

# MORTGAGE SERVICER RESPONSE TO BORROWERS IN CRISIS: *A Report From the Front Lines*

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## Executive Summary

On radio and television, in advertisements and public service announcements, we have all heard what seems like a simple message: “If you are behind on your mortgage loan, contact your lender.” But is dealing with a troubled mortgage really that simple? Is it possible that the recent foreclosure crisis could have been prevented if a few million homeowners had simply called their lenders seeking assistance?

To help answer this question, we turned to people working on the “front-lines” of the housing crisis: foreclosure-intervention counselors. In the midst of the current mortgage foreclosure crisis, foreclosure-intervention counselors serve as mediators between troubled homeowners and their mortgage servicers. They have a first-hand look into the conditions of homeowners facing foreclosure, as well as into how mortgage servicers are responding to homeowners in crisis. This approach gave us access to the experiences of a broad spectrum of homeowners in various markets. It also specifically opened the door on borrowers who showed a desire to save their homes and proactively sought out assistance.

We conducted focus group discussions with 40 counselors in 16 agencies in 12 states in all regions of the country between October 2008 and January 2009. These discussions revealed several important trends:

- Borrower experiences with servicers can be extremely unproductive and frustrating and are often unsuccessful at keeping borrowers in their homes. Indeed, even for the most diligent homeowners or those armed with the assistance of a professional foreclosure prevention counselor, the process of loss mitigation can be lengthy and arduous and may well contribute to the borrower losing his or her home.
- Lack of capacity and accessibility of loss mitigation personnel at mortgage servicers present serious obstacles to the successful modification of delinquent loans. Areas in which servicers need to improve include accessibility, efficiency, communication, consistency, and offering solutions that actually help homeowners stay in their homes.
- Counselors can be a value-added intermediary for both borrowers and servicers; however, counselors are overworked, under-funded, and not used efficiently by servicers. Counselors often waste time trying to communicate with servicers, time that could have been spent helping borrowers.

We also recognized that the foreclosure crisis and servicer responses to it are constantly evolving. In August of 2009, we checked in with the same agencies (13 of the 16 participated) to see where they had noticed improvements or deterioration. This follow-up highlighted good news and bad news:

- We observed positive signs that servicers were becoming more responsive. Particularly since the launch of the Obama Administration’s Making Home Affordable (MHA) program in early 2009, there were indications of at least modest improvement in servicer willingness to seek solutions.

- The fundamental problems mentioned above persisted however. MHA implementation has been slow and spotty, while borrowers' increased demand for assistance has actually bogged some servicers and counselors down.
- Meanwhile, deteriorating conditions are getting ahead of efforts. As of August 2009, counselors reported the growing impact of job and income losses on causing households to default. And, despite continuing value declines and more and more borrowers owing more than their home is worth, we learned of a near total lack of modifications to reduce loan amounts.

Thus, despite reports of many steps in the right direction we come to the conclusion that the traditional servicing model is not set up to meet the challenge of stanching the foreclosure losses. Our report closes with some recommendations for improved foreclosure prevention.

## I. Background

In 2007, mortgage delinquencies began a rapid upward climb, abruptly ending the housing boom. Since the start of 2007, the number of foreclosures has increased threefold; currently, a foreclosure is filed in this country every 13 seconds.<sup>1</sup> Nationwide, home values have declined by more than 30% from their peak,<sup>2</sup> in a vicious cycle of mounting vacant property inventories, tight credit markets, declining home values, and further foreclosures.

As alarm bells sounded across the housing industry in 2007, research undertaken in 2005 by Freddie Mac received significant attention: Freddie Mac found that in more than half of all foreclosure cases, borrowers had no contact with their lenders or servicers.

Citing such findings, industry and policy groups made it a priority to encourage financially strained borrowers to reach out for help. In June, 2007, NeighborWorks America, in partnership with the Ad Council, announced a three-year media campaign with the slogan "Nothing is worse than doing nothing." During just the fourth quarter of 2008, the campaign's television ads reached 74 million households.<sup>3</sup> The campaign encourages borrowers to call a national hotline set up by the Housing Preservation Foundation.<sup>4</sup> (This service later came to be known as the Hope Hotline.) From 2008 through April 2009, the hotline averaged 7,000 calls per day.<sup>5</sup>

In October, 2007, at the encouragement of United States government agencies, the Hope Now alliance of lenders, servicers, industry groups, and counseling organizations was formed to "reach and help as many homeowners as possible."<sup>6</sup> The Alliance's member servicers launched a mail campaign carrying a simple message to troubled homeowners: contact your servicer. They also endorsed and continue to promote and financially support the Hope Hotline.<sup>1</sup> State and local governments have also taken steps to encourage struggling borrowers to reach out. To give just two examples, 1) the City of New York has added mortgage foreclosure prevention counseling to its 311 non-emergency service phone line, and 2) the State of North Carolina requires servicers of certain loans to notify the State 45 days prior to foreclosing; during this window the State sends a letter encouraging the borrower to seek assistance. One of the main goals of this North

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<sup>1</sup> Hope Now alliance members contribute 74 percent, or \$46 million, of the Hotline's annual budget.

Carolina policy, to “improve communication between homeowners, counselors and mortgage servicers,” captures the common theme of much of the policy and industry response to the crisis.

Of course, having borrowers contact their servicers is only the first step. For their part, servicers must respond on a case-by-case basis, whether by proceeding to foreclosure or offering temporary forbearance, short-term repayment plans, or more complex solutions requiring some form of concession.

Faced with mounting delinquencies, the servicing industry has encountered a number of constraints, including inadequate fee structures, lack of capacity, and contractual restrictions. Traditional mortgage servicing operations are designed to efficiently process a large volume of monthly payments for a fee (typically .25% to .50% of each loan’s balance per year). This equation works out as long as problem loans -- those requiring a higher level of engagement from collections and loss mitigation staff -- remain a small share of the total loans managed. But with almost 40% of subprime loan clients not making their most recent monthly payments, servicers’ resources can easily become strained.<sup>ii</sup> The fact that a sizeable share of loans is serviced on behalf of outside parties (investors) further complicates a servicer’s predicament. The servicer is often obligated to continue advancing payments to the investor even if the borrower does not pay; these advances will not be recoverable until resolution of the loan, putting some servicers in a cash flow squeeze. Meanwhile, contracts between servicers and investors (Pooling and Servicing Agreements or “PSAs”) typically set limits on a servicer’s ability to offer concessions that can help keep borrowers in their homes.

Such issues have led to efforts to systematize the loss mitigation process. As early as December 2007, for example, the American Securitization Forum (ASF), which advocates for the securitization industry’s interests, issued a streamlined modification protocol for certain subprime adjustable rate mortgage (ARM) borrowers facing payment hikes due to rate increases or “resets.” The ASF reported 111,000 of these modifications through October 2008.<sup>7</sup> When the FDIC took control of IndyMac, a California lender with significant exposure to subprime and exotic mortgages, it piloted and ultimately endorsed a model loan modification program, nicknamed “mod in a box.” Through these and other efforts, as of April 2009, 7% of securitized mortgages originated from 2005-2007 had been modified.<sup>8</sup> The Hope Now alliance reported that borrower workout plans more than doubled - from a monthly pace of just over 100,000/month in the beginning of 2007 to 270,000/month by the first quarter of 2009.

