Remarks by

John G. Walsh

Chief of Staff and Public Affairs

Office of the Comptroller of the Currency

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Renae, thank you for that introduction and for arranging this panel. I'm really glad to be here, in part because this is probably one of the few audiences outside of a banking industry that might not be expecting me to talk about the latest design idea for the $20 bill. The Office of the Comptroller of the Currency isn't exactly a household name, but with the work each of you does in explaining mortgage lending and banking issues, I suspect that you knew what the OCC does – even before Renae's kind introduction. But since I don't get as many opportunities as I would like to talk about the OCC, I'll take just a minute to give you a thumbnail of our agency.

The OCC was the creation of President Lincoln, which means that we're the oldest of the federal bank regulatory agencies. The banks we supervise represent about 70 percent of the industry's assets. Among them are many of the nation's largest financial institutions, including JP Morgan Chase, Bank of America, Wells Fargo and Citibank. We maintain resident staff at each of our largest banks – examiners who work on nothing else but the bank to which they're assigned. At our largest banks, we have more than 60 examiners on-site all the time, supplemented, of course, by experts from our Washington policy shop on such things as risk modeling and securitization.

However, most of the banks we supervise are smaller, community-based institutions. Even for the smaller banks, we have an on-the-ground presence. We have more than 1,700 examiners, located in virtually every state in the country, devoted to the supervision of community banks. We were visited this week by members of the Kansas Bankers Association, in town for an exchange of views as part of the ABA's Washington Visits program, but our real understanding of banking in Kansas comes from the 80 examiners assigned to one of three separate offices located around the state. They know their banks and they know the communities those banks operate in. So while the OCC is a nationwide regulator, with all of the resources that a federal agency can bring to bear upon its mission, we also have a very strong local presence throughout the country.

Our mission is not just to maintain the safety and soundness of those institutions, but to ensure fair access to financial services and fair treatment for the customers of national banks. We take both of those objectives very seriously.

With that commercial behind me, let me say that it's a pleasure to have this opportunity to speak to so many editors on a subject that could not be more important or more timely. I'm sure that nearly every one of you has written about the foreclosure crisis in Some form or fashion.

I can tell you that this has been a critical issue for those of us who work at the OCC. Back in 2005, only a few months after John Dugan took office as Comptroller, we realized that exotic mortgages that had become commonplace – instruments like option ARMS, where customers could decide for themselves how much to pay each month – were fraught with risk.

One of the first speeches the Comptroller made warned that millions of Americans could see their monthly mortgage payments increase dramatically when those loans reset, with potentially disastrous consequences if home price appreciation stopped. We pushed guidance through the interagency process in what seemed like record time, and followed up quickly with interagency guidance on subprime loans.

I have to tell you – 2005 seems like a long time ago. As you know, house values not only stopped rising, they dropped precipitously, making it impossible for many families to refinance out of mortgages that reset to monthly payments they could not afford. And as the economy deteriorated, many more families found themselves without the income to afford any mortgage.

As we began looking at the foreclosure problem in detail, one of our frustrations was a lack of quality data. Banks report more financial information than almost any other kind of public company. But the call reports they file didn't have the detail we needed to understand what was happening in individual mortgage markets, much less to individual borrowers.

And the sources of data on delinquencies that were often cited were usually surveys: better than nothing, but not rigorous, and not comprehensive.

That's why, in late 2007, we began collecting loan-level data using standard definitions for terms like "prime," "subprime," "payment plan," "modification" that had previously varied across the industry. We required the nine largest national bank mortgage servicers to submit data on each of the more than 23 million first-lien mortgages they hold or service.

Based on the 1.5 billion pieces of data produced, our first Mortgage Metrics Report in June 2008 offered a detailed look at the volume of payment plans and modifications, foreclosure trends, and the performance of mortgages overall, and by risk category.

Shortly after that first report, we began working with the Office of the Thrift Supervision to cover all national banks and federally regulated thrifts. Published in September 2008, the first joint report covered more than 60 percent of all mortgages serviced in the United States – about 35 million loans – with outstanding balances of more than $6.1 trillion. It showed mortgage delinquencies rising and servicers shifting from payment plans to loan modifications. The growth in loan modifications raised an important question—were they working?

For our December 2008 report, we expanded the data required from our servicers to help answer that question. The new data let us present, for the first time anywhere, information on the performance of loan modifications based on loan-level data covering a broad portion of the mortgage industry. Our findings were pretty controversial because the delinquency rates after modification were unexpectedly high. Six months after modification, 37 percent of modified loans were more than 60 days delinquent. More importantly, delinquencies continued to rise even after six months with no signs of leveling off.

In January 2009, we expanded our data collection again to gather information on affordability and sustainability of modifications. Not surprisingly, our April report showed loan modifications that reduced Principal and Interest payments worked better. Modifications that reduced payments by more than 10 percent had half the serious delinquencies after six months compared to modifications that left payments unchanged or higher.

