

**AN EXAMINATION OF THE HOMEOWNER  
AFFORDABILITY AND STABILITY PLAN**

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**HEARING**  
BEFORE THE  
**COMMITTEE ON**  
**BANKING, HOUSING, AND URBAN AFFAIRS**  
**UNITED STATES SENATE**  
**ONE HUNDRED ELEVENTH CONGRESS**  
FIRST SESSION

ON

AN EXAMINATION OF THE ADMINISTRATION'S HOMEOWNER AFFORD-  
ABILITY AND STABILITY PLAN AND HOW IT ADDRESSES THE ROOT  
CAUSE OF OUR ECONOMIC PROBLEMS

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FEBRUARY 26, 2009  
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## **AN EXAMINATION OF THE HOMEOWNER AFFORDABILITY AND STABILITY PLAN**

**THURSDAY, FEBRUARY 26, 2009**

U.S. SENATE,  
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,  
*Washington, DC.*

The Committee met at 10:11 a.m., in room SD-538, Dirksen Senate Office Building, Senator Christopher J. Dodd (Chairman of the Committee) presiding.

### **OPENING STATEMENT OF CHAIRMAN CHRISTOPHER J. DODD**

Chairman DODD. The Committee will come to order, and let me welcome our witness and congratulate you again, Secretary Donovan, for your confirmation and for your willingness to do this. Senator Schumer and others have raved about you and the tremendous work you have done in New York, and a lot of other folks I know have talked glowingly about your ability to get things done in that city on housing issues, and we are very excited about your stewardship.

We are fortunate to have on our Committee, of course, Mel Martinez who knows exactly what it is like to sit in that chair, having run that agency himself, and he has brought a wealth of knowledge and understanding of these issues to our Committee over the years he has served with us. So we are particularly delighted to have you.

What I am going to do is make some quick opening comments myself, Senator Shelby, and then ask my colleagues for any opening comments they would like to make as well. You are our only witness today. We do not have a second panel. And so when I can, I like to let members have a chance to express themselves, and I know this is particularly appealing to Senator Warner and Senator Bennet, I assume as well to Senator Hutchison and others who are at sort of the end of the line. So this way they get a chance to be heard a little bit before we actually get down to the question-and-answer period.

Senator Shelby will certainly appreciate this, Senator Martinez, Senator Reed, Senator Menendez. This is—and I hate to use a Yankee expression from a Yankee, Yogi Berra, but it is “deja-vu all over again,” in a sense. It was about this time 2 years ago that we had the beginning of a long series of hearings on foreclosures. Senator Shelby will tell you. I do not know how many times we met and talked and gathered with people to try and get people to move to workouts, to get something done on this problem. This was early 2007. And I think back on it now, and maybe we did not push hard

enough. I cannot imagine how much harder you could have pushed. And nothing happened. Nothing happened. And we are in large part where we are today because of that—not that that was the only reason. Obviously, this problem began long before 2007. But had we and had the administration, the previous administration—and I say this respectfully—moved on that issue at a time, we could have mitigated this problem substantially.

As long as I live, I will remember Bob Menendez's comments that day, our first hearing. I think you were the first person to call it a "tsunami of foreclosures" that would happen. Today you hear that expression over and over again because we are in the middle of it. But in 2007, in January and February, you were considered being hyperbolic if you used language like that. You were an alarmist. It was just politics to talk like that. And, of course, we have now learned painfully that, in fact, if they were guilty of anything when they used those words, it is that they were underestimating the problem when we gathered here to talk about it.

So I will share some opening comments and thoughts and then turn to my colleagues, and then obviously, Secretary Donovan, we are very anxious and, I must say, enthused a bit about what we have heard over the last few days in a new administration and a willingness to make some—and the President's comments on the subject matter.

Today the Committee is going to meet to discuss, obviously, the administration's Homeowner Affordability and Stability Plan outlined 2 weeks ago to address the root cause of our economic crisis: the foreclosure crisis. This plan represents in my view a sharp change in direction from the previous administration's approach. It draws upon funds expressly authorized by this Committee to prevent foreclosures in the Troubled Asset Relief Program, which was created as part of the Emergency Economic Stabilization Act that was passed in October. And it could not come at a more critical time. At the end of the day today, another 10,000 families in our country will have received a foreclosure notice.

In my State of Connecticut—and I know my colleagues, each of them here, some more dramatically than others, can point to their own statistics and numbers. But we can see in my State, the small State of Connecticut, nearly 60,000 foreclosures in the next 4 years. In all across our Nation, as many as 8 million families could lose their homes.

Over the course of some 80 hearings and meetings in the 110th Congress, this Committee has asked a very simple question, the same question that we get asked every time we go back to our respective States: How in the world could this have been allowed to happen?

Certainly, as this Committee has uncovered, the problem's origins lie in the scourge of the unchecked, abusive predatory lending practices. A little over 2 years ago, on February 7, 2007, this Committee heard from Delores King, who sat right at this table—that is exactly where she was sitting, right there to your right. She had owned her home in Chicago for 36 years and was in danger of losing it due to an exotic mortgage she was duped into signing by a telemarketing mortgage broker.

That day we also heard from a North Carolinian, Amy Womble, whose broker intentionally misrepresented her income in order to secure a loan that she could not afford. A mother with two children, she wanted to pay off the debts left by her husband after his untimely death. She was trying to act responsibly, and she ended up facing foreclosure.

Last year, we met Donna Pearce, a grandmother from Bridgeport, Connecticut, where there are now 5,000 families with subprime mortgages in danger of foreclosure. Donna was offered assurances by her lender that she would be able to refinance in 6 months, but he failed to mention the thousands of dollars in penalties that refinancing would cost her in the process.

Mr. Secretary, I defy anyone to suggest that these cases were somehow the exception, that these were aberrational. The vast majority of people losing their homes today are decent, hard-working, good Americans—grandparents on fixed incomes, working families who have lost a job or faced a health care crisis, many of whom were taken advantage of.

To suggest, as one or several commentators have, that this problem was created, and I quote, by “deadbeats with an extra bathroom” is not only insulting and infuriating, but to the families who are suffering right now, it is tremendously damaging. It effectively lets unscrupulous brokers, lenders, credit rating agencies, and investment banks off the hook. It ignores the toll that these foreclosures are taking on home values, an 18-percent drop nationally, and far more severe in certain areas of the country. And it makes our task up here, getting credit flowing again to families and businesses, that much more difficult.

As one mortgage lender told this Committee, this crisis was the consequence of “mortgage malpractice”—his words when he appeared before this Committee. We do not blame the patient when a doctor fails to tell them they might not survive the surgery. Why should we blame the homeowners in many ways?