Still, workout efforts are dwarfed by the sheer number of delinquencies. The alliance also reported 3 million loans 60 or more days delinquent in the first quarter of 2009, up almost 2 million from the start of 2007.<sup>9</sup> Overall, in March 2009, we estimate nearly six million borrowers were behind on their mortgages or in process of foreclosure.<sup>ii</sup> Evidence also suggests that the quality of workouts may be at issue; more than half of all loans that have been modified often slide back into delinquency within twelve months. Many modifications do not reduce the borrower’s payment or balance due and usually increase one or both of these by adding past due

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<sup>ii</sup> According to the Mortgage Bankers Association’s national delinquency survey, as of the 1<sup>st</sup> quarter of 2009, 22.97% of subprime loans were delinquent and another 14.34% were in foreclosure inventory, for a total of 37.3% non-paying; the corresponding figure for all mortgages was 12.07%. On a base of roughly 50 million mortgages, 6 million are thus estimated to be non-performing.

payments and fees to the loan amount. Such “traditional mods” represent a large portion of modifications reported by the industry, but have demonstrated, predictably, a low likelihood of success.<sup>10</sup>

To overcome barriers to borrowers connecting with their servicers and getting the most appropriate loss mitigation plan, networks of housing counseling agencies have been mobilized.

Homeownership counseling dates from well before the current foreclosure crisis; its origin is generally cited as the passage of the Housing and Urban Development Act of 1968. Over time, housing counseling came to focus on pre-purchase services that encourage homeownership. However, the recent foreclosure crisis has renewed the demand for post-purchase counseling, particularly emergency default counseling. In 2007, for the first time since 1999, more housing counseling clients sought post-purchase counseling (including mortgage-default counseling and other types of post-purchase counseling) than sought pre-purchase counseling. Between 2006 and 2007, the number of clients seeking foreclosure-intervention counseling increased by 55%.<sup>11</sup>

Unfortunately, the increase in demand for foreclosure intervention counseling has strained counseling agencies. According to Herbert et. al. (2008), a major challenge for counseling agencies is finding and training foreclosure counselors. Counseling agencies also have difficulty communicating and negotiating with servicers on behalf of homeowner clients because of a lack of servicer responsiveness. Further, counselors often lack the necessary resources, such as grants or loans, to help their clients avoid foreclosure.

Building on the expertise of local agencies that offer pre- and post-purchase housing counseling, Congress began funding a “National Foreclosure Mitigation Counseling (NFMC) Program.” By March 31, 2009, the program had appropriated \$410 million, administered by the federally supported NeighborWorks America, to distribute to some 1,600 agencies. Funds are allocated according to the level of counseling provided, for example, Level One counseling (\$150) involves working with the client to develop a budget and an action plan for the client’s use; Level Two (\$300) requires validation of the budget and assistance with implementing the action plan, and often includes servicer contact by the counselor; Level Three combines Levels One and Two and earns \$450. As well as partially supporting the Hope Hotline, these resources have stimulated a rapid expansion of local housing counseling agency resources, enabling assistance to 410,000 households in the first 15 months.<sup>12</sup>

According to NeighborWorks America, almost half of the clients served cite loss of income as the primary reason for default, while 8% cite medical issues, and 14% report poor money management or increased loan payments. Only 38% have a fixed rate mortgage with an interest rate less than 8% (the remainder have either adjustable rate mortgages or higher-rate fixed rate mortgages). Perhaps as an indication of the success of campaign advertisements, more than half of borrowers are less than 60 days late when they reach out to a NFMC counseling agency. A recent analysis by the Urban Institute found that the earlier the stage of delinquency at the time of counseling, the better the chances of avoiding foreclosure. That analysis of 70,103 borrowers who received NFMC-sponsored counseling found that 76% had not entered foreclosure, and that those who received loan modifications where the payment was reduced were less likely to go into foreclosure than those who received no modification.<sup>13</sup>

Still, significant obstacles to foreclosure mitigation remain. Counseling at Levels Two and higher are highly labor intensive and are estimated to require 10 to 20 hours and, according to some estimates, cost at least \$750 per client.<sup>14</sup> The majority of NFMC funding has gone to Level One counseling activities (70% of the first round).<sup>15</sup> The mortgage industry, which stands to gain from reduced losses and case management assistance offered by counselors, has provided systematic support to the Hope Hotline only.

Meanwhile, counselors report consistent frustrations no matter what level of assistance they provide. Servicer responsiveness is the biggest challenge reported to the NFMC; according to NeighborWorks America, counselors “routinely spend hours and hours on back-and-forth communication with the servicers (typically over a period of many weeks and months)” and “often have to spend a great deal of time pushing back on unrealistic solutions offered by the servicers.”<sup>16</sup> Susan C. Keating, president of the National Foundation for Credit Counseling, echoes this assessment: “The two biggest barriers to foreclosure mitigation are systemic failures on the part of some servicers and the unwillingness of some lenders to provide effective loan modifications.”<sup>17</sup> Counselors involved with North Carolina’s Emergency Program to Reduce Home Foreclosures cite communication problems, inconsistent results, lack of sustainable solutions offered by some servicers, and long response times as concerns.<sup>18</sup> Frustration over borrowers waiting too long or not doing the necessary follow-up work have also been cited. Finally, many counseling agencies report being at capacity, and, overall, the industry continues to call for increased resources. Yet even as counselors work to their limits, delinquencies and foreclosures continue to climb.

To inform the national search for strategies to stem the loss of homeownership, we sought to better understand the experiences of those borrowers who reach out to servicers and counselors for help. We conducted our foreclosure counselor interviews with counselors primarily engaged in Level Two and Three services, at the end of 2008 and the very beginning of 2009--just before the Obama administration took office. At the time of these interviews, national foreclosure counts were hovering around 300,000 per month.<sup>19</sup> A number of states had declared foreclosure moratoria, and certain lenders as well as Fannie Mae and Freddie Mac (who had been taken into government conservatorship in that September) were observing voluntary foreclosure halts as well. While many more modifications were being reported, the majority of these involved “traditional mods,” though a few servicers were becoming more active with concessionary modifications.

At the same time, the unemployment picture was worsening, and the primary cause of foreclosure in many areas was shifting from bad loan products to weak economic conditions. These trends signaled a new phase in the country’s housing crisis even as the new administration introduced its own plan to help troubled borrowers and encourage servicers to modify loans. This sets the stage for the comments provided in the next three sections, derived from the initial interviews conducted at the end of 2008 and beginning of 2009.

To capture the impact of changes since early 2009, we conducted a follow-up poll with counseling agencies in August, 2009, results of which are found in the final section.

