealth Gaps Rise to Record Highs Between Whites, Blacks, Hispanics (July 26, 2011), *available at* http://www.pewsocialtrends.org/2011/07/26/wealth-gaps-rise-to-record-highs-between-whites-blacks-hispanics/.

[6] Mortgage Bankers Association Delinquency Survey, Second Quarter, 2013.

[7] Mortgage Bankers Association Delinquency Survey, 1st Quarter, 2012, at 12.

[8] *See, e.g.,* Staff of the Jt. Econ. Comm., 110th Cong., 1st Sess., *The Subprime Lending Crisis: The Economic Impact on Wealth, Property Values, and Tax Reveues, and How We Got Here* (2007).

[9] *See* National Consumer Law Center, Foreclosure Prevention Counseling 7 (2d ed. 2009) (showing rates of subprime and prime foreclosures dating back to 1998).

[10] OCC Mortgage Metrics Report for the Second Quarter of 2013, at 36.

1% received HAMP permanent modifications. The remaining 95% of delinquent homeowners received no modification.[11]

Even for those who receive loan modifications, they often are not adequately keyed to affordability. Homeowners who receive loan modifications with substantial reductions in loan payments fare much better than those with increased payments or even those with small payment decreases.[12] Yet, there is insufficient standardization of payment reductions and post-modification debt-to-income ratios. Modifications that reduced monthly principal and interest payment by 20% or more have, since 2008, consistently had the lowest 60-day delinquency rates in the first quarter of 2013, compared to other modifications.[13] For loans modified in 2012, the six-month 60+ day delinquency rate for loans with payment reductions of at least 20% was 8.8%, while modifications with payments reduced by less than 10% showed delinquency rates at 22.1%.[14] Modifications where monthly payments were increased showed the highest re-default rates at 29%, more than three times as high as the rates for payment reductions of 20% or more.[15] HAMP, with its target DTI of 31%, has produced deeper payment reductions and more sustainable loan modifications than industry modifications without a standard measure of affordability.[16] Moreover, even HAMP has failed to take into account the impact of back-end DTI, which can trigger redefault. .

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[11] These calculations are based on data from the MHA Performance Reports, the NDS Data, and the OCC Mortgage Metrics Report. According to the NDS Survey, 2,393,322 homeowners were 90+ days delinquent during the second quarter of 2013. We adjusted that data to reflect the NDS coverage of the market at 80%. Adding the numbers of new HAMP trial and permanent modifications for April-June 2013, we get a total of 50,000 and 46,077, respectively, or 1% and 1% of the delinquencies. The OCC Mortgage Metrics data reports an additional 90,341 proprietary modifications during the same period or 3%.

[12] Roberto G. Quercia et al., Ctr. for Cmty. Capital, Loan Modifications and Re-default Risk: An Examination of Short-term Impact (2009), *available at* http://www.ccc.unc.edu/documents/LM_March3_%202009_final.pdf; *Modified Current Loans Are Three Times as Likely to Default as Unmodified Current Loans*, Moody's ResiLandscape (Moody's Investors Service), Feb. 1, 2011, at 10; Laurie S. Goodman et al., Pew Ctr. on the States, Modification Effectiveness: The Private Label Experience and Their Public Policy Implications 6-7 (2012), *available at* http://www.pewstates.org/uploadedFiles/PCS_Assets/2012/Goodman_et_al_%20Modification_Effectiveness.pdf

[13] OCC Mortgage Metrics Report for the Second Quarter of 2013, at 39.

[14] OCC Mortgage Metrics Report for the Second Quarter of 2013, at 38.

[15] *Id.*

[16] *Compare* MHA Performance Report Through April 2012 (median HAMP permanent modification has resulted in a 37% payment reduction) *with* OCC Mortgage Metrics Report for the First Quarter of 2011, at 32 (in the fourth quarter of 2011 payment reductions for proprietary modifications were less than half those offered in HAMP, only 14.7%).

II. A New Housing Finance System Should Be Focused on Access and Affordability

Focusing the new housing finance system on access and affordability for homeowners across the country will benefit homeowners, communities, lenders and investors. The role of the secondary market is to provide housing to our nation's families. However, lenders generally cater their loans to the preferences of their investors (which is how the abuses that caused the recent crisis developed—loans were made for investor profits at the expense of sustainability for homeowners). A secondary market focused on access and affordability will be more likely to produce an inclusive market.