So, Mr. Secretary, I appreciate the speed with which the administration has acted to address this issue. The plan, as I think most of us know, has three crucial elements:

First, it offers 4 to 5 million homeowners who are current on their loans the opportunity to refinance into lower rates. This feature will open up the mortgage market to homeowners who have been locked out and unable to take advantage of the new lower mortgage rates currently available because their home values have dropped. This provision is aimed squarely at working and middle-class families.

Second, the plan finally creates a program to modify the loans touched by troubled borrowers. This will help 3 to 4 million families keep their homes and finally start to put a bottom on the housing market.

And, finally, the plan calls for bankruptcy reform, allowing bankruptcy judges to lower mortgages on first homes, subject to carefully crafted repayment plans. Clearly, the industry and the previous administration were late, as I have said over and over again, in acknowledging the problem and very timid in their responses. With this plan that I have just mentioned, and ones we will talk

about this morning, issued only a few weeks after taking office, the contrast could not be sharper.

Over and over, as we have begun to grapple with the mountain of problems facing our country from skyrocketing health care costs to energy, you have heard members on both sides of the aisle say the same thing over and over and over again: "We need to fix housing first." And I could not agree more. And that is not just the Chairman of the Banking Committee talking. That is also the Republican Leader from Kentucky, Senator Mitch McConnell; that is our colleague Senator Kyl of Arizona; Senator Enzi of Wyoming; Senator Ensign of Nevada; Senator Coburn of Oklahoma. All of these individuals have said the same thing: "Fix housing first." So you are not talking about some great political divide up here when it comes to this issue. We may debate about which nuanced approach works better than the other, but we are all ears and want to help in getting to the bottom of this.

And so John McCain and Barack Obama, again, during the Presidential campaign echoed the same theme: "Fix housing first." It is a bipartisan notion, as bipartisan a notion as I can say than anything I have heard in the Congress in the last number of years.

So, with that, let me turn to Senator Shelby, and then my colleagues, and then we will get to your comments and responses to questions. We thank you again for being with us. Senator Shelby.

#### **STATEMENT OF SENATOR RICHARD C. SHELBY**

Senator SHELBY. Thank you, Senator Dodd.

A little more than a week ago, President Obama proposed his Homeowner Affordability and Stability Plan. The proposal aims to stabilize our crumbling housing market and help struggling homeowners. Unfortunately, I believe the proposal is long on good intentions and short on providing a credible solution for our ailing housing market.

For example, the proposed Fannie Mae and Freddie Mac refinancing program appears to focus its efforts on those households least in need of assistance. The program would be open to households that are neither behind on their mortgages nor struggling to make their payments. Consequentially, the program would waste, I believe, resources on lowering the interest rate for borrowers who presently can and are paying their mortgages.

Mr. Secretary, I believe our immediate attention should be to help those most in need who can be helped and are willing to help themselves.

One part of the President's proposal, the Homeownership Stability Initiative, is supposed to help the most troubled homeowners. I believe, however, that it does so at considerable cost to the taxpayer and mainly serves as a further bailout to the very banks that helped us get into our current condition. The initiative, for example, will pay servicers \$1,000 for each mortgage they modify and servicers and mortgage holders \$500 and \$1,500, respectively, if they modify a loan before a borrower falls behind. Mortgage holders would also get partial insurance to cover losses on a modified mortgage if housing prices decline further. Adding up all these payments, lenders could receive at least \$4,000 per loan modification.



This would be equal to about almost 5 months of principal and interest on the typical mortgage.

All of this, of course, would be paid for by the taxpayer. The proposal would potentially pay billions to lenders who have already received tens of billions under the TARP and other recovery programs.

For instance, with its acquisition of Countrywide Bank, Bank of America now services almost 13 million loans. If only a fifth of those loans, Mr. Secretary, receive assistance under the President's proposal, Bank of America would receive an additional \$10 billion in taxpayer assistance on top of the already over \$45 billion that we know of in taxpayer funds it has already received.

Mr. Secretary, before the American public commits another \$10 billion or more to Bank of America, for example, to perform the same services it is already paid to do, we need to consider whether this is really the best way to help struggling homeowners.

We should also consider whether this proposal is fair. If implemented, the American people may have to pay billions of dollars to banks and servicers simply to do the job they are supposed to do.

In addition to the lender and servicer payments, the President's proposal also pays borrowers up to \$5,000 through a reduction in their loan balance. That sounds good. In other words, they get paid to make their payments.

I am confident that the vast majority of American homeowners would welcome a \$5,000 subsidy simply for doing what they are supposed to do—make their mortgage payments.

I am equally confident that the vast majority of Americans believe that it is not their responsibility to pay for that subsidy to someone else.

I spent last week traveling around my State of Alabama, and the public reaction to your plan was not good. At a town hall meeting I had in Boaz, Alabama, I spoke with a gentleman named Darren Latta, who, with his wife, Carol, is struggling to keep their dry-cleaning business going. Mr. Latta told me and everybody else there that, despite his struggles, he would never ask anyone to pay his mortgage. In addition, he said he resented Congress—us—taking his hard-earned money to make somebody else's house payment.

Mr. Secretary, I believe he was not alone among my constituents or the American people. We all want to help struggling homeowners. The question is how. It is crucial, however, that we do so in a manner that is carefully targeted and based on proven solutions, and especially if we are going to spend billions of dollars more of taxpayers' money that has to be borrowed.

As President Obama said Tuesday night, and I quote, "With a plan of this scale comes an enormous responsibility to get it right." He is absolutely right there. The American people should be able to have confidence that their tax dollars are being used effectively, and I believe they do not think so here. To build that confidence, the administration should be able to provide a reasonable estimate of how many foreclosures it believes its \$75 billion will prevent, as well as its impact on housing prices. The administration, through you, should also be able to demonstrate that its proposal is based on verifiable data rather than ad hoc policy choices.

Until we begin, Mr. Secretary, developing solutions based on facts and analysis, I do not believe we can hope to rebuild either our devastated housing market or our confidence in our ailing economy.

Thank you, Mr. Chairman.

Chairman DODD. Thank you very, very much, and I will now ask my colleagues—Senator Menendez, any opening comments?

Senator MENENDEZ. Thank you, Mr. Chairman. I want to thank you for holding what is an incredibly important hearing. And, Mr. Secretary, while I have several questions, I certainly want to commend you and the administration for taking the housing crisis seriously and developing a proposal that I think lays the foundation for some real relief to American families.

As a member of this Committee, I feel as if we have been listening to a fire alarm wail for years as millions of Americans watch their dreams of homeownership go up in smoke. We shouted the statistics as long as we could. We held meetings to develop legislation, but for years, the previous administration just covered its ears. And now, finally, we have one that is willing to call in the fire department, so to speak, and the question is how big a fire pumper do we need and how do we turn on the water.