## II. The Borrowers

### ***Borrower Paths to Counseling Agencies***

Borrowers facing foreclosure came to counseling agencies through various avenues. The most common referral source by far was the lender or servicer, which demonstrates that mortgage servicers recognize the value of foreclosure-intervention counseling and/or that they would rather deal with counselors than with borrowers themselves.

The second most commonly mentioned pathway into the agency was word-of-mouth referrals from friends, family members, and neighbors, which suggests a high degree of satisfaction among clients. The next two most commonly mentioned referral sources were structural mechanisms that have been put in place to deal with the foreclosure crisis: the Hope Hotline and the counseling referral network sponsored by HUD.

Other referral sources identified by counselors at three or fewer agencies included: the Internet, advertisements in local newspapers, community meetings and workshops, other housing non-profits, local hotlines, local social service/government agencies, offices of public officials, and realtors.

### ***General Borrower Characteristics***

A general theme was that the crisis had brought in not only more clients but also a broader mix of clients. In particular, counselors said clients with higher incomes than their traditional clientele, even as high as \$200,000, were seeking assistance. Additionally, several counselors noted that more elderly clients were coming in for foreclosure-intervention counseling. One counselor summed up the increased diversity of clients:

*Our customer base is all over the board in terms of race, ethnicity, [and] income. It's not just people in the poorer sections of town. You know what I mean? It's not just elderly. It's people making \$20,000 a year. There [are] people making \$120,000 a year. I think that's been the biggest surprise to us is that there are a lot of people struggling out there with their money and obviously their house [is] the priority. So I think it's really hard to characterize. I mean [there are] people that are highly educated, people that aren't.*

### ***Mortgage Characteristics Leading to Default***

Counselors listed ARMs and rate resets most frequently as mortgage features that led their clients to default. The mortgage features noted by counselors as having an impact on default include adjustable rate mortgages (ARMs) versus mortgages with fixed interest rates, option ARMS or variations on ARM loans that may have negative amortization features, a general lack of loan affordability, prepayment penalties, and refinances of previous mortgages. One counselor described these as “adjustable rates that have adjusted the people right out of the house.” As one counselor put it:

*Before the resets they were fine. Once the resets kicked in, then they really started having problems making the payments. Without the resets, we probably would not have the volume that we have today.*

One counselor mentioned that among clients with ARMs, she estimated that 90% had interest rates that had adjusted to over 10%. There was frustration and disbelief that clients had been qualified for such loans through teaser rates. Although clients could afford these initial rates for short periods of time, these loans were clearly not sustainable in the long term.

Other risky loan characteristics had impacted these borrowers. For instance, one counselor described how clients were qualified for loans using the monthly payment calculated for the interest-only payment period. When payments began to amortize, these clients could no longer afford to pay their mortgages. Another counselor's clients were able to purchase homes without having their income verified. These clients could not refinance into a more sustainable loan product when they began to have trouble, as lending standards had tightened at that point and income had to be verified. Finally, another counselor said prepayment penalties attached to clients' loans made refinancing too costly.

Such borrowers were impacted by the plethora of complex and unconventional mortgage products that they did not have the training to understand fully. As one counselor put it succinctly, "People...got hooked into loans that they didn't understand."

### ***Borrower Circumstances Leading to Default***

Those with safer mortgages were not immune to difficulties, however. As one counselor explained, "The fixed rate products...if they come in the door, something catastrophic has happened that has caused them to fall behind." Another counselor similarly saw clients whose loss of employment or reduced income had made their mortgages unsustainable:

*...we began seeing people who originally bought homes they could afford with mortgages that were affordable. But, due to the economic instability, [they] were beginning to lose income, were losing their jobs, maybe getting reemployed at lowered levels of income; and what used to be affordable and sustainable is no longer affordable and sustainable.*

Many counselors' clients were more likely to have encountered financial difficulty related to employment: temporary interruptions in, loss of, or reduction in income. One counselor noted that as the economy worsened his clients were employed at lower-paying jobs than previously and could no longer afford to pay their mortgages. Counselors from another agency pointed out that even a temporary loss of income could cause a client to fall behind on mortgage payments.

Other factors leading to default that were most frequently cited by counselors were recent refinancing, overextension, and medical issues, often in combination.

Clients at three foreclosure-intervention agencies were mostly short-term homeowners or homeowners who had recently refinanced and thus garnered negative equity, particularly in markets where housing values had declined. One counselor estimated that approximately 70% to 75% of his clients had purchased their homes within the last five years, and that 70% of his clients had negative equity in their homes. These counselors said that even many clients with longer tenures had refinanced their mortgages within the last two years to pay off non-housing debts.

The counselors we interviewed often cited the theme of personal responsibility on the part of clients, and stressed that not all were victims of circumstances beyond their control. Counselors at half of the organizations interviewed said that some of their clients' incomes did not cover their expenses. Counselors at three organizations indicated that clients had over-extended themselves financially in their home purchases, what one counselor described as "too much house that they really don't need." Another counselor saw clients who had over-extended themselves with investments in rental properties.

According to a few counselors, clients had also experienced illnesses that caused major financial interruptions or prevented them from working. One counselor said:

*I've seen a lot of people who have been sick, permanently disabled. I have a person who suffered a stroke and they're going through the process of getting on disability and they've been denied several times.*

Additionally, one counselor's elderly clients had encountered trouble because of medical expenses. These clients sometimes took out unsustainable second mortgages to pay off their medical expenses.

### ***Regional Variation***

We noticed variation between high-, low-, and mid-cost housing markets in relation to the loan characteristics and other characteristics leading to default cited by counselors.

Counselors in high-cost markets estimated that 90% to 95% of their clients had obtained ARM or option-ARM mortgages. While counselors in high-cost markets also mentioned employment loss as a factor leading clients to foreclosure-intervention counseling, particularly as the economy worsened, risky loan products were a more prevalent cause for mortgage defaults among their clients. On the other hand, clients of agencies that serve more rural, low-cost markets more typically had difficulty paying their mortgages because of reduction in income or loss of employment. In more mid-cost markets, clients sought foreclosure intervention counseling because of a mixture of these factors. Organizations in these markets approximated that around half of their clients had fixed-rate mortgages while the other half had ARMs.

### ***Client Position in the Foreclosure Process***

Clients come to foreclosure-intervention counseling agencies to seek assistance at many points in the foreclosure process.

In the case of ARM resets, some clients came to counseling agencies before the reset occurs because they know they will have trouble paying the mortgage after the reset. Other clients came to counseling after recently falling behind on their mortgages, a stage at which counselors feel they can offer the most benefit. Unfortunately, some homeowners came to counseling agencies late in the foreclosure process, when it becomes more difficult for counselors to help them stay in their homes. Finally, a growing number sought counseling just before an imminent foreclosure sale. According to one counselor,

*We've had a lot more people that have come in recently that... have had their heads buried in the sand...They're coming in a week before trustee sale asking us to stop it.*

Another disturbing trend reported by counselors at two agencies was the increase in clients whose houses were on the market. Such clients often came in through a referral from their realtor after they had listed the home for a long period of time and were running out of money. One counselor said:

*I'm also seeing realtor referrals where the house has been listed. Things have not been bad. Over the course of time money has run out. Now things are bad and realtors are referring folks to us in that way. I've seen a lot of people whose family sticks with a realtor for six months, a year [but] have not had success and now they're just out of funds, out of options.*

### ***Clients' Psychological Distress***

Counselors reported ample evidence of clients' psychological stress at the prospect of losing their homes to foreclosure.