The data also showed that nearly 27 percent of the 423,000 modifications implemented in 2008 left payments unchanged and almost 32 percent of them actually increased payments. While there are circumstances where this may make sense, these numbers seemed too high, and high re-default rates suggested these modifications were not sustainable. As a result, we directed our largest mortgage servicers to review their 2008 modifications to ensure that criteria applied to those and future loans result in modifications that are affordable and sustainable.

We continue to improve data reporting, and one new feature in our next report will be information on the various types of changes made by modifications—rate freeze or reduction, term extension, principal deferral or reduction, capitalization of delinquent fees and payments, or combination of these.

We'll continue to look at how changes in monthly payments affect modification performance, and we'll be able to show how specific vintages of modifications have performed over time – that is, how many modifications made in each quarter remain current, fell delinquent, or resulted in foreclosure. If you've used the report in the past, I think you will find the next edition very interesting. If you haven't, I encourage you to take a look when it comes out.

The evolution of the data in the Mortgage Metrics Report is testament to the changes in mortgage modification programs and financial policies that have been made in response to the spreading crisis. National banks have been working to prevent avoidable foreclosures throughout this downturn. Initially, standard practice would have been to rely on payment plans and modifications that capitalized missed payments and fees to get borrowers back on their feet. But as the mortgage problem emerged in 2007, beginning with subprime, banks had to change their approach to address broader and deeper financial problems.

Banks experimented: some offered rate freezes at low introductory rates, ranging from five years to the life of the loan. As home prices fell further and many homeowners found themselves owing more than their homes were worth, refinancing became impossible and customers needed more creative solutions to ensure sustainable payments. But securitization rules and second liens made modifications that reduced payments or principal very difficult to accomplish in many cases. Foreclosures soared, and began to spread from subprime to other categories of mortgages.

As the recession deepened, a variety of Federal programs began to take shape and some banks began pursuing larger scale efforts. Through the HopeNow Alliance, banks voluntarily offered more generous terms and expanded the volume of modifications, but foreclosures and delinquencies continued to rise. As the Obama Administration came into office, the largest servicers declared temporary moratoriums on foreclosures to allow time for a new national program to take shape. On March 4th, the Administration announced the Making Home Affordable program which all of the largest servicers embraced, and which is now in the early implementation stage. Adjustments to the FHA *Hope for Homeowners* program also offer homeowners another avenue to refinance into more sustainable mortgages.

But it is still too early to see the effects of these developments in the mortgage data. In fact, the mortgage data continues to show rising and spreading foreclosures despite the rapid evolution of programs and policies in response to the crisis.

Two factors not captured in the mortgage data are crucial to our understanding of the problem. First, declining home values are a major concern because the further individuals are under water, the less capacity or incentive they have to swim to the top. In May, the National

Association of Realtors reported that the median home price fell 14 percent from the previous year and prices fell in 134 of 152 regions. The length of time home values continue to fall or stagnate will affect the success of foreclosure prevention efforts.

The other area that isn't captured is how leveraged individual borrowers are – and, thus, how willing and able they are to bring their overall debt burden – both mortgage and consumer debt – under control.

This is where the good work of our friends at NeighborWorks and other counseling organizations comes in. When struggling homeowners are able to develop a debt management strategy based on both financial assistance and coaching, success rates rise: more people stay in their homes; fewer REOs bloat housing inventories and deflate prices; and fewer vacant homes dot our neighborhoods.

While counseling and affordable modifications will help prevent avoidable foreclosures, no one expects re-default rates or foreclosures to fall to zero. High unemployment is really just beginning to take its toll and delinquencies are rising among prime borrowers who make up two-thirds of the loans in our report.

In our most recent report, serious delinquencies among prime borrowers jumped 44 percent. And the Mortgage Bankers Association released data in late May that showed prime fixed-rate loans now represent the largest share of new foreclosures. Unfortunately, in this highly stressed economic environment, there is no way to <u>eliminate</u> foreclosures. No level of debt burden is manageable for homeowners who find themselves without an income. But equally, there is no <u>acceptable</u> level of re-defaults or foreclosures, and no <u>optimal</u> level of losses.

And the question of how much to change mortgage market rules or how much public money to spend to reduce those impacts is a very active subject of public policy debate.

What's not open to debate is that the economy will recover eventually; real estate values will come back; and real estate markets will revive. Those will be positive developments, but what lessons will we have learned to help avoid another bubble forming and abuses creeping back into the system.

Fortunately, the OCC and other regulators have already taken actions to prevent a recurrence of the practices that got us into this mess—the emergence of complex products and weak underwriting that left too many borrowers with financial obligations they could neither understand nor afford, and created risk beyond lenders' ability to manage. And with the adoption of the SAFE licensing regime, steps are being taken to broaden oversight of unregulated lenders.

For those policies to be truly effective, we need a national mortgage standard that applies to all lenders in every part of the country. That standard must balance the need for prudent underwriting with the equally important need for access to affordable credit. And to be truly effective, it must be enforced in a comparable manner across the country. It will do no good to have rigorous standards in place for commercial banks if mortgage brokers can once again sell high risk products with impunity.

With that, I'll stop. I look forward to the discussion and to your questions.