At a hearing in March of 2007 that the Chairman mentioned, I said then that we were going to have a tsunami of foreclosures, and the administration basically said I was an alarmist. Well, at that same hearing, I started to shed some real light on the crisis and shared a story of a woman from my home State of New Jersey who was given an adjustable-rate mortgage she could not afford and the promise of a new mortgage term in 1 year. It did not take long for her to fall behind on her payments and a foreclosure notice to arrive. That was March of 2007.

Over 20 months later, these stories are flooding into my office as fast as they ever have. There are 6,600 foreclosures starting every week in this country, one every 13 seconds. In New Jersey, since the beginning of this year, there have been over 9,000 new foreclosures, and we expect there to be over 60,000 new foreclosures before the year ends.

Just recently, my office received a phone call—I know that Senator Shelby talked about his constituent in that drycleaning business, and I appreciate what he thought. But I will tell you a different story. My office had a New Jersey resident who is a sergeant in the United States Army Reserves. He recently returned from a long tour of duty in Iraq. During deployment, he fell behind on his mortgage. When he came back, he took on not only one but two jobs. But in this tough economy, his income has greatly decreased, and he is having trouble making ends meet. He has three kids who are depending on him, and my office is working with him. We are going to his servicer to try to work out an arrangement, but nothing has worked out so far.

Families like this army sergeant are all over America waiting for their lender or servicer to strike an agreement. And if that does not happen, they are waiting for a padlock on their doors. And to top it off, he thinks it is unfair—and so do I—that lenders can take taxpayer money but do not have to help homeowners. That was not

the intention in our original bill. In fact, it was quite the opposite. And we need to fix that as soon as possible.

So the relief you are talking about is not a moment too soon, and as much as I really commend you for these commitments on paper, none of us can be satisfied until we see them put into action. I look forward to hearing the details of the administration's plan. I think the whole country is waiting to find out exactly how American families are going to receive assistance and how fast, because in the end, this is about all of us. It is about declining values of the home next door that may not be in foreclosure. It is about declining values in neighborhoods. That has real consequences. As a former mayor, it has real consequences for a community. You either have to cut delivery of services because your rateable base is going down, or you have got to raise taxes. Both options are pretty horrid in this economy. And at the end of the day, it is really about all of us as Americans because our collective economy is—this is one of its major drivers. And when it is not driving, it is falling. And when it is falling, we all suffer.

So at the end of the day, I look forward to see what the administration's full plan is and how fast we will get there.

Thank you, Mr. Chairman.

Chairman DODD. Thank you, Senator, very much.

Former Secretary of Housing and Urban Development.

#### **STATEMENT OF SENATOR MEL MARTINEZ**

Senator MARTINEZ. Thank you, Mr. Chairman, very much. I want to welcome Secretary Donovan and continue to wish you the very best in your job, and I appreciate the willingness to take this difficult leadership position at this point in history.

Let me say, before I comment on the current plan, that it is important that we not totally forget history. The fact of the matter is that while to some it may have seemed like the prior administration was completely ignoring the housing problem, I think it would come as a surprise to those that work for you at FHA who are working on Hope for Homeowners, which was a well-intended program, has not had the success we hoped it would have, but if we simply ignore the fact that sincere efforts were made by your predecessors to deal with this problem, we will not learn the lessons of why some of those programs did not work as successfully as everyone had hoped at the time that they would work.

So I think it is terribly unfair to simply say the problem was ignored, people did not care about poor people losing their homes. I just do not think that is accurate or the case. So I think as you look forward to implementation of this program, looking to Hope for Homeowners and some of the issues that arose in that program, that created problems in participation by private servicers, are some of the very issues that I think we need to deal with in the plan that is being currently suggested.

I was pleased with the President's initiative last week. I think it is very important that we begin to deal with this very, very serious problem that is afflicting so many Americans. And I believe we can help deserving families stay in their homes by curbing unnecessary foreclosures and, in doing so, help to preserve communities and put our housing market on a pathway to recovery.

The President has laid out the groundwork for the plan which includes three main components: a refinancing option for qualified homeowners whose loans are currently owned or guaranteed by Fannie Mae and Freddie Mac; a \$75 billion interagency loan modification strategy; and an additional \$200 billion in funding commitments to the housing GSEs.

I applaud the administration for taking aggressive steps to tackle this crisis, and I also want to be sure that as we go forward, we get some answers to some of the details. I question whether we will be more effective than the current programs in preserving homeownership, and that is at the very core of why I say it is not just enough to say the prior administration tried nothing. Some things were tried—not successfully—and we need to learn those lessons rather than just simply ignore that the effort was made.

One of the major stumbling blocks to the success of the current preservation programs has been the lack of participation by servicers of privately securitized mortgages. These mortgages, which were originated without a guarantee from the Government-sponsored enterprises, account for more than one-half of the foreclosure starts, despite the fact that they only are about 15 percent of all outstanding mortgages. Servicers of these securitized mortgages make a critical decision of what to do when a mortgage becomes delinquent by choosing to pursue foreclosure or a modification of the mortgage. Existing research suggests that these servicers opt for foreclosure much more often than private lenders that service their own mortgages.

While Fannie Mae and Freddie Mac and FHA and private lenders are actively and aggressively pursuing mortgage modifications, servicers of securities loans are still lagging. Two primary factors are driving mortgage servicers' reluctance to modify loans when modifications would make economic sense: one is that servicers are not compensated for loan modifications; and second are the legal constraints and the potential for litigation that dissuade many servicers from pursuing modification.

I was glad to see that President Obama's plan addresses one part of this problem by providing monetary compensation to the servicers, but it neglects to address the legal constraints hindering the services' participation. Without this critical second element, I do not believe the private marketplace will be any more willing to pursue modification over foreclosures than they have in the past.

The Chairman and I cosponsored an amendment to the stimulus bill which covered both of these items, and I commend to you a look at that amendment, which passed but ultimately was not part of the final bill, which I think would have dealt with both aspects of the problem, not just the compensation but also the legal safe harbor provided to the servicers.

I have concerns about the Federal Government's becoming a guarantor of loan modifications enacted under this program. Although the housing market may be stabilizing in some areas, there are still places around the country, including cities in Florida, where home prices are expected to decline further. According to the Obama administration's own projections, 40 percent of loan modifications through this program are expected to redefault. We need to ensure that the Federal Government is using taxpayer dollars

wisely and that we are working to really solve problems, not just delay them.