Adjectives used by counselors to describe clients included "desperate," "scared," "confused," "depressed," and "frustrated." One counselor described the desperation of clients who wanted to know anything they could do to stay in their property. Another counselor echoed this sentiment by pointing out that "some of them seem to be getting more desperate." One counselor noted that much of clients' frustration stemmed from the long delays and uncertainty that they experienced while waiting for a decision from their lender. She discussed the stress that facing foreclosure was putting on couples and families she saw:

*Tears. I've seen tears ... A lot of them have children. Their children are having to watch this happen. You know, Mommy and Daddy, they're so stressed out.*

## **III. The Servicers**

Interviews with foreclosure prevention counselors reveal that lack of capacity and accessibility of loss mitigation personnel at mortgage servicers present serious obstacles to the successful modification of delinquent loans. Even for the most diligent homeowners or those armed with the assistance of a professional foreclosure prevention counselor, the process of loss mitigation can be lengthy and arduous. In this section, we first describe the obstacles encountered when initiating a dialogue with the servicer, and then we describe the types of workout solutions offered by servicers. Finally, we highlight some of the best and worst practices reported.

### ***Reaching Out to Mortgage Servicers***

According to counselors, homeowners who try to contact their servicers directly encounter a variety of obstacles.

Such obstacles include long wait times and an inability to get through to someone with the authority to help. Even if borrowers are able to talk to someone, most are either rebuffed by collections representatives or ultimately leave the encounter confused. It is important to note that a few counselors did cite helpful treatment of borrowers by some servicers. Still, the majority of

counselors described areas for improvement rather than success stories, even when pressed.

The most common obstacle homeowners encounter when they try to contact servicers is being put through first to collections department personnel. Collections representatives usually cannot initiate a loan modification; rather, they can only make a borrower pay or possibly arrange a repayment plan. Often, homeowners are not aware that they should ask for the loss mitigation department, and their encounters with collections leave them discouraged. These homeowners have likely seen public service announcements encouraging them to contact their lenders or servicers, and when they do so the results are surely disheartening, as one counselor emphasized:

*You know that people watch commercials and they say, "Contact your lender. Contact your servicer." Well what happens is when they contact their lender or their servicer they're not going to get to somebody who's actually interested in, trained, paid and etc. to help them. They're getting in touch with somebody who's interested in, trained, paid and etc. to do one thing and one thing only ... Get money.*

A counselor from the Southeast further described borrowers' daunting experiences with collections representatives:

*So customer service might tell them something or they could get transferred to the collections department ... So they're going to pressure the client to get the money and say that they have no option but to pay. So at that point when they get to us sometimes, they're desperate and they're thinking that they're going to lose their property because the lender told them that there was nothing they could do for them.*

Such encounters surely increase borrower distrust and fear of mortgage servicers and make them less likely to initiate constructive dialogue.

In addition, borrowers who attempt to contact their servicers often find themselves tangled in the convoluted web of mortgage servicers' telephone customer service systems. Half of the agencies interviewed described how homeowners attempting to contact their servicers were transferred around many times and unable to talk to anyone who would give them a straight answer. Obviously, this can leave homeowners frustrated and confused, as one counselor from the Mid-Atlantic region pointed out:

*So they have a horrible experience in speaking with the first point of contact and they will get shuffled through about ten different phones and never get to anyone. [This] just [leads to] frustration, and they're scared.*

A counselor from California saw this lack of straightforwardness as a deliberate ploy:

*Unfortunately, these companies use the tactic to defer. They'll send [the borrowers] some paperwork that says fill this out. Then they'll send them back some more paperwork and fill this out. [The borrowers] never really get a straight answer.*

Even if the borrower can reach someone at the mortgage servicer who has the authority to work

out a modification, the borrower faces rejection from inflexible customer service representatives and loss mitigation officers. Four counselors mentioned being contacted by borrowers who had attempted to talk to their servicers and had been flatly denied any sort of modification. One counselor from California said,

*85% that I get [a] phone call on, they contact the lender before they come in and they always get rejected, turned away by their lender.*

Some servicers insist that the delinquent borrower make an up-front payment before entering any negotiation, an unfeasible option for many borrowers whose financial difficulties led them to contact the servicer in the first place. Some servicers are unwilling to modify loans without this payment, even when the borrower is willing and has the ability to resume payments, unnecessarily costing some borrowers their homes:

*[The borrower] only owed two months payments. But the servicer ... refused to accept anything less than two full payments ... That guy is now in the process of foreclosure, isn't up for sheriff's sale yet, but he's already vacated the property and refuses to even try to do anything with them anymore. He just can't take it anymore ... The income was there. It shouldn't have been difficult. It should have been savable.*

### **Negotiating a Workout Solution**

While counselors reported a general increase in willingness to offer workouts and modifications over the time period studied, there remained gaps between workouts offered by servicers and sustainable modifications that would actually allow borrowers to stay in their homes.

One counselor's comments illustrate the distance between certain types of assistance offered:

*Well the least effective would be forbearance agreement where they increase the payment so that the client can get caught up with the monthly payment. That's a useless fix, because if they couldn't afford the payment to begin with, why increase the payment? So a loan modification would make more sense for the client, reducing the interest rate, fixing it for the full term of the loan in most cases and then [putting] any delinquent payments toward the principal down, giving them basically a fresh start.*

#### **➤ Most Common Workout Offered by Servicers—Repayment Plans**

Repayment plans, sometimes coupled with temporary forbearance, were by far the most common form of resolution offered, the counselors reported. They are generally the quickest and easiest way for the servicer to modify a delinquent loan and therefore were usually the first form of assistance offered. As one counselor said:

*Initially what the servicer wants to do is ... especially if the homeowner's talking to collection ... they want to put them in a repayment plan. Basically [the servicer is] trying to get them caught up on the payments by adding the arrearages onto the current home payment, which usually sets the homeowner up for disaster.*

On the surface, this is an ideal situation for the lender in the short term because by increasing current payments they do not sacrifice any principal or interest. Even if the servicer is ultimately

willing to agree to a modification, a catch-up repayment plan is the first offer and, in fact, is the only type of resolution that can usually be worked out by a collections department. Some servicers will in fact do only repayment plans. One counselor from the Mid-Atlantic region said:

*There are those who will only do a repayment. They will not do anything besides a repayment. So we still fight with those servicers who don't, saying [that because of their] investor guidelines, they're not allowed to do [anything except a repayment].*

Most counselors were quick to point out that repayment plans, in general, do not work. If a homeowner has trouble making a payment before contacting his or her servicer, a repayment plan that increases the payment will be even more unaffordable. One counselor put it simply, "If they have a problem making the regular payment how are they going to pay extra?" However, counselors noted that such plans were sometimes the only offer and would at least buy the homeowner some time. Repayment plans were also beginning to be used as trial modifications; if the borrower sustained the payment for a few months, the loan could qualify for restructuring.

