

**Testimony of Secretary Thomas E. Perez**  
**Maryland Department of Labor, Licensing and Regulation**  
**Congressional Oversight Panel**  
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Good morning Madame Chair and members of the Panel. Thank you for the opportunity to testify before you today regarding Maryland's efforts to combat foreclosures, barriers to foreclosure mitigation and the need for a meaningful state-federal partnership in these efforts.

Maryland's battle against the foreclosure crisis that has devastated families and communities across our State is approaching the two year mark. Governor O'Malley convened the Homeownership Preservation Task Force in 2007, which led to sweeping legal and regulatory reforms in 2008. The Task Force also led to the creation of an extensive outreach effort and a number of financial assistance products to help homeowners avoid foreclosure. I will begin with a brief summary of our actions, and then discuss some lessons we've learned that could inform any federal action going forward.

**Legal and Regulatory Reform**

In response to the foreclosure crisis and as a result of the Task Force recommendations, Governor O'Malley introduced and later signed into law four bills, all of which received overwhelming bipartisan support from the General Assembly. The new laws created greater protections for homeowners at the front end of the lending process by tightening lending standards and imposing stricter licensing requirements on the mortgage industry. We banned pre-payment penalties for mortgage loans and now require a lender or broker to verify a borrower's ability to repay a loan, including their ability to repay at the fully indexed rate for an adjustable rate loan.

The new laws also eliminated the fast track to foreclosure by extending the foreclosure process in Maryland from a minimum of 15 days to approximately 150 days from default to sale. The foreclosure process law also requires that more notice be given to homeowners before a foreclosure filing and at the time of filing. They also give additional tools to investigators, prosecutors and homeowners to combat mortgage fraud. The new foreclosure process law, meanwhile, provides homeowners with more time and notice to find alternative solutions.

The legislative package also included two laws to crack down on mortgage fraud, including the creation of a criminal mortgage fraud statute and a strengthening of protections against foreclosure scams.

Our legislative package was supplemented by a number of new regulations adopted to combat foreclosures and prevent future crises. The new regulations included the imposition of a duty of good faith and fair dealing on brokers, lenders, originators and

servicers, and a requirement that they show a reasonable net tangible benefit to a borrower when refinancing.

We also created a requirement for servicers regulated by Maryland to begin reporting their loss mitigation activities to the Commissioner. Maryland was the second state to require this information, which allows us to understand the number and nature of loan modifications. Our data has taught us some critical lessons about servicers.

## **Enforcement**

In an effort to help homeowners who were exploited or defrauded by industry professionals during the housing boom, DLLR has stepped up its investigative and enforcement efforts. In 2007, Governor O'Malley authorized 4 new investigators and examiners for DLLR's enforcement and compliance units in order to increase the Department's capacity to crack down on fraud and bad practices.

The increased capacity, combined with a greater focus on holding licensees accountable for bad practices, has led to an increase in enforcement actions, including subpoenas, cease and desist orders, other disciplinary actions and new cases.

In the summer of 2008, eight individuals were indicted in a foreclosure rescue scam conspiracy that was the largest case of mortgage fraud in Maryland history. DLLR's enforcement unit investigated the case of the Metropolitan Money Store, based here in Prince George's County, which involved at least 100 homeowners being robbed of more than \$10 million in equity. One of the new laws passed this year, which reformed the Protection of Homeowners in Foreclosure Act, prohibits the fraudulent conduct that was the centerpiece of the conspiracy in the Metropolitan Money Store case.

The new criminal mortgage fraud statute provides prosecutors with critical tools to punish fraudulent activity. The statute also provides homeowners with a private right of action, which expands the enforcement opportunities under the law.

## **Outreach**

The Homeownership Preservation Task Force also led to an extensive outreach effort to help more homeowners facing foreclosure now. The State created the HOPE hotline to allow homeowners to access assistance from housing counselors. The hotline has taken upward of 20,000 calls from homeowners and helped thousands of them keep their homes. Working with the judiciary, we elicited a call for pro bono attorneys to assist homeowners facing foreclosure, and more than 700 have been enlisted in the effort. Homeowners can access their legal expertise through the hotline. We launched a multi-media outreach campaign to advertise the hotline and the assistance available by advising homeowners to seek help immediately.