One major factor for accelerating defaults is that consumers are saddled with debt beyond their homes, including credit card debt, auto loans, medical bills. You know, the fact that continued unemployment is a part of our daily landscape is something that cannot be ignored as an added element of what is happening here.

In any event, I want to thank you for the job you have undertaken. I want to thank you for the initiative that I hope we can see all of the details of, and I want to work with you because this is a plan that America needs to succeed. We need for it work.

So I hope we will continue to develop a plan in consultation with the Congress that can not only begin to stave off more foreclosures and declining values, but also begin to really see a re-emergence of the housing sector, which is a vital part of an economic recovery.

Thank you, Secretary, and I look forward to hearing your testimony.

Chairman DODD. I thank you very much, Senator. And I am glad the Senator mentioned it; I regret I did not do so myself, but I want to thank him for his amendment that we worked on together during the stimulus vote. And I tried—I would tell my colleague, when I got word at the last hour of that negotiation, I guess in conference, what was going to happen, I called, and I should say to the credit of the leadership, they apologized. They raced back in to try and salvage the language. There was no cost to it. In fact, quite the opposite. There was quite a benefit to it. And they were not able to do so, and they regret that. So it was unfortunate that it got dropped because it really would do exactly what the Senator has just described and played a very important role. We need to find a way to incorporate that into something we do here pretty quickly. So I thank the Senator for it.

Senator Brown—and there is a vote that started. I am going to go vote and come right back, and we will just keep the hearing going so we do not have any delay.

#### **STATEMENT OF SENATOR SHERROD BROWN**

Senator BROWN. Thank you, Mr. Chairman, for your leadership, and, Mr. Secretary, thank you for your public service in New York and thank you for what you are doing today. You have inherited quite a mess—a mess born of get-rich schemes for the very wealthy and the monetary middlemen who conceived of and carried out these schemes, mortgage schemes that painted unaffordable homes as easily within rich, unregulated credit markets fueled by false promises and sustained by false hopes, and Government regulators who slept through all of it. Not only did the perpetrators of these schemes paralyze American families and the American economy, they tainted the American dream.

We all hear disillusionment and despair and unbridled outrage in the voices of Americans. I hear them in the voices of Ohioans as they watch their homes slip away, their property values plummet, their communities crumble. Their gut-level feeling is that all of this is not only unjust but perhaps criminal.

We owe it to the Americans we serve to respond quickly and forcefully to the housing crisis. We owe it to them to stop

prioritizing the demands of corporate moguls over the well-being of everyday Americans.

We all need, of course, to worry about the erosion of home values. Too many working families who pay their mortgages on time are facing lower home values when their neighbors' homes are foreclosed. As we know, each foreclosed home reduces nearby property values by several percent, and it does not stop at home values. Police, fire, schools, and other programs that are funded based on property values are also facing massive shortfalls.

Other building blocks of the American dream are also under siege: a car in every driveway, a stable income upon retirement, a college education for every child. A quick Internet search of just one Web site yields in the community of Pickerington, a suburb outside of Columbus, a generally affluent suburb, yields 109 foreclosures for sale in Pickerington. Pickerington has an estimated population of 16,000 people.

Profiteers exploited the American dream, peddling subprime loans in the quest for more bonuses, more private jets, more European vacations. No one cared how much they spent. They always had the golden parachute to safely land when the money dried up. That is the problem that you are left with, that we are left with, cleaning up after a long, loud party.

While I know the nuts and bolts of the administration's Homeowner Affordability and Stability Plan are to be released next week, the broad outline looks promising. I understand that the plan the administration is proposing will help at least 9 million struggling families hold onto their homes, which is necessary if we care whether people get back on their feet or fall into poverty. It is also a smart move to help neighborhoods thrive rather than fragment and help communities on shaky ground to get on stabler ground.

I am heartened that after 8 long years we finally have an administration that remembers that it reports to Main Street, not to Wall Street.

Thank you for your service. Thank you, Mr. Chairman.  
 Senator REED [presiding]. Thank you, Senator Brown.

#### **STATEMENT OF SENATOR JACK REED**

Senator REED. Secretary Donovan, welcome. We are all delighted that you are in the leadership of the Department of Housing and Urban Development. You have extensive experience there. In addition to that, you have been doing a remarkable job in New York City and we thank you for that, also.

I share the sentiments of so many of my colleagues that action delayed over the last several months has worsened this crisis, and so the action plan that you proposed along with the President, I think, is vitally important at this moment. I think also the ability to react to the ups and downs of the market is going to be critical. You are going forward with a good plan, but I think you are also going to prepare to modify, adapt, and respond to changes in the situation.

One of the fundamental aspects, I think, of our recovery is stabilizing housing prices and then beginning to get people to go back to work. And once the American families feel that their housing

prices are stable and hopefully begin to appreciate once they are confident of their jobs, then the rest will be, I think, much—not easy, but the path ahead will be surer and more confident for families across the country.

One thing I want to particularly thank you for is I heard today that within the President's proposal there will be a \$1 billion fund to launch the Affordable Housing Trust Fund. That is in the budget. I know Senator Shelby and I worked on that. It was a key element of the legislation a year ago, last August, and in this time when people are losing their homes, particularly low-income Americans, expanding affordable housing opportunities is more critical.

And in addition, too, I think it sends the signal that our housing policy can't rest simply on home ownership, that there are scores of American families whose best and wisest course of action is to be in affordable rental housing because of their family situation and because of their economic situation. I think we were too, in a sense, beguiled by this notion that we could put everyone in a home, and I think we found out that some people, despite their best efforts, as it turns out today, couldn't afford it or were given loans that were just not commensurate with their ability to pay and to sustain the home ownership.

So for all of these reasons, I want to commend you. I would note, I believe, Senator Shelby, you have already had your opening comments. We are waiting for the return of Senator Dodd. Senator Shelby, should we go in recess for a moment? Do you want to start?

Senator SHELBY. Go ahead.

Senator REED. See, I am relying on the wisdom and the counsel of the former Chairman, so that shows at least—

Senator SHELBY. You have got the gavel.

Senator REED. I have got the gavel, but he has got the wisdom and the experience.

Mr. Secretary, would you begin your statement, please?

**STATEMENT OF SHAUN DONOVAN, SECRETARY, DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT**

Secretary DONOVAN. Thank you, Mr. Chairman, Senator Shelby, distinguished members of the committee. Thank you for the opportunity to appear here before you today.

Homeowners in communities throughout the country have been devastated by the economic crisis. Many responsible families making their monthly payments have experienced falling home values that disqualify them from opportunities to refinance with today's low interest rates, and millions of American workers have been laid off or forced to accept less work and are grasping at every resource possible to make their mortgage payments.