Many agencies did report some servicers willing to negotiate loan modifications right away. The most common modifications were interest rate reductions, fixing adjustable interest rates, extending loan terms, or a combination. Many times, interest rate reductions were only temporary. One counselor mentioned that she would only do permanent loan modifications, even if it meant the borrower would end up paying a few extra percentage points of interest, as permanent modifications were much more likely to keep the borrower in the home in the long term. Still, the majority of counselors who saw loan modifications pointed out that they were temporary modifications. The average term mentioned for temporary interest rate reductions was three to five years.

### ➤ **Most Effective Assistance Offered by Servicers--Modifications That Reduce Payments**

The most effective assistance that can be offered by servicers to help borrowers retain their homes is a loan modification that reduces monthly payments to a level the borrower can afford. As one counselor from the Mid-Atlantic said,

*Modification, definitely [is most effective]. If they do modify the terms of the loan to where it becomes affordable to the borrower.*

Unfortunately, the availability of interest reductions fell far short of the levels sought. Our interviews with counselors reveal that the desire of counselors and borrowers to implement interest rate reductions exceeds servicers' willingness to offer them. Counselors across the board emphasized the effectiveness of interest rate reductions; as one counselor from the Southeast put it simply,

*The best solution is a permanent modification to a low interest rate. I mean certainly that would be the best-case scenario for everybody.*

Fixing the interest rate and extending the loan terms were other modifications offered by servicers. To a large extent, the effectiveness of these modifications seems to depend on a

concurrent reduction of the interest rate.

One striking aspect of conversations with foreclosure prevention counselors is the almost complete absence of principal write-downs as a realistic means to keep borrowers in their homes. This is surprising because of the attention given to the subject in academic and policy discussions about possible solutions to “underwater” mortgages, in which the amount owed on the house exceeds the assessed value of the property. If a mortgage is underwater, the homeowner has a powerful incentive to walk away from the house, especially if they are struggling to make ends meet, or need to move to find work or reduce housing expenses.

According to the counselors we interviewed, principal write-downs are just not part of servicer-borrower conversation:

*We’ve seen, for example, modifications in conjunction with principal reductions where the principal owed on the property vastly exceeded the value of the property. We see that very, very infrequently. But if you want a perfect world ... you would adjust the principal balance of a loan to reflect no more than 100% of the property’s current market value and you would adjust the interest rate on the mortgage to reflect a mortgage payment at that new principal balance that was truly, sustainably affordable for that borrower - not on their gross income, but on their net income.*

Other counselors saw principal reductions maybe only once, like one counselor from a high foreclosure market in the Southwest:

*I had one situation where a servicer ... actually did a principal reduction and they gave my client an interest rate of 4% and that was the most amazing modification I had seen.*

For both of these counselors, a principal reduction was an ideal rather than a modification practiced consistently by servicers. Indeed, for most of the counselors, principal reduction was not even discussed:

*It’s been very difficult to get principal reduction... that’s not something that’s on the table.*

### ***Servicer Practices—the Good, the Bad and the Ugly.***

Among different servicers, and even within servicers, there exists a great deal of inconsistency in approaches to clients seeking help with their mortgages. Counselors shared both positive and negative stories about servicers and pointed out that they would like to be able to better predict what to expect from servicers when seeking loan workouts for their clients.

#### **➤ The Good...**

Counselors pointed out that borrower success in working with servicers can depend on several factors: the individual employee at the servicer, the servicer’s organizational structure, and the borrower’s stage in the foreclosure process. Servicer practices associated with positive outcomes

included:

- A Helpful Contact: Counselors reported some very helpful individuals and practices at certain mortgage servicers. According to these counselors, having a good contact at the servicer can help immensely. As a counselor from the Southwest pointed out, these contacts sometimes go above and beyond the call of duty to help homeowners:

*We do work with one [servicer employee] who's our liaison there and she does things like stop sales the day of [foreclosure sale]. Just as long as we can show her that this person can sustain the property, she will go over whoever she needs to stop a sale to just really make sure that the client is getting the service that they deserve. ... She's an angel.*

Five of the counselors said that some homeowners had success in contacting servicers on their own. A California counselor who mentioned that though 85% of her borrowers were flatly rejected pointed out that the other 15% were actively working with their lenders and were just using her for advice. Another counselor said that servicers are generally responsive to borrowers up to the point of foreclosure. A counselor from the Pacific Northwest said that if a borrower was more than 60 days late but had not yet entered foreclosure, they could contact someone from loss mitigation who would generally work with the borrower.

- Willingness and Authority to Modify: Some servicers are willing to help borrowers stay in their homes and come up with inventive ways to do so. Several counselors referenced creative solutions offered to borrowers, such as an interest rate reduction to 2% for a two-year period and a shift of portions of the loan balance to a balloon payment at the end of the loan. Counselors also described instances where servicers helped a client avoid foreclosure even if the client could not stay in the home:

*... the person didn't keep the home, but the servicer did work along with the person in doing a deed in lieu of foreclosure. It took a couple months to get through that, but that's what the client wanted and she didn't want to keep the house at that time. She wanted to do a deed in lieu. She felt that that would look better on her credit record than a foreclosure.*

- Dedicated Departments: Counselors mentioned the evolution from loss mitigation departments to “home retention” or “homeownership preservation” departments by some servicers. Counselors described their experiences with these departments as more positive and productive than interactions with traditional loss mitigation departments:

*[The client] got a loan modification, by just asking if there were other options, she received a repayment plan. And it was under their homeownership retention program. So they got her into that and then they said that she was able to get a Homesaver Advance Program but she also qualified for a national homeownership retention program. So they were able to come up with now three different programs that they didn't have previously.*

*Now we do have the telephone numbers for the HUD Homeownership Preservation department with each servicer and they seem to be much more responsive and quicker to act. I don't know where those people came from but they answer the phone, 'Homeownership Preservation' ...it seems to be a department that's different from the loss mitigation from the servicer.*

- **Fast Turnaround:** Speedy resolution can get the borrower back on track quickly and eliminate frustrations all around.

