Executive Summary[*]

When the Panel last examined the foreclosure crisis in October of 2009, the picture was grim. About one in eight mortgages was already in foreclosure or default, and an additional 250,000 foreclosures were beginning every month. The Panel's report raised serious concerns about Treasury's efforts to address the problem, noting that six months after the programs had been announced and two years into the foreclosure crisis, the Home Affordable Modification Program (HAMP) had permanently modified the mortgages of only 1,711 homeowners, that it had failed to address foreclosures caused by such factors as unemployment and negative equity, and that it appeared unlikely to help any significant fraction of the homeowners facing foreclosure.

Since then, Treasury has taken steps to address these concerns and to stem the tide of foreclosures. HAMP began requiring loan servicers to explain to homeowners why their applications for loan modifications had been declined, and Treasury launched a drive to convert temporary modifications into long-term, five-year modifications. In keeping with Panel recommendations, Treasury also announced new programs to support unemployed borrowers and to help "underwater" homeowners – those who owe more on their mortgages than their homes are worth – regain equity through principal write-downs.

Despite Treasury's efforts, foreclosures have continued at a rapid pace. In total, 2.8 million homeowners received a foreclosure notice in 2009. Each foreclosure has imposed costs not only on borrowers and lenders but also indirectly on neighboring homeowners, cities and towns, and the broader economy. These foreclosures have driven down home prices, trapping even more borrowers in a home that is worth less than what they owe. In fact, nearly one in four homeowners with a mortgage is presently underwater. Although housing prices have begun to stabilize in many regions, home values in several metropolitan areas, such as Las Vegas and Miami, continue to fall sharply.

Treasury's response continues to lag well behind the pace of the crisis. As of February 2010, only 168,708 homeowners have received final, five-year loan modifications – a small fraction of the 6 million borrowers who are presently 60+ days delinquent on their loans. For every borrower who avoided foreclosure through HAMP last year, another 10 families lost their homes. It now seems clear that Treasury's programs, even when they are fully operational, will not reach the overwhelming majority of homeowners in trouble. Treasury's stated goal is for HAMP to offer loan modifications to 3 to 4 million borrowers, but only some of these offers will result in temporary modifications, and only some of those modifications will convert to final,

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[*] The Panel adopted this report with a 3-1 vote on April 13, 2010.

five-year status. Even among borrowers who receive five-year modifications, some will eventually fall behind on their payments and once again face foreclosure. In the final reckoning, the goal itself seems small in comparison to the magnitude of the problem.

After evaluating Treasury's foreclosure programs, the Panel raises specific concerns about the timeliness of Treasury's response to the foreclosure crisis, the sustainability of mortgage modifications, and the accountability of Treasury's foreclosure programs.

> **Timeliness.** Since early 2009, Treasury has initiated half a dozen foreclosure mitigation programs, gradually ramping up the incentives for participation by borrowers, lenders, and servicers. Although Treasury should be commended for trying new approaches, its pattern of providing ever more generous incentives might backfire, as lenders and servicers might opt to delay modifications in hopes of eventually receiving a better deal. In addition, loan servicers have expressed confusion about the constant flux of new programs, new standards, and new requirements that make implementation more complex.
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> The long delay in dealing effectively with foreclosures underscores the need for Treasury to get its new initiatives up and running quickly, but it also underscores the need for Treasury to get these programs right. Even if Treasury's recently announced programs succeed, their impact will not be felt until early 2011 – almost two years after the foreclosure mitigation program was first launched – and more than three years after the first foreclosure mitigation program was undertaken.
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> **Sustainability.** Although HAMP modifications reduce a homeowner's mortgage payments, many borrowers continue to experience severe financial strain. The typical post-modification borrower still pays about 59 percent of his total income on debt service, including payments on first and second mortgages, credit cards, car loans, student loans, and other obligations. Furthermore, HAMP typically does not reduce the total principal balance of a mortgage, meaning that a borrower who was underwater before receiving a HAMP modification will likely remain underwater afterward. The typical HAMP-modified mortgage has a balance 25 percent greater than the value of the underlying home.
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> Most borrowers who proceed through HAMP will face a precarious future, but their resources will be severely constrained. With a majority of their income still tied up in debt payments, a small disruption in income or increase in expenses could make repayment almost impossible. Many will have no equity in their homes and are likely to question whether it makes sense to struggle so hard and for so long to make payments on homes that could remain below water for years. Many borrowers will eventually redefault and face foreclosure. Others may make payments for five years under a so-

called "permanent modification," only to see their payments rise again when the modification period ends. The redefaults signal the worst form of failure of the HAMP program: billions of taxpayer dollars will have been spent to delay rather than prevent foreclosures.

Accountability. As always, Treasury must take care to communicate clearly its goals, its strategies, and its specific metrics for success for its programs. The Panel is concerned that the sum total of announced funding for Treasury's individual foreclosure programs exceeds the total amount set aside for foreclosure prevention. It is unclear whether this indicates that Treasury will scale back particular programs or will scale up its financial commitment to the foreclosure prevention effort. Treasury must be clearer about how much taxpayer money it intends to spend. Additionally, Treasury must thoroughly monitor the activities of participating lenders and servicers, audit them, and enforce program rules with strong penalties for failure to follow the requirements.

Treasury has made progress since the Panel's last foreclosure report, and the Panel applauds those efforts. But the Panel also notes that even now Treasury's programs are not keeping pace with the foreclosure crisis. Treasury is still struggling to get its foreclosure programs off the ground as the crisis continues unabated.