In the absence of action, over six million families could face foreclosure in the next few years, with millions more struggling to stay above water. In the absence of action, we would have seen an intensifying spiral of more lenders foreclosing, pushing nearby home prices even lower and putting more families underwater. In fact, when a family loses their home to foreclosure, nearby homes drop in value by as much as 9 percent, causing harm to every homeowner, even those who make every payment, when foreclosures in their communities increase.

On February 18, President Obama announced the Homeowner Affordability and Stability Plan, a plan to help make available to as many as seven to nine million homeowners who are fighting hard to make their payments and stay in their homes. The plan will not provide money to speculators. It will target support to the working homeowners who have made every possible effort to stay current on their mortgage payments.

The Homeowner Affordability and Stability Plan is part of the President's comprehensive strategy to get the economy moving in the right direction. Just as the American Recovery and Reinvestment Act works to save or create several million new jobs and the Financial Stability Plan works to get credit flowing, the Homeowner Affordability and Stability Plan will support a recovery in the housing market and ensure that these workers can continue paying off their mortgages. The plan not only helps the responsible homeowners at risk of losing their homes, but prevents neighborhoods and communities from decay, as defaults and foreclosures fuel falling home values, local business collapses, and further job loss.

There are three parts to the plan. First, encourage home ownership by helping keep mortgage rates low. Second, support for refinancing of up to four to five million responsible homeowners to make their mortgages more affordable. And third, to launch a \$75 billion Homeowner Stability Initiative to reach up to three to four million at-risk homeowners.

To help keep mortgage rates low and promote stability and liquidity in the marketplace, the Treasury Department will continue to purchase Fannie Mae and Freddie Mac mortgage-backed securities. In addition, the Treasury Department will increase its funding commitment to Fannie Mae and Freddie Mac to ensure the strength and security of the mortgage market and to help maintain mortgage affordability. This backing will bolster confidence in the mortgage market, allowing interest rates to remain at generational lows and to continue to provide mortgage affordability for responsible homeowners.

As noted, mortgage rates are currently at historic low levels. But under current rules, only families with conforming loans owned or guaranteed by Fannie Mae or Freddie Mac who owe less than 80 percent of the value of their homes are eligible for refinancing to these low interest rates. Unfortunately, given the recent decline in home prices, millions of responsible homeowners who made downpayments and timely mortgage payments are unable to access these lower rates.

The President's plan will help as many as four to five million of these homeowners refinance to lower interest rates through Fannie Mae and Freddie Mac by opening eligibility to borrowers who owe on their mortgage 80 to 105 percent of their current value of their home.

Finally, the President has announced an initiative to reach millions of responsible homeowners who are struggling to afford their mortgage payments. In the current economy, millions of hard-working families have seen their mortgage payments rise to 40 or even 50 percent of their monthly income, particularly if they received subprime or exotic loans with exploding terms and hidden fees. The



Homeowner Stability Initiative operates through a partnership of lenders, servicers, borrowers, and the government to help responsible borrowers stay in their homes, providing families with security and neighborhoods with stability.

Based on estimates of the effects of foreclosures on the value of nearby homes, the Homeowner Stability Initiative could protect the owner of an average-valued home in the U.S. from as much as a \$6,000 decline in home prices. Homeowners with high mortgage debt compared to income may be eligible for a loan modification as long as their home mortgage does not exceed the GSE conforming loan limits. Further, the increase in GSE conforming loan limits, up to \$729,750 in some high-cost areas, as enacted in the American Recovery and Reinvestment Act, will allow more borrowers to qualify.

Significantly, this program will not require homeowners to be delinquent in their payments to qualify for eligibility. Loan modifications are more likely to succeed if they are made before a homeowner becomes delinquent. Thus, the plan will include households at risk of imminent default despite having not yet missed a mortgage payment.

Borrowers with large non-housing debts can qualify, but only if they agree to enter HUD-certified counseling. Specifically, homeowners with total back-end debt, which includes not only housing debt, but other debt including car loans and credit card debt, equal to 55 percent or more of their income will be required to agree to enter a counseling program as a condition for a modification.

The Homeowner Stability Initiative could reach up to three to four million at-risk borrowers in all segments of the mortgage market, reducing foreclosures and helping to avoid further downward pressure on overall home prices. The program has several key components.

First, the government will partner with lenders to reduce the homeowner's monthly payment to an affordable level. The lender is solely responsible for interest rate reductions and other changes necessary to lower the borrower's monthly payment to 38 percent of his or her income. From that point, the government will match, dollar for dollar, any additional reductions the lender makes to lower that ratio to 31 percent. These adjustments could mean a monthly mortgage payment lowered by more than \$400 for a borrower with a \$220,000 mortgage. The lower interest rate arrived at must be kept in place for 5 years, at which point it can gradually be increased to the conforming loan rate at the time of the modification. Lenders will also have an option of decreasing monthly payments by reducing the principal owed on the mortgage with the government sharing those costs.

Second, servicers will receive \$1,000 for each eligible modification meeting initiative guidelines. They will also receive fees to reward them for continued success, awarded monthly as long as the borrower stays current on the loan, up to \$1,000 each year for 3 years.

Third, to encourage borrowers to stay current, the initiative will provide a monthly principal balance reduction payment. As long as a borrower stays current on his or her loan, he or she can get up to \$1,000 each year for 5 years.

Fourth, because loan modifications are more likely to be successful if they are made before a borrower misses a payment, to keep lenders focused on reaching borrowers who are trying to stay current on their mortgages, an incentive payment of \$500 will be paid to servicers and an incentive payment of \$1,500 will be paid to mortgage holders if they modify at-risk loans before the borrower misses a payment.

Finally, to encourage lenders to modify more mortgages and enable more families to keep their homes, the administration, together with the FDIC, has developed an innovative home price decline reserve payment. The fund, which may be as large as \$10 billion, will provide holders of mortgages modified under the program with an additional payment in the event that the home price declines and therefore the risk of losses of cases of default is higher than expected.

As mentioned earlier, the Homeowner Affordability and Stability Plan is not a self-contained initiative but is intended to work in conjunction with other efforts, such as the American Recovery and Reinvestment Act and the Financial Stability Plan to provide a comprehensive and multifaceted response to the current economic troubles.

As part of the American Recovery and Reinvestment Act signed by the President, the Department of Housing and Urban Development will award \$2 billion in competitive Neighborhood Stabilization Program Grants for innovative programs that mitigate the impact of foreclosures by supporting strategies to address the problem of vacant foreclosed properties.

Additionally, the Act includes \$1.5 billion to provide assistance to renters facing displacement, reducing homelessness and avoiding entry into shelters. HUD allocated that \$1.5 billion of homelessness prevention funding to recipients yesterday, just 1 week after the bill was signed, as part of our successful allocation of three-quarters of Recovery Act funds for HUD programs yesterday.