*I usually can get a decision right on just the first initial phone call because the lenders are plugging it in as you're talking to them, the financial information, and it comes back and gives them a decision on what options the borrower would qualify for. Typically I'll have a loan modification within a week for the borrower to review it.*

- **Improvement Over Time:** Even though counselors noted many difficulties in working with servicers to modify loans, many also acknowledged improvements in the process. Of the 16 agencies interviewed, nine said that it was becoming easier to work with servicers because they were either more responsive or more willing to negotiate and modify loans to terms that borrowers could afford. One counselor's story exemplifies this increased willingness to negotiate:

*At first they had told us they didn't want to work with the client, even though she had a surplus in her budget. And then a week later she received a modification that was reducing her principal, I think by \$30,000, \$40,000, which definitely decreased her payment in about half almost. So that was a really good one.*

#### ➤ **The Bad...**

Despite these best practices, many challenges remained in borrower-servicer interactions, several of which appeared to be due to lack of servicer capacity in the face of high delinquencies:

- **Poor Communication:** Counselors mentioned problems with maintaining a consistent point of contact; this led to difficulty in negotiating a loan workout, as the counselor had to explain the situation to a different person every time he or she called. Callers were also kept on hold for long periods of time. The road from initial contact to final resolution was often fraught with mixed signals, lost documents, and miscommunication. The story of one counselor from the Southeast reflects many stories told:

*A lot of times we try to call the servicer. They're not available. So you'll have to make a follow up appointment or get it released and fax it to the servicer who says, "Well call me back in three or four days" and you call them back and, of course, they can't find it so you have to refax it. And when they do get it...I mean, some of these people we meet with and you think I'm kidding you, probably some people six or seven times. And I mean it's just overwhelming, the follow up. And when you get the papers in, of course, if it is a work out, they will bring those in because they want you to look over them to make sure they're right and then you're caught sending that overnight, plus following up to make sure that's okay.*

As this story illustrates, the most common problems in trying to follow up with servicers were that servicers took a long time to return or did not return phone calls, or servicers lost faxed documents that they needed to approve a modification. One counselor reported that after leaving a message and following up it could take up to three months to get a response and that response time averaged 30 to 45 days. It is likely that most borrowers face a much more challenging situation than counselors when it comes to communication.

- **Slow Response:** The bulk of counseling agencies reported an average of two to four months to modify loans, with three months most common and six months not unheard of. We learned of a case where, because the servicer was taking so long to arrange a modification, her client was actually forced to file for bankruptcy. In another example the borrowers were able to keep their home but the servicer's delays in negotiating a modification ended up costing them a lot of money:

*..the end result was the customer[s] still stayed in their home, but due to the servicer's delay, we had submitted [their] partial claim, which the borrowers were well eligible for with an FHA loan. And because of screw ups with the servicer, the loan went into foreclosure. ... So the borrower[s] ended up having to bring in money for legal fees. ... they were only two months behind when I got involved and it was like an eight month process by the time we actually did the partial claim. So the customer[s] still stayed in their home and they got a partial claim. What should have been a couple months ended up being eight or nine months and \$3,000 more because of legal fees. That's ridiculous.... and they're still in the house and they're making their payments, but it just wasn't right.*

- **Unreasonable Requirements of Clients to Bring Money:** Counselors complained that certain servicers consistently would not negotiate loan workouts unless the client had money to offer. A counselor from one agency described a servicer who would only accept a full or half payment of the client's past due balance:

*I have one servicer in particular that what the client owes is what they want and they are not willing to work with you. They're not willing to modify the payment, no repayment plans, nothing. 'This is the past due balance and this is what she needs to pay us or half of it at least' is what they're asking for, if these clients haven't been making their mortgage payment, there's no way they have half of that past due balance to provide the servicer with. And this servicer just will not budge....at that point, they're not going to modify the loan. They're not going to drop the interest rate. You're just going to basically start over and they're going to add that, the rest into the loan.*

- **Inconsistency:** Throughout, counselors lamented a lack of consistency in terms of service levels, processes, practices, requirements, and responses. This inconsistency existed not only between one servicer and the next, but within servicers, from one contact to the next or from one month to the next. Lack of training, unwillingness to share guidelines, and the changing landscape of housing policy and the industry were cited as causes.

### ➤ **And the Ugly...**

- **Servicer Obfuscation and Inflexibility:** In some cases, a servicer expressed interest in working with a client but would not put forth consistent good-faith efforts to try to successfully complete the loan workout. One counselor even described a servicer that lied to counselors and purposely obstructed loan workouts:

*They either don't respond or when they do ... I'm going to say they flat out lie. Just they flat-out lied to me. One person tells you one thing, so you go with that and then you wait for your time frame. Call to follow up on that. 'Oh well, okay. It's not this, it's that.' And then, 'Okay we're going to send you a modification that's going to say this,' and then you get it and it's completely different from what they said it was going to be. Just crazy stuff like that. It's extremely frustrating. And we're just at their mercy when it comes to that. We can't force them to obviously*

*do anything. We had two of them this summer with [servicer name], which should have both been able to be worked out.*

In this case, the client simply gave up and walked away from the property, an especially disheartening outcome considering that the counselor assessed the case as curable. Another counselor described a case where a servicer offered a modification that she knew would not help the borrowers in the long run:

*Well, I had an older couple earlier this year with [servicer name] ... It took forever to get the modification. When I finally did get it, it was a lousy offer. ...it didn't bring the payments anywhere close to affordable. I fought and fought and fought with them on behalf of the borrower saying, 'You know this isn't really helping the situation at all. It's setting them up for failure again.' Too bad, we couldn't get anything else.*

- Harassment of Clients: Counselors and clients have even been harassed and treated rudely by servicers. One counselor described a particularly disconcerting experience in which a teacher who had lost her job was called a “moocher” by the servicer:

*They talk down to you. They verbally abuse the client if we do a conference call as being ... irresponsible. I had one woman call my client an irresponsible moocher, which I thought was just completely uncalled for. She had lost her job and was ... She was actually a teacher and out here in [state in Southwest] you know there were many teachers that lost their jobs and got a reduction in income for a certain period of time, and this woman was back east and started verbally abusing her for her requiring assistance.*

## IV. How Counselors Can Help

In principal, foreclosure counseling agencies can be advantageous to both servicers and borrowers. First, counselors can help streamline the loss mitigation process by taking on some of the workload from overwhelmed servicers. Second, they can improve the quality of contact between servicers and borrowers, as they may be better equipped to understand and navigate the servicer's world. Additionally, they can obtain better quality information because the borrower is likely to trust the counselor and because the counselor may have more time to spend diagnosing the borrower's true condition. Counselors are also in a better position to connect borrowers to support networks, such as social services, legal aid, employment assistance, and low-cost child care.

### ➤ **Extra Capacity to Help Manage Delinquent Borrower Caseloads**

Counseling agencies reported increases in staffing over the past several months, some even more than doubling, particularly in hard-hit markets. In most cases, the first steps were to shift pre-purchase counselors over to the default counseling function; this was followed by bringing in new, outside resources. The majority of counselors participating in the focus groups had previously performed pre-purchase counseling, with many of these having long experience (an average of nine years) while the next largest component came from the lending industry.

To deal with the growing caseloads as efficiently as possible, some counseling agencies had modified work flows and established divisions of labor. These agencies usually reported having some counselors designated to work with incoming clients, while other resources were allocated to negotiating and following up with servicers or handling reporting, scheduling, and client tracking.

Two of the agencies interviewed had installed software designed to better manage borrower data and identify optimal solutions. At the time of the interview, one had just started using this software and was enthusiastic about its functionality, while the other was waiting to attend a training session. However, there was virtually no data interface with servicers.