As a result of the new foreclosure process law, the Commissioner now receives a copy of the Notice of Intent to Foreclose that a lender must send to a borrower at least 45 days

prior to filing a foreclosure action. The Commissioner's office sends each of these borrowers information about how to seek help and warnings about foreclosure-related scams. To date, we have sent more than 80,000 such information packets to homeowners.

### **Servicer Agreements**

Early in 2008, responding to reports that homeowners in distress were having difficulty even getting their servicers on the phone, let alone accessing meaningful loss mitigation services, Governor O'Malley announced plans to meet with servicers to address this problem. Representatives from major loan servicing companies, as well as Fannie Mae and Freddie Mac, met with the Governor and Administration officials in February and March. From those meetings, a framework for a streamlined and transparent loss mitigation process was developed. Intensive discussions with more than a dozen loan servicing companies to negotiate the details of the framework ensued. Six major servicers that represent nearly 25 percent of the state's mortgage market signed agreements with Maryland. Citi, HSBC, Ocwen, Litton, GMAC ResCap and AmeriNational Community Servicing, Inc. pledged to abide by the following five-point framework for loss mitigation:

- I. Process—Maryland's 5/10/60 Timeline for Loss Mitigation
  - 5 days: Acknowledgement of Receipt of Loss Mitigation Package
  - 10 days: Confirmation of Completeness of Package
  - 60 days: Decision Made on Loss Mitigation and cooling off period that halts a foreclosure action and the accrual of fees until a decision is reached
- II. Team Maryland – Servicers designate key contacts for Maryland homeowners
- III. Technology – Commitment to explore and utilize technology to expedite the process.
- IV. Modification Guidelines – Sharing acceptable guidelines and parameters for loan modifications
- V. Marketing and Outreach – Participating in the outreach efforts to reach homeowners

These servicers have worked with our foreclosure prevention network to provide information about their guidelines and resolve cases. Our work with these servicers is ongoing and we are expanding our discussions to improve the process and results of short sales.

### **Modification Data: What We've Learned**

Maryland has been at the forefront of data collection. Our reporting requirement for servicers enacted last year has enabled us to collect data on roughly 380,000 Maryland mortgage loans. This data has provided a window into modification activity and has informed the other elements of our strategy.

For example, while modification volumes began to increase in early 2008, we became increasingly concerned through our examinations, complaints from borrowers,

discussions with servicers and other sources, that these modifications were actually providing astonishingly little relief.

As a result, we began to collect data not only on modification activity, but on the impact of modifications on monthly payment. We have collected that data since August, and we believe we are the only government entity at any level gathering this information.

The results have been startling – in August and September, roughly 60 percent of the modifications reported resulted in the same or an even higher monthly payment. More recently, this data has improved somewhat. The percentage of borrowers receiving a modification where their payment remained the same or increased fell to 52 percent in October and 43 percent in November.

Meanwhile, Countrywide, our largest reporting servicer, continues to report each month that 75 percent or more of its modifications do NOT lower the borrower's monthly payment.

Through our negotiations with servicers, we learned that in the vast majority of cases, loan servicers have substantial discretion to modify the terms and conditions and loans, including the ability to reduce principal owed. However, while all servicers claim to want to avoid foreclosures, the data suggests that efforts to do so have been more talk than action. They have lacked the will to exercise their authority and provide homeowners with sustainable modifications, including principal reductions. Recently, there has been some improvement and we look forward to more gains with the President's new initiative.

### **Data Limitations and Need for Federal Cooperation**

Your invitation also suggested that I comment on the level of cooperation that we have received at the federal level. As I consider these data collection efforts, I must convey that our experience has been less than productive and, frankly, at times frustrating. Understanding the limitations of our reach as a State regulatory agency, and realizing that data about monthly payment impact was critical, we worked with Congressman John Sarbanes in July 2008 to craft a request to the OCC and OTS to collect similar data.