In addition to the already mentioned efforts, the President's overall Economic Recovery Plan will seek careful changes to personal bankruptcy provisions. The administration will work with Congress to ensure that legislation works well in conjunction with our voluntary modification approach.

Finally, the Hope for Homeowners Program offers one avenue for struggling borrowers to refinance their mortgages. In order to ensure that more homeowners participate, we support changes to the program that will reduce fees paid by borrowers, increased flexibility for lenders to modify troubled loans, permit borrowers with higher debt loads to qualify, and allow payments to servicers of the existing loans.

Thank you, and I look forward to your questions.

Senator REED. Well, thank you very much, Mr. Secretary.

I note we have been joined by Senator Johanns. We have been asking if you have opening statements—very good. In that case, I will begin a quick round of questioning. Let me just do this, because we have to vote. I will recognize Senator Johanns for questions and by the time you finish, Senator Dodd will be here and all will be well. Thank you, Senator Johanns.

Senator JOHANNNS. Mr. Secretary, welcome.

Secretary DONOVAN. Thank you.

Senator JOHANNNS. It is unusual that we get this kind of opportunity, but I appreciate the opportunity.

Let me, if I might, offer a thought, and then I would like your reaction to a couple of questions. The thought is that one of the challenges we are finding in the marketplace in terms of lending at the moment is the market is looking for stability, predictability. They are looking for confidence in the ability of that borrower to repay, et cetera. So I want to turn to just the last comment you made about the bankruptcy provisions. I think what you are referring to is cramdown, although you did not use that word.

Talk to me about how that fits into what you are doing here. How would a cramdown approach fit with what you are proposing here today?

Secretary DONOVAN. That is a very important question, Senator, and let me first start by saying, as the President made clear in his announcement of the plan last week, that this is an issue of fairness to him and to the administration, whether it is a second home or any other kind of debt, that currently can be modified in a bankruptcy. We have been able to find ways to ensure that markets are stable for those types of loans, as well. But we also agree that particularly in this time of difficulty in the market, we don't want to disturb the markets any further. And so there are a couple provisions that we think are important in terms of carefully tailoring this legislation.

One of those is to make it available only for loans that are already in existence. In other words, new mortgage loans would not have this provision apply to them, and—

Senator JOHANNNS. If I might just interrupt, you lost me there. Make what available?

Secretary DONOVAN. The option to modify a loan in a bankruptcy proceeding—

Senator JOHANNNS. The cramdown—

Secretary DONOVAN. —would apply only to loans that have already been originated.

Senator JOHANNNS. OK.

Secretary DONOVAN. In other words, the idea is not to have an impact on lenders that are out making mortgage loans today and to potentially impact interest rates as a result of that.

Senator JOHANNNS. OK. So let me stop you there, just so we are on the same wavelength.

Secretary DONOVAN. Yes.

Senator JOHANNNS. You have got, I don't know how many dollars' worth of loans out there today, billions and billions and billions. They would all be subjected to this new bankruptcy authority is what you are saying. Now, if you end up with a loan the day after, you don't benefit from that new bankruptcy authority. Are we together so far?

Secretary DONOVAN. Right. The idea is that prospectively, for new loans that will be originated, this provision would not apply, and therefore there is no risk of it affecting originations going forward.

Senator JOHANNNS. OK. Now let me take another step with you, because I think I know where you are going. Let us say that we

are going to continue to ask the taxpayer to bail these things out, because I think that is kind of what is going on here, and they are going to in some form or fashion, whatever the idea is, they are going to in some form or fashion be the owner of these bad loans or a certain portion of them. How can we assure the taxpayer that with this new bankruptcy authority, as you referred to it—I call it cramdown, because it is—I am a lawyer and that is what we call it—how can we assure them that there will be stability, because all of a sudden we have forced into that basket of debt that the taxpayer is going to own a big uncertainty?

We have got one judge somewhere who has been empowered to say, that loan isn't worth what you think it is because I am going to force something different. Isn't that the very uncertainty that we are trying to avoid in the marketplace?

Secretary DONOVAN. Again, I think with careful tailoring of this legislation, there are a number of ways to ensure that it doesn't introduce that kind of instability. One of them is this is prospective. Another is to make sure that every effort is being made to modify loans, keep people in their homes, before they ever get to bankruptcy. So we would support a provision that would—if a lender has made a good faith effort to use this modification plan, that that would exempt them from the bankruptcy.

So in other words, we want to be very clear. This is not a solution to the issues that homeowners have struggling with their payments as a primary response. It is only a last case resort. We want to make sure that we are getting to this problem of modifications, and that is why we have our proposal, as early on as possible to take away exactly the instability that you are talking about, to ensure that mortgages are affordable and that people can make their payments, and that will help markets to stabilize, because it is the foreclosures today that are happening and that instability that is driving so much of the problems in our mortgage market.

Forty-five percent of all home sales in December were distressed sales, and so helping to make mortgages more affordable before you ever get to bankruptcy is incredibly important. So there are a number of ways to do that built into the bankruptcy provisions, we think.

Senator JOHANNIS. I am out of time and the Chairman has arrived, so let me just wrap up with this. I hear what you are trying to say, and I think you are trying to assure me that, Mike, it isn't going to be that bad. But if the only option is for these people who are in default or have missed payments, if the only option is bankruptcy, they will probably take that option. I think you will see bankruptcies skyrocketing.

And then, like I said, because of the uncertainty that you have now introduced into the valuation of that mortgage debt, what is it worth, if a judge holds that power, I think as this trails out, the people who are going to pick up the tab for that is the taxpayer out there, because I think in the end, they are going to own—it looks to me like they are going to own a lot of those bad debts.

Secretary DONOVAN. If I could, Senator, there is one other provision that I haven't mentioned that I think is important, as well. There has been discussion about a limitation of any reduction of the debt in bankruptcy to—the maximum it could be reduced is to

the market value of that home. And I think also that is quite important in terms of taking away some of the uncertainty that you are talking about.

So again, I think there are a number of ways to minimize that uncertainty, and we clearly agree that bankruptcy is not the way to work out these mortgages and we have taken action. That is exactly what the modification plan that we have introduced is, is to make sure that we avoid the problem of foreclosure and bankruptcy in the first place and help as many families as possible, responsible homeowners, stay in their homes with the modification.

Senator JOHANNIS. Mr. Chairman, thank you.

Chairman DODD [presiding]. Thank you, Senator, very much.

Senator Merkley, I know you didn't get a chance to make an opening comment at all, so why don't you take the floor.