### ➤ **Better Communication with Servicers**

At twelve of the agencies we contacted, counselors said that servicers were generally responsive when a counselor called on behalf of a borrower or that servicers were more responsive to counselors than to homeowners. As one counselor from the Southwest put it:

*My contact experiences (with servicers) have been good. Just letting them know who I am, where I'm calling from and what I am doing as a third party seems to open up the door where they're more relaxed in relaying information to me than they are [to] the customer.*

This higher level of responsiveness to mortgage counselors results mostly from the counselor's ability to navigate servicers' tangled customer service phone lines, an often impenetrable barrier for borrowers who wish to renegotiate their loans. Counselors are aware of the need to ask for a loss mitigation representative instead of collections. Counselors at 11 of 16 agencies said that

they used direct numbers to reach loss mitigation departments or were able to get through to the correct person to negotiate a loan modification. Often these counselors had formed working relationships with employees in the servicers' loss mitigation departments. In addition, they often had access to special homeownership preservation phone lines and other phone numbers that were not available to the general public.

### ➤ **Higher Quality Diagnoses**

Several counselors felt they were better at extracting the right data from the client, which is key to finding the most optimal solutions, while getting the budget wrong "is usually the kiss of death." Some borrowers were thought to deliberately understate their desperation, others to overstate it, but the most common problem was simple lack of understanding.

*The number one problem is that they do not look at their financials. They are not prepared before they speak to the servicer and therefore, whatever information they give the servicer that's what the servicer's going to use to review and make a decision on their modification.*

Or, as one counselor pointed out:

*When they're not workable, when the homeowners did themselves.*

A counselor at one agency suspected that lenders send clients to her agency specifically because they know that the agency will help clients assess and work on their budgets, a critical step in reaching the most sustainable solution.

### ***What's Getting in the Way***

Unfortunately, despite the potential benefits that counselors offer, the general experiences deviated markedly, and failed to tap into the full potential value the counseling function offers. Counselors identified a number of obstacles that reduced the level of value they could bring:

### ➤ **Continued Communication Problems**

Counselors face many of the same obstacles as borrowers in dealing with certain servicers' poor communication techniques. Servicer-counselor interaction can be extremely inefficient, which can even cause a borrower to lose a home:

*I can't even tell you how many countless hours I've spent on the phone with [the servicer] trying to get this resolved after it'd been set. Told I was going to get one modification and then got another. ... like it was supposed to be \$2800 down versus about \$6500 down, big difference. Completely different terms. They kept telling me, "Oh no that's wrong. You're going to get the right paperwork. You're going to get the right paperwork" and then it's our eleventh and a half hour. After about three hours being on the phone with [the servicer] I finally get told by somebody, "Oh no. It wasn't approved that way. The paperwork you got is the correct paperwork" and that was the end of that one.*

### ➤ **Inconsistent Servicer Practices**

Counselors frequently dealt repeatedly with the same servicers, and developed a good knowledge

of processes and practices. The reported how servicers' inconsistent offerings in similar situations make it difficult for counselors who have to guess at what types of ratios, hardships, and payment levels a servicer will consider affordable. Instead, it often seemed that a favorable solution is reached because a counselor happens to contact a negotiator who is willing or able to consider a workout.

*If I could just know based on this, if I submit this to [servicer name], this is what I'm going to get - an offer from [servicer name] based on my previous experiences ... but you never know. I would just like to see the consistency to be able to tell a little better up front as to what the outcome will be.*

*Give me the guidelines. I don't want to have to waste two months of my client's time to find out what you want and what you feel is an acceptable ratio to prove that the client can sustain the property.*

### ➤ **Lack of Capacity at Counseling Agencies**

Not unlike their servicer counterparts, counselors reported feeling “overwhelmed” and “stressed out” because of the increased workload and were having trouble just keeping up. Agencies were responding in various ways, such as prioritizing clients with the most immediate concerns, like imminent trustee sales, or offering workshops where they are able to process a large number of cases at a time. Counselors at one agency triaged and “weeded out” borrowers they would be less able to help so that they could use their limited time on cases where they could have the most impact. Meanwhile, counselors were wasting precious time on hold with servicers, being transferred between different departments, or re-sending faxes.

Unfortunately, until such obstacles and inefficiencies are addressed, it is unlikely that the full potential of foreclosure prevention counseling to keep borrowers in their homes will be realized.

## IV. Update, Conclusions & Recommendations

### *Update*

Since these discussions were held, much has been done at the policy level to encourage more loan modifications, most notably, the Obama administration's Making Home Affordable (MHA) program and Home Affordable Modification Program (HAMP). This latter element of the MHA program imposes standards and requirements for loan modifications and provides financial incentives to servicers, investors, and borrowers to implement sustainable modifications. The administration has also set out to craft rules of the road for settling second liens and protect servicers from possible investor backlash over modifications, concerns which have impeded modifications.

On September 9, 2009, the Treasury Department reported on the status of the MHA program, providing evidence that the plan was having a measurable effect: As of the report, eighty-five percent of the mortgages in the country were covered by the HAMP program and 360,000 trial modifications were underway, putting the program on track to reach a goal of 500,000 modifications by November 1, 2009.<sup>20</sup>

However, there remain major concerns, a primary one of which is acknowledged by Treasury's report: the sheer volume of foreclosures and delinquencies. The report outlines steps the administration is taking to address a lack of servicer capacity, to increase transparency, and to improve borrower outreach. As servicers and counselors face an additional influx of calls and even greater demands on their resources, and given the strains already obvious, it seems likely that some of these problems may get worse before they get better.

In August, we once again turned to the participating counselors to tell us what changes they have observed since the beginning of the year, when we first spoke with them, particularly with respect to the main themes already presented:

#### ➤ **Borrower Situations and Experiences with Servicers**

While risky mortgage products and poor financial management continued to be key causes of borrower distress, every agency but one said that job or income loss had become a larger contributor to their case load, with most of them saying it was contributing "a lot" more. With regard to borrowers' experiences reaching out to servicers themselves and getting in contact with helpful staff, about half reported "some" improvement and half reported "some" deterioration; borrower problems navigating servicer communications systems were broadly reported as unchanged.

#### ➤ **Servicer Response and Modifications Offered**

There was a clear increase in likelihood of getting a modification that was sustainable, one with a reduced payment and/or a reduced rate of interest, with just under one-third reporting "a lot" better likelihood. There were mixed responses on whether modifications were more or less likely to be permanent, but there was near unanimous agreement that principal reductions were still not

on the table.

### ➤ **Servicer Attributes**

Along several dimensions, the majority of respondents indicated no change: treatment of borrowers, (in)consistency of guidelines, and use of information collected by the counselors. In the case of communications, servicer shops appeared to be all over the map, with an equal share of counselors observing at least somewhat improved conditions as observed somewhat worse conditions. Two areas showing a bit more improvement on net were accessible/helpful contacts and establishing dedicated departments for foreclosure prevention. On net, servicers earned worse marks in August when compared to the start of the year with respect to turnaround times.