Communities without access to affordable credit create vacuums that can be filled by predatory lenders. Those abuses generally have had a disparate impact in low-income communities and communities of color. Subprime mortgage products were sold disproportionately to lower-income homeowners.[17] Studies show that low-income homeowners are denied credit more often, even after adjusting for credit score and affordability.[18] Thus, lower-income families are forced of necessity to seek higher-cost forms of credit. A higher-cost product sold overwhelmingly to lower-income homeowners will, by definition, have a disparate impact on borrowers of color, whose incomes (and assets) lag far behind that of whites—even further behind as a result of the recent crisis. One example of the cumulative disparate impact is that white neighborhoods typically experience housing costs 25 percent lower than similar neighborhoods with a majority of African American residents.[19]

The nation's housing finance system must include mechanisms to ensure that equal housing opportunities are provided in places where sustainable lending has been harder to find. This should be done through several complimentary mechanisms. In addition to properly funding the National Housing Trust Fund and the Capital Magnet Funds, the new system should promote broad access to lending by inhibiting credit rationing and "creaming" of the market. Lenders should be required to serve all population segments, housing types and geographical locations.

Yet, any statute should not dictate specifics of underwriting that would result in less flexibility to meet these broad access goals. Housing finance legislation should leave open the specifics of down-payment requirements, credit scores and debt-to-income ratios. Down-payment requirements are keyed directly to wealth, which itself varies widely by demographics and is not always tied to creditworthiness or ability to repay.

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[17] Center for Responsible Lending (CRL), Lost Ground, p. 26 (2011); Ira Goldstein, Bringing Supbrime Mortgages to Market, Harvard Joint Center for Housing Studies, p. 4; Ginny Hamilton, Rooting Out Discrimination in Mortgage Lending (Testimony before House Financial Services Committee) (2007).

[18] Christian Weller, Center for American Progress, Access Denied: Low-Income and Minority Families Face More Credit Constraints and Higher Borrowing Costs, p. 1 (August 2007).

[19] Ojeda, The End of the American Dream for Blacks and Latinos 11 (June 2009), *available at* http://www.wcvi.org/data/pub/wcvi_whitepaper_housing_june 2009.pdf.

Debt-to-income ratios are an inadequate measure of lending capacity. For some borrowers with very low income, the 43% debt-to-income ratio in the CFPB Qualified Mortgage rule will still result in inadequate cash to cover basic living expenses. Yet the requirement of a 43% debt-to-income ratio also excludes some borrowers who can afford higher payments. Compensating factors and residual income[20] are difficult measures to calibrate and should be left to the regulatory process.

Credit scores often do not provide a reliable picture of a borrower's credit profile. They often contain errors and otherwise reflect disparate access to sustainable credit—a legacy of decades of redlining. Moreover, credit scores cannot predict if any particular person will actually engage in any particular behavior. In fact, often the probability is greater that a particular low-scoring person will not engage in the behavior. For example, a score of between 500 and 600 is generally considered to be a poor score.[21] Yet at the beginning of the foreclosure crisis in 2007, only about 20% of mortgage borrowers with a credit score in that range were seriously delinquent.[22] Thus, if a score of 600 is used as a cut-off in determining whether to grant a loan, the vast majority of applicants who are denied credit would probably have *not* become seriously delinquent. A study by Federal Reserve researcher and a Swedish scientist, based on Sweden consumers, similarly found that most consumers with impaired credit did not engage in negative behavior.[23]

Credit scores also differ substantially by race. Congress should not enshrine these racial disparities into the law by mandating the use of scores. Requiring the use of scores does not just permit a practice with disparate impact--it actively mandates it. Studies showing racial disparities in credit scoring include: a 2012 study by the CFPB, which found that the median FICO score for consumers in majority minority ZIP codes was in the 34th percentile, while it was in the 52nd percentile for ZIP codes with low minority populations; [24] a 2007 Federal Reserve Board report to Congress on credit scoring and racial disparities in which, for one of the two models used by the Federal Reserve, the mean score of African Americans was approximately half that of white non-Hispanics (54.0 out of 100 for white non-Hispanics versus 25.6 for African Americans) with

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20 For a discussion of why residual income can be a better measure of affordability than a straight debt-to-income ratio, see Michael E. Stone, et al., The Residual Income Method: A New Lens on Housing Affordability and Market Behaviour (2011), *available at* http://works.bepress.com/michael_stone/8.

21 FICO, myFICO Insider's Guide to 2010 Credit Card Reform and New FHA Mortgage Rules (2010), (noting that under the Federal Housing Administration rules, "it may be difficult for a borrower to even begin the process [of getting a mortgage] with FICO scores below 600."), *available at* www.myfico.com/Downloads/Files/myFICO_Guide_CCFHA.pdf (visited Sept. 29, 2013).