Senator MERKLEY. Well, thank you very much, Mr. Chair, and thank you for your testimony and I will keep it very simple. This is an incredibly important plan for millions of American homeowners, certainly important to the financial foundations for our families, but also for the health of our economy, and I look forward to hearing the exchanges of questions and thoughts and working with the administration to try to make sure that this program works, both for our families and for our economy. Thank you.

Chairman DODD. I want to say, Mr. Secretary, that Senator Merkley, as we talked a little bit yesterday, as well, privately, has, as all of us do, a very deep and abiding interest in this subject matter and spent a lot of time on his own, in fact, meeting with people outside of Washington to talk about this issue, as well. He has some very strong ideas I am sure you will listen to.

Let me just open with a couple of things. One is, I don't need to tell you, Mr. Secretary, the level of frustration of the country is beyond probably anything any of us have witnessed in a long, long time. The word frustration and anger and disappointment, the adjectives don't even begin to adequately describe what so many millions of our constituents are feeling, whether they are directly affected by a job loss or foreclosure, retirements being dissipated almost before their very eyes, if they know people, or they know what their children are going through.

I don't know anybody not adversely affected by this at this moment, and obviously they are looking for answers and how this is all going to work. I presume the other offices are not unlike mine. We are getting a lot of calls coming in saying they are optimistic about this now and how does it work and how do I qualify and what do I do. Can you share with us any plans that the administration has as to how we can begin to communicate directly with the American people about this so they can understand this and determine whether or not—because obviously timing is important in all of this, where you are in that economic cycle—

Secretary DONOVAN. Yes.

Chairman DODD. —can determine whether or not you are going to benefit from this or not. If you act too early, you may not. If you are too late, you may not. So the windows are not terribly wide for people to step through, and I think it is critically important that the very people we are trying to help here understand

what this is and how it works and what they need to do and can do.

Secretary DONOVAN. Mr. Chairman, an incredibly important question. We have been spending a lot of time with my staff, staff on the National Economic Council, at Treasury, reaching out to organizations that are talking to homeowners, to servicers, to make sure that we get as much information out as possible. You may have seen that Secretary Geithner and I hosted a meeting yesterday with the largest national groups that are involved in counseling and servicing to make sure that we do that.

First of all, we have a lot of information available today. I think as you know, next week, on March 4, we are going to publish the detailed guidelines, and there will be more detailed information available then. But we already know a lot about who is eligible for the program and we have already begun communicating with the servicers and the counselors about how to talk to borrowers to help them understand if they are eligible.

And what I would suggest most specifically is that, whether it is your office or anyone interested in getting more information, you can go to HUD's website at *www.hud.gov* and get all of our question and answers, all of the detailed information we have today, or pick up the phone and call the Hope Hotline, which is 888-995-HOPE, and we have been working very closely with them to make sure they have the very latest detailed information on who is eligible and how to get assistance.

As you know, the servicers have all agreed to stop foreclosures until the detailed guidance is out next week, and we would expect them to begin modifying loans immediately after the guidelines are out based on that information. So we believe that this can happen very quickly and that there is the information available today to start to help homeowners make those decisions.

Chairman DODD. Well, I would hope in that regard—obviously, all of our officers are prepared to try and answer what we can, and certainly yours will, as well, but we are also very conscious this is a new administration. You are not exactly fully staffed, I presume, yet, as well, in addition to everything else you are doing, to handle the volume.

I raise this with you merely as an idea and a thought, and others may have some similar suggestions. I wonder if you might even be convening the major heads of some of our largest television, radio outlets for them to, as a public service to the country, provide some basic information. Lending institutions themselves, particularly those receiving TARP funds here, ought to be required in some way to do something in a proactive way so the people are going right to the source where they can.

All of us are getting a lot of calls coming in. Certainly, we welcome those calls, but we are going to be wanting to defer them, and if we do it just to you, you end up with a set of problems. But if we could actually hook them up—

Secretary DONOVAN. Yes.

Chairman DODD. —with the people who then can actually deliver or answer their questions very directly. I think it is one of those moments where the kind of cooperation of some of our major media outlets could really be of help at a time like this, to give

those numbers out, to give numbers of where people can call, or do something that would allow people who are more likely to get good information through that than watching a hearing, with all due respect to C-SPAN, who I love dearly. The idea that they all watch this is unlikely.

So I raise that with you, and there may be other thoughts and ideas and we ought to talk about it.

Secretary DONOVAN. It is a terrific idea.

Chairman DODD. Let me quickly jump to one other question I have for you, as well, and that is a lot of us have heard the debates about whether or not we ought to have an affordable payment plan or have a principal reduction model, and obviously, the number of e-mails and others from people who are very knowledgeable in the area of finance and have argued for the principal reduction model rather than the affordable payment plan.

Could you share with us briefly why you decided to opt for the affordable payment plan rather than the principal reduction plan and what the pitfalls would be, as I presume you have drawn the conclusion, in the principal reduction proposal?

Secretary DONOVAN. Mr. Chairman, it is an outstanding question. In some ways, this gets to the very heart of the key to how we think this plan will be successful, and we spent a lot of time, you can believe, with Larry Summers, with the President, with Secretary Geithner thinking through these issues.

What we found, looking at the evidence, is that we believe very strongly that by getting payments to an affordable level, that is the single most important thing we can do to keep people in their home. The evidence from a series of studies, most recently a Boston Fed study, shows that a very small percentage of people who are underwater but can afford their mortgages actually walk away or default.

Now, I will recognize with all humility that we are in an unusual time, that we may not be able to compare our current environment to what has happened historically, but there is very clear evidence—this recent Boston Fed study said that for people who are underwater but can afford their payments, only in the range of one to 2 percent of those homeowners actually walk away and go through foreclosure.

So we believe, based on the best evidence that we could gather, that the key to keeping people in their homes is getting them to an affordable payment rather than focusing on principal reduction, and frankly, it is also, we believe, a more cost effective way to reach more people. There are estimates, a range of estimates, but it would have been hundreds of billions if not trillions of dollars to try to get to principal reduction across the whole portfolio of people who are at risk. So those are really the two primary considerations.

Chairman DODD. It would appear there would be obvious benefits to the principal reduction in that it would allow people to start to accumulate equity back in their homes, the wealth creation idea. That is obviously appealing from that perspective.

Secretary DONOVAN. Yes.

Chairman DODD. There were also complaints—or not complaints, but questions raised—I guess complaints as well—about what would happen in the bond market and so forth in this area because

of this choice of affordability over principal reduction. Can you respond to that?