While our data is limited because our regulatory authority is limited, federal regulators have access to loan level data on millions of loans nationwide and are well positioned to capture critical data including payment impact data. As Congressman Sarbanes wrote in his letter, "as the volume of modifications continues to grow, an accurate picture of the nature of these modifications becomes more critical by the day." Congressman Sarbanes received a letter from both the OCC and OTS on September 3, 2008 denying his request.

Since that time, the OCC and OTS released new data showing the number of redefaults for loans modified earlier in 2008. They expressed shock at the high percentage of borrowers who redefaulted – about 50 percent – and indicated that the results raised questions about the efficacy of modifications. While they may be shocked, we were not.

If most distressed borrowers don't receive modifications that lower monthly payments, it should come as no surprise when those same borrowers default again.

This effort highlights the importance of asking the right questions. Our public debate on modifications should be based on the right data – and it hasn't been. Our state was fortunate to have statutory licensing authority to gather payment data, but most other states were not so lucky. With the servicing industry continuing to consolidate in federally chartered banks and holding companies, we will only be more dependent on Federal oversight in the future. As we regulatory restructuring is considered, our experience is instructive. It highlights the critical role of state regulatory oversight. States are in a key position to identify and respond to emerging market trends and developments, such as the need for monthly payment data.

As they move forward with their data collection, I would offer an additional suggestion. We know that minority homeowners were disproportionately impacted by the subprime lending spree that led to this crisis. While 18 percent of white homeowners were given subprime loans, 54 percent of African American homeowners and 47 percent of Hispanic homeowners received subprime loans. In Maryland, those communities with large minority populations, including Prince George's Counties, are the ones most impacted by the foreclosure crisis. As they begin collecting meaningful data about the number and nature of loan modifications, federal regulators should also require data on the race and ethnicity of borrowers receiving the modifications to ensure there are no violations of the Fair Housing Act.

I understand that servicers may raise concerns about whether they can report such data. I would suggest, however, that this is precisely the type of data collection contemplated by the Reg B exemptions and it is specifically analogous to the HMDA reporting that is done at origination. HMDA data has provided us with exceedingly useful information to gauge lending practices. That same data is no less necessary in the context of unprecedented large-scale loan modification programs that involve federal dollars. This data should be among the requirements we make of servicers and lenders in exchange for their voluntary participation in these programs. This data should be part of the core accountability we require.

### **Consumer Protection**

This crisis shines a light on the need for consumer protection and every phase of the lending and homeownership process, and for regulatory reform at the federal level.

As noted above, Maryland licenses and oversees servicers, which has enabled us to take certain steps, including imposing a duty of care on servicers, conducting examinations and collecting data. However, the impact of these steps is muted daily by Federal pre-emption, and the problem is getting worse every day. As servicing entities continue to consolidate under Federally-preempted entities, our regulatory authority shrinks. With the acquisition of Countrywide by Bank of America, we now license servicers handling less than 20 percent of Maryland loans. Other licensees are owned by investment banks

which have now become bank holding companies. Our leverage in this area is weak and weakening.

This wouldn't be so discouraging if our Federal counterparts had been up to the regulatory task in recent years. While the FDIC has shown creativity and leadership, the OCC and OTS, which regulate the servicers that dominate the mortgage market, have been behind every step of the way.

A lack of oversight by federal regulatory agencies, along with a regulatory focus on the banker rather than the lender got us into this mess. There is a need for real reform at the federal level to ensure we don't repeat history, and the reforms must be consumer focused.

I would also caution federal regulators as they move forward with the President's plan to modify loans to stay alert for the growing phalanx of "loss mitigation specialists." As in the case of foreclosure rescue scams over the last several years, scam artists are eager to take advantage of homeowners trying to modify their loans, and they will be on the prowl for vulnerable homeowners who are eligible for assistance through the new federal program.