22 Yuliya Demyanyk, *Did Credit Scores Predict the Subprime Crisis*, The Regional Economist (Federal Reserve Bank of St. Louis Oct. 2008), *available at* www.stlouisfed.org/publications/re/articles/?id=963. *See also* VantageScore Solutions, L.L.C., VantageScore 2.0: A New Version for a New World, 2011 (consumers with VantageScore of 690/-/710, or borderline between "C" and "D" grade, have about a 9% risk of default).

23 Marieke Bos and Leonard Nakamura, Federal Reserve Bank of Philadelphia, Working Paper No. 12-19/R, Should Defaults Be Forgotten? Evidence from Quasi-Experimental Variation in Removal of Negative Consumer Credit Information, Apr. 2013, at 1, available at www.philadelphiafed.org/research-and-data/publications/working-papers/2012/wp12-29R.pdf.

24 Consumer Financial Protection Bureau, Analysis of Differences Between Consumer- and Creditor-Purchased Credit Scores, at 18, Sept. 2012, *available at* http://files.consumerfinance.gov/f/201209_Analysis_Differences_Consumer_Credit.pdf.

Hispanics fairing only slightly better (38.2);[25] and a 2006 study from the Brookings Institution which found that counties with high minority populations are more likely to have lower average credit scores than predominately white counties.[26]

There should be flexibility going forward for determining underwriting requirements for the nation's housing finance system. Without it, the promise of access and affordability would be empty.

III. Housing Finance Reform Should Contain Key Essentials of a Healthy Mortgage Servicing System, including a Requirement for Servicers to Provide Loan Modifications That Benefit the Taxpayer and the Homeowner

Following the recent economic crisis, new mortgage servicing rules have been adopted in an effort to improve loss mitigation outcomes for homeowners facing foreclosure and for the investors in those loans. Despite the creation of the Home Affordable Modification Program (HAMP), changes to FHA and GSE servicing regimes, and the National Mortgage Settlement, the mortgage servicing companies have continued to circumvent existing requirements at the expense of investors, homeowners and communities. While the CFPB issued regulations creating long-term procedural rules on default servicing, additional work is needed. A new GSE system should systematize loss mitigation that benefits investors while avoiding unnecessary foreclosures. Mortgage servicers often benefit from pursuing foreclosure over loss mitigation. Housing finance reform should realign incentives to maximize beneficial outcomes.

Getting servicing right must be a core piece of housing finance reform. The nation's housing finance system should not only make home lending broadly accessible but ensure that the entire life of the loan is supported. Routine processing of loan and insurance payments must not result in errors or abuse that lead to unnecessary costs, defaults and foreclosures. Homeowners facing genuine hardship who can still make loan payments that benefit the investor or taxpayer must have options to save their homes. Properly functioning servicing infrastructure is good for individual families, communities, and the system as a whole.

A. Servicers' Incentives Incline Them Toward Modifications With Increased Fees and Foreclosures Over Sustainable Modifications

Once a loan is in default, servicers must choose to foreclose or modify. A foreclosure guarantees the loss of future income, but a modification will also likely reduce future income, cost

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[25] Board of Governors of the Federal Reserve System, *Report to the Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit* 80-81 (Aug. 2007).
[26] Matt Fellowes, Brookings Inst., *Credit Scores, Reports, and Getting Ahead in America* 9-10 (May 2006).

more in the present in staffing, and delay recovery of expenses. Moreover, the foreclosure process itself generates significant income for servicers.[27]

Servicers do not make binary choices between modification and foreclosure. Servicers may offer temporary modifications, modifications that recapitalize delinquent payments, modifications that reduce interest, modifications that reduce principal or combinations of all of the above. Servicers may demand upfront payment of fees or waive certain fees. Or servicers may simply postpone a foreclosure, hoping for a miracle.

For servicers, the true sweet spot lies in stretching out a delinquency without either a modification or a foreclosure. Income from increased default fees and payments to affiliated entities can outweigh the expense of financing advances for a long time. This nether-world status also boosts the monthly servicing fee and slows down servicers' largest non-cash expense, the amortization of mortgage servicing rights, since homeowners who are in default are unlikely to prepay via refinancing.[28] Finally, foreclosure or modification, not delinquency by itself, usually triggers loss recognition in the pool. Waiting to foreclose or modify postpones the day of reckoning for a servicer. But delay can cost a homeowner the opportunity to obtain a modification.