### ➤ **Counseling Agency Dynamics**

All agencies but one have experienced a greatly increased workload. About two-thirds reported at least “some” increase in resources. In general, more agencies than not felt that they are “somewhat” or “a lot” more able to help their clients keep their homes.

### ➤ **Feedback on Making Home Affordable**

With respect to the Making Home Affordable program, general comments from many different agencies conveyed that counselors find it a great concept and a new tool to help borrowers. At the same time, there was marked frustration with the slowness and unevenness of implementation, with servicers who were struggling or not even trying to implement the program, and, as before, with servicer inconsistency and lack of guidelines. Counselors reported an increase in borrower calls and workload for both themselves and their servicer counterparts, and a related slowing of response times, though some complained that servicers were not giving borrowers more breathing room, and sometimes even less. Several counselors pointed out that HAMP addresses mortgage issues, but may not help borrowers struggling with other debt, and thus often raised “false hopes.” As in the earlier interviews, many counselors took up the theme of borrower responsibility, suggesting that getting a workable solution under the current conditions required borrowers to be proactive.

In conclusion, we found the MHA and HAMP programs to be great tools that have motivated more borrowers to seek assistance and helped some servicers to standardize modification decisions. Both the numbers and the feedback from counselors indicates that this plan is having a positive effect on servicer response to borrowers in crisis. Unfortunately, this tool only addresses some of the problems faced, by some borrowers, working with some servicers.

## ***Recommendations***

Based on our Research, we make the following recommendations:

### ➤ **Systematically identify and reward best practices or penalize worst practices.**

We recommend continuing to build on those benefits resulting from the MHA and HAMP programs. Tracking, benchmarking and reporting performance metrics (such as workout ratios, turnaround times, and modification, foreclosure and re-default rates) along with carrots for high

performers and/or sticks for stragglers could guide and encourage better loss mitigation performance.

A number of specific recommendations for improving servicer service delivery have been surfaced in this research project. The Counselors' "Wish List" featured straightforward and actionable suggestions:

- **"I guess my magic wand would be consistency"**

Many counselors just wanted guidelines to know what would be required for certain solutions to resolve delinquency. This would help counselors assess client conditions more quickly and facilitate solutions that would be acceptable to the servicer.

- **Better Communication**

A key area in which counselors would like to see improvements is communication, with seemingly simple requests: single points of contact, direct lines for negotiators, and use of email.

- **More—and More Sustainable—Modifications**

As front-row observers, counselors recognize when a solution is likely to be effective. They repeatedly reported that many workouts offered were temporary, inadequate, and unsustainable. Instead, they called for reasonable sounding concessions, including:

- market level interest rates,

*Let's see five-percent... if they can't afford it at five-percent then let it go ...That's all I want, simple request. And I'm not asking for two percent, I'm not asking you to cut the value in half. It's something within reason.*

- at fixed terms,

*But if I say the lenders were required to do one thing, then I would say that they're to reset the adjustable rate ARMs to fixed rate at something just above the normal lending rate. .... You'd cut foreclosures in half.*

- Or with principal reductions to reflect the true value of the property:

*Principal reduction mortgages, because they're upside down...and a decent fixed rate would be perfect. That would be the perfect world.*

➤ **Monitor the experiences of those borrowers who are trying to do the right thing.**

Mechanisms to obtain feedback from borrowers, particularly those who have reached out to a counseling service, will provide a different and important vantage point on the situation, and give the borrowers some voice in evaluating the success of industry and policy efforts. We suggest regular, representative surveys of borrowers or counselors to get at some of the most common

problems sighted here and by others.

➤ **Better integrate the third party counselors into the loss mitigation process.**

While we did not set out to study counselors, we did gain insight into the potential value of a neutral, qualified, third-party mediator. Unfortunately, we also learned that this potential is not being realized in such a way to maximize returns to the public and private investments that it requires. Better communications and information systems integration between counselors and servicers are examples of two immediate opportunities to increase the value of counseling services.

➤ **Find a solution for underwater borrowers.**

Policy makers need to address the near total lack of loan modifications which take into account the reality that some borrowers owe more on their mortgage than their property is worth. Servicer guidance for when and how to modify loans by reducing principal balance should be incorporated into MHA rules.

➤ **Look beyond incremental changes.**

There is growing recognition that the traditional servicing model and infrastructure is inadequate to today's challenges. As we tinker with the system, foreclosures continue to mount and households continue to lose their homes. This crisis provides the opportunity to rethink the delinquency and default servicing models.

It is not within the scope of this project to identify major new business models. However, related areas to consider include establishing a permanent and more substantive role for third-party counselors. We also recommend exploring more detailed and public reporting of servicing activities on a loan-level basis. Rather than relying on incremental process improvements, special servicers could be brought in to replace worst performing servicers. If current programs fail to stem the foreclosure tide, court-ordered modifications and workouts can encourage servicer cooperation while at the same time giving borrowers another avenue.

Clearly, such solutions will not arise from within the servicing industry; they require the urgent attention of policy makers.

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- <sup>18</sup> State of North Carolina Commissioner of Banks. 2009. The Emergency Program to Reduce Home Foreclosures: Report to Joint Legislative Commission on Governmental Operations. 13 February.
- <sup>19</sup> Source: Realtytrac “Nearly 3.2 Million Foreclosure Filings on More Than 2.3 Million Properties Reported” Jan 15, 2009 <http://www.realtytrac.com/contentmanagement/pressrelease.aspx?channelid=9&ItemID=5681>
- <sup>19</sup> Assistant Secretary for Financial Institutions Michael S. Barr; Written Testimony before the House Financial Services Committee, Subcommittee on Housing and Community Opportunity on Stabilizing the Housing Market. September 9, 2009.

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### ***Notes on Methodology***

We conducted focus group discussions by phone (except for one in-person session) with 40 counselors in 16 agencies in 12 states in all regions of the country (see Table below), and a follow up in August 2009 with 13 of these agencies. Two to five counselors participated in each of the initial focus groups, which took place between October 2008 and January 2009. These in-depth discussions took approximately one hour each; the August follow-up sessions were much briefer. Initial sessions were recorded, transcribed, and analyzed using NVivo 8 qualitative data analysis software.

To provide context, we first asked counselors to identify the circumstances of the homeowners coming to them for foreclosure-intervention assistance. We also asked counselors about developments in their markets and within their organizations. We then raised a series of questions designed to assess the difficulty or ease with which both homeowners and counselors could contact and negotiate with servicers. Additionally, we sought information on what types of loan workout assistance were being offered by servicers and whether that assistance was effective. Throughout the study, we encouraged counselors to cite specific examples. Our follow-up questions probed key themes identified from the initial discussions, asking whether counselors had seen significant improvement, some improvement, no change, some worsening or significant worsening in each area. Discussion guides and follow-up questions are available upon request.

<b>Counseling Agencies by Region</b>	
<b>Agencies by Region</b>	<b>Number in Each Region</b>
Northeast/Mid-Atlantic	2
Southeast	3
Midwest	4
Great Plains	2
Southwest/California	3
Pacific Northwest	2