Already we are seeing the emergence of this burgeoning industry which charges homeowners up front fees and claims it will help them access modifications in return. Typically this ends in nothing but wasted money and, worse, wasted time. As a result of our new laws in Maryland, if a homeowner is more than 60 days in default anyone offering assistance, including a "loss mitigation specialist", is prohibited from collecting upfront fees for these services.

While we have recovered thousands of dollars of fees paid by borrowers in our state, we can never recover the time that could have been spent accessing a real modification. Similarly, credit repair operations are on the rise during these troubled times. In Maryland these companies are prohibited from charging upfront fees. These businesses wind up taking money that could have been used to reduce the consumer's debt and leave the consumer in the same poor credit shape they were in before. We are working hard to get the word out that consumers shouldn't pay upfront fees for these services and, more importantly, it is help they can get for free or do themselves.

In many ways, these are state enforcement issues, best overseen and addressed at the state level. However, I would urge that federal efforts be tailored to support these efforts, particularly as the President's program ramps up. Thought could be given to capping third party fees in modifications, or to banning them altogether. At a minimum, however, simple disclosure should be required for these modifications, including pre-and post-modification payment, balance and other key terms. It should also include the name, address and amounts involved of any third party fees that have or will be paid. All of these data items could be easily captured by HUD for oversight, and our state could then access this data, review the third party information and move forward with oversight armed with accurate and timely information

## **A State-Federal Partnership**

So far, federal programs have been of very modest help to our foreclosure related efforts.

While the counseling support provided through Neighborworks has been extremely helpful in providing assistance to homeowners and working with servicers, other resources have been limited. State resources financial assistance programs to address the foreclosure crisis have been limited, and the lack of uptake in the federal programs, such as Hope For Homeowners, is well documented.

More structural approaches through HOPE Now or Fannie Mae and Freddie Mac have also provided only limited relief. These entities have thus far been unable to create a standardized modification process and, while their efforts have resulted in a large number of modified loans, the modifications have not been sustainable and have resulted in high rates of redefault.

President Obama's new housing initiative seeks to rectify this balance and to join the battle with substantial federal resources. We welcome the assistance. The standardization that will result will have lasting impact. After billions of dollars of our federal response to this housing-driven crisis have been devoted to the security holder, focusing some resources to the borrower is clearly warranted and overdue.

Going forward, it is critical that the federal government work in partnership with the states. Our efforts have been aggressive ongoing, but our reach is limited. At the same time, we would encourage the federal government to avoid taking any steps that would pre-empt stronger protections at the state level.

## **Lessons Learned**

Our efforts in Maryland have provided us with a number of insights into what is needed going forward to address the national foreclosure crisis. We hope you will consider these lessons in your work, and that they will be used to inform the comprehensive federal efforts:

- In the majority of cases, servicers have substantial discretion to modify the terms and conditions of mortgage loans. This includes the ability to reduce principal owed. Until now, they have not exercised this ability to the extent necessary to make a meaningful dent in the number of homeowners facing foreclosure.
- Collecting timely data is critical to ensuring we understand how many people are accessing help and to informing our efforts to combat foreclosures. More importantly, the type of data we collect is critical – if we are not collecting the right data, we cannot understand how many people are or are not receiving real help. We must track detailed data at the federal level about the number and nature of loan modifications, including principal reductions.

- We should also collect data regarding the race and ethnicity of borrowers receiving loan modifications. We know minority homeowners disproportionately received subprime loans in the years leading up to this crisis. We must ensure discrimination is not keeping them from receiving real help now. We understand that there
- We must refocus regulatory efforts on consumer protection, and learn from the mistakes of the past. We should revamp those regulatory agencies that for too long have been bank oriented, and ensure that going forward they remain consumer focused.
- States do not have the resources nor the reach to address this crisis in a vacuum. In order to effectively combat the foreclosure crisis, the federal and state governments must work together.

Thank you for allowing me to address you today regarding our efforts and the gaps that must be filled by federal efforts. I am optimistic about President Obama's plan going forward, and I and other Maryland officials look forward to working with his administration in partnership in the future.