These dynamics require a housing finance system that promotes sustainable loss mitigation that benefits investors and homeowners. Without aligning the incentives of servicers with those of other stakeholders, public monies and the welfare of communities will be jeopardized.

Recent experience with GSE loss mitigation confirms the need to incorporate a stronger system of servicer accountability into the structure of a new housing finance system. While the U.S. Treasury Department's Home Affordable Modification Program established substantial loan modification rules keyed to affordability, the GSE program lagged behind in several significant ways. Homeowners with GSE loans facing hardship had no effective appeals process when servicers disregarded GSE requirements; yet many homeowners found that servicer noncompliance with GSE rules was endemic. Additionally, GSE rules regarding access to loan modifications for homeowners in bankruptcy (particularly the Fannie Mae rules) have lagged behind other programs. GSE rules allow and even incentivize servicers in many instances to pursue foreclosure while a homeowner is seeking a modification. Finally, the GSE standard modification is not keyed to affordability based on a debt-to-income ratio but rather to a percent of payment reduction that may or may not result in a payment that is affordable.

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[27] A fuller treatment of servicer incentives may be found in Diane E. Thompson, Nat'l Consumer L. Center, Why Servicers Foreclose When They Should Modify and Other Puzzles of Servicer Behavior (Oct. 2009), *available at* http://www.nclc.org/images/pdf/pr-reports/report-servicers-modify.pdf.

[28] *See, e.g.,* Ocwen Fin. Corp., Annual Report (Form 10-K) 30 (Mar. 12, 2009):

> Servicing continues to be our most profitable segment, despite absorbing the negative impact, first, of higher delinquencies and lower float balances that we have experienced because of current economic conditions and, second, of increased interest expense that resulted from our need to finance higher servicing advance balances. Lower amortization of MSRs [mortgage servicing rights] due to higher projected delinquencies and declines in both projected prepayment speeds and the average balance of MSRs offset these negative effects. As a result, income . . . improved by $52,107,000 or 42% in 2008 as compared to 2007.

B. Housing Finance Reform Should Include Several Key Improvements to Existing Mortgage Servicing Rules

The new housing finance system must require affordable loan modifications that are consistent with investor interests. The CFPB, while it has issued a series of procedural requirements for servicers, has declined to issue such a mandate. Yet, the data show that almost all delinquent homeowners still get no modification at all. Those homeowners lucky enough to receive a modification seldom get one with the best terms available. The housing finance system should promote proven regimes for modifying loans with optimum loan performance. This should also include limited, government-backed portfolio capacity to hold modified loans.

Second, homeowners seeking loan modifications should not be faced with an ongoing foreclosure while they are processing their loan modification request. Instead, such foreclosures should be put on temporary hold rather than subjecting the homeowner to the "dual track" of foreclosure and loss mitigation. This is the most crucial procedural protection for homeowners. Homeowners dealing with a foreclosure often face skyrocketing costs and the challenge of repeatedly rescheduling foreclosure sales—as well as the danger and sometime occurrence of the home being sold before the loss mitigation review is complete. While CFPB rules provide some protections for homeowners who have not yet been put into foreclosure, many homeowners seeking assistance after the foreclosure has begun are locked out of a reasonable chance to save their homes. Homeowners in foreclosure should be able to obtain a temporary pause to a foreclosure to promote efficient evaluation of a loan modification application. Additionally, dual track protections must be keyed to the homeowner's initial application in order to promote timely loan modification reviews over foreclosures. Requirements keyed to a "complete application" invite manipulation of the process based on a subjective determination of an application's status.

While existing regulations provide some level of protection against dual tracking, stronger GSE rules are nevertheless appropriate. Because a pause in the foreclosure process during a loss mitigation review is the key procedural protection that stands between a homeowner and an unnecessary foreclosure, substantial flaws in existing requirements must be addressed. Moreover, the GSE system has long been a leader in market developments. The housing finance system should promote the highest standards for loss mitigation, as it has for home lending. Such progress would promote broader market changes and demonstrate the viability of sustainable loan modification reforms.[29]

Third, the new housing finance corporation should be authorized to directly purchase insurance, including force-placed insurance. The current system, in which the GSEs reimburse servicers for force-placed hazard and flood insurance, has resulted in vastly inflated prices for

[29] The GSE guides are a more appropriate locus for some of the other details regarding mortgage servicing. While legislation can take on the structural issues and key needed changes, the regulatory process is the locus for more calibrated treatment of mortgage servicing (as well as lending).

borrowers and, when borrowers default, the GSEs and taxpayers. An investigation by the New York Department of Financial Services found that "premiums charged to homeowners for force-placed insurance are two to ten times higher than premiums for voluntary insurance, even though the scope of the coverage is more limited."[30] It also found that "insurers and banks have built a network of relationships and financial arrangements that have driven premium rates to inappropriately high levels ultimately paid for by consumers and investors."[31] Fannie Mae's Request for Proposal on lender placed insurance in 2012 highlighted the reverse competition typical of this market and the effect on investors and the taxpayer. The proposal noted that "[t]he existing system may encourage Servicers to purchase Lender Placed Insurance from Providers that pay high commissions/fees to the Servicers and provide tracking, rather than those that offer the best pricing and terms to Fannie Mae. Thus, the Lender Placed Insurers and Servicers have little incentive to hold premium costs down."[32] A mechanism allowing the new housing finance corporation to purchase force-placed insurance—as well as title insurance and private mortgage insurance—directly from insurers would decrease costs for borrowers and the corporation by circumventing the kickbacks to servicers that drive up insurance prices.

Fourth, the new housing finance system should promote transparency and accountability. An Office of the Homeowner Advocate should be established to assist with consumer complaints and compliance matters. This would help remedy the current situation in which non-compliance problems with GSE loans often go unaddressed. Moreover, loan level data collection and reporting should include demographic and geographic information, to ensure that civil rights are protected and equal opportunity to avoid foreclosure is provided. Aggregate information about complaints and the data about loss mitigation must be publicly available, as HMDA data is. Work to develop the new housing finance system, and to administer and oversee it, should include stakeholders such as community groups and representatives of homeowners, in addition to the corporate stakeholders on the lending and servicing sides. Finally, in order to ensure that the housing system meets its goals, there must be strong regulatory levers for securing compliance, including robust monitoring, reporting and supervision.

IV. Any Federal Electronic Registry Must Be Transparent, Mandatory and Supplemental to State Rules

Any new, federal electronic registry for housing finance must be available to the public, transparent, mandatory and supplemental to state requirements. Only a public, supplemental system will assure homeowners of access to key information in the foreclosure process while allowing states to continue their role as primary regulators of their own foreclosure procedures and land records.

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[30] Memorandum from Benjamin M. Lawsky, Superintendant, New York Department of Financial Services to State Insurance Commissioners, Reforming Force-Placed Insurance (Apr. 5, 2013).
[31] *Id.*
[32] Fannie Mae, Request for Proposal: Lender Placed Insurance, Insurance Tracking, Voluntary Insurance Lettering Program (Mar. 6, 2012).

There are several important reasons why any federal registry should be supplemental to state systems. First, local registries provide a unified system of records for all interests affecting a particular property: judgments, tax liens, assessments, divorce decrees. A national mortgage registry is unlikely to duplicate this. Second, in many states, such as Massachusetts, the mortgagee holds legal title to real property and the mortgage conveys a distinct property interest. The land registries establish property interests by guaranteeing title to recorded interests such as mortgages. Third, many state foreclosure laws, particularly in non-judicial states, incorporate requirements to record documents in land records in order for a non-judicial sale to convey valid title. These include various notices of default and sale, and even affidavits of compliance with state loss mitigation laws. Several states, such as Oregon and Minnesota, require that mortgages be recorded before a non-judicial sale can take place. There has been disagreement about whether a nominee system like MERS (which designates a straw party to serve as a placeholder regardless of who owns the loan) can comply with one of these recording requirements. Even if the registry name is allowed to substitute for the real owner, use of a universal straw party nominee name destroys transparency. Finally, local land records are fully public and available to all who come to the examine records.

A national registry system should include records of servicing rights, ownership of mortgages and deeds of trust, as well as ownership of the promissory notes themselves. All records should comply with federal e-sign requirements to ensure there is only one authoritative electronic record. The system should assign each security instrument and related promissory note a unique identification number. Participation in the registry system must be mandatory. Enforcement of registry system requirements should include a schedule of sanctions for noncompliance, as well as a private right of action, and attorney's fees, for homeowners with noncompliant loans (with the recoupment serving as a setoff against the loan). Recent history has made clear that without the specter of private litigation noncompliance is common and too often goes unaddressed.

V. Conclusion

Thank you for the opportunity to testify today. The nation's housing finance system is in need of a revived sense of public purpose. Loan origination and servicing mechanisms should ensure broad and sustainable access to credit throughout the life of the loan. I will be happy to take any questions you may have.