Secretary DONOVAN. Yes, and I do think it is very important to make clear principal reduction is a good thing, and we have done everything we can in the plan to ensure that the owners of these loans can go ahead and reduce principal. And, in fact, we will share—if they choose to get the payments more affordable through principal reduction rather than interest rate reductions or principal deferral, we will match that dollar for dollar in the same way that we would an interest reduction. We also have this feature that for successful modifications, over 5 years borrowers can get up to a \$5,000 payment to reduce the principal. So we have ways that we can help to start build equity again.

Finally, I would say that we have other tools that get to principal reduction. Hope for Homeowners is a good example. We have been talking with a number of the investors that you mentioned and want to make sure that our plan treats across the board principal reduction with the same sort of incentives that we have provided for affordability. We have not gone to the point of actually paying for that principal reduction in a scale that we think could, you know, have a cost of hundreds of billions, if not trillions of dollars.

So we do allow it, we do encourage it, but we do think that the most important focus is on affordability.

Chairman DODD. Great. And I am going to come back. I will ask you in the next round I have about Hope for Homeowners and what steps you think—Senator Shelby and I worked very hard on that last year to try and put a plan with Mel Martinez, and it was difficult because there were a lot of—we were not quite in the intense moment we are today in all of this, so there were a lot of issues being raised, and I think we sort of, with all the good intentions, created a process that was so intimidating and so filled with hurdles that it discouraged both lenders and borrowers from being involved. And I would love to know if you have given that some thought, how we might modify that so that that program could also work, certainly far better than it has.

But let me turn to Senator Shelby.

Senator SHELBY. Thank you, Senator Dodd.

Mr. Secretary, Section 1517 of the Housing and Economic Recovery Act of 2008 requires HUD to undertake a study of the root causes of high foreclosure rates among residential mortgages. An interim report was due January the 31st of this year, and I know you have not been there long, Mr. Secretary. I believe such a report could, however, provide a valuable foundation upon which to structure foreclosure assistance. Until we have a firm understanding, Mr. Secretary, of what is driving foreclosures, I believe assistance plans will continue to be ad hoc and uninformed, for the most part.

When can the Committee—the Banking, Housing, and Urban Affairs Committee here—expect to see HUD's foreclosure report that is required by law?

Secretary DONOVAN. First of all, let me say, Senator, that—and you made this comment in your opening statement. I could not agree with you more that we need to take actions based on history, based on data, based on real information, and I am happy to talk about a lot of the detail and assumptions underneath what we have



done. I think we have tried to do that and to meet your standard, which is absolutely the right standard.

On the report, when we took office, roughly a month ago—it seems like a little longer some days—we had a rough draft of that report presented to us. We have been reviewing that, not only within HUD but also at OMB and at the White House, to make sure we understand, to ask for any more detailed information where we think there should be, and I can promise you we will have that report to you within the coming weeks based on the review that we are undertaking right now.

Senator SHELBY. Do you believe that report is important?

Secretary DONOVAN. I do believe it is.

Senator SHELBY. The targeting of assistance, historically the No. 1 event resulting in mortgage delinquency has been job loss. When a family has lost the wage of its primary earner, it is unlikely that any reduction in their mortgage rate will keep them in their home, generally.

Mr. Secretary, what does the President's foreclosure plan do to help families that are struggling to pay their mortgages due to job loss? What is there? I do not see it there.

Secretary DONOVAN. First of all—

Senator SHELBY. You know what I am asking, don't you?

Secretary DONOVAN. Yes. First of all, I think the President made clear in his speech this week to Congress that we cannot think about the mortgage and the housing problem in isolation from the other parts of the recovery. We have to take action, and we have, to create or preserve 3.5 million jobs through the Recovery Act. We must get credit flowing again, and the Financial Stability Plan will do that.

And so I cannot tell you that the housing plan alone solves all the problems of job loss, but—

Senator SHELBY. We know that.

Secretary DONOVAN. And you will see this in the detailed guidelines that we release next Wednesday, that we are looking at job loss in particular as a factor that we use in determining eligibility for the plan.

For example, if a borrower is still current on their mortgage but has recently lost a job, that would be one indicator we would use to be able to say there is a reasonably foreseeable event of default—is the sort of term of art in many of these pooling and servicing agreements—that that could be one factor, for example, that would allow a servicer to say, well, they are current, but it is important that we go ahead and modify based on their new job information.

You are absolutely right, if someone has no income, it is going to be very difficult to get a modification to work for them. But in many cases, what you have is people working two jobs, other wage earners in the family. And so with that attention to recent job loss, I think we will be able to make sure that the plan reaches as many of those unfortunate families who are suffering from job loss or reduction in wages.

Senator SHELBY. Mr. Secretary, I brought this up in my opening statement, and I will just pose it as a question in a minute. A number of banks that have received assistance, including the TARP

funds, have agreed to implement foreclosure mitigation plans as a condition of that assistance. Citibank, for one, has agreed to implement a foreclosure plan based upon FDIC's IndyMac model that you are familiar with.

Mr. Secretary, will those financial institutions that have already agreed to implement foreclosure mitigation plans be eligible for subsidies under your new plan, the President's plan?

Secretary DONOVAN. This is a very important question and I am glad you asked this, and this goes to Senator Martinez's point as well. We cannot forget history here. We cannot forget that there are things already happening in terms of modification plans. We do not think they have been as successful as they could be, for a number of reasons. But we have had a lot of discussions with FDIC, with servicers, and what we are generally seeing in the current modification plans is that they get down in the best cases to a 38-percent debt-to-income ratio. And so one of the reasons why we structured our plan the way that we did is we want to build on the current efforts that are there, like the Citibank one, where we are requiring lenders 100 percent at their own cost to bring the payments down to a 38-percent debt-to-income ratio, and then we will share costs.

So this actually builds on those current efforts. It does not mean that they are going to get paid for something they were already doing. What it means is we are going to bring what was a plan to bring somebody down to a 38-percent DTI through a shared payment with them further to a 31-percent DTI, which we think is the right affordability standard and will make sure that modifications are successful.

Senator SHELBY. Mr. Chairman, if I could ask one more question on lender payments. Subprime mortgage servicers, it is my understanding, are paid about 20 basis points annually, or about \$400 a year, to service the typical subprime loan. The President's proposal would more than double the current per loan servicing payment for modified loans. This appears to be a significant subsidy to pay servicers to perform the job they are already paid to do.

Mr. Secretary, could you explain to the Committee how the \$1,000 up front and the \$1,000 annual lender subsidies in the President's plan were derived? In other words, what was that based on?

Secretary DONOVAN. Yes. It is a very important question, Senator. I think hindsight is 20/20, they say, and if you look at these securitizations, the way that the pooling and servicing agreements were done, I think we all recognize today that there were a range of mistakes in the way the incentives were set up that, frankly, made sure that the people originating these mortgages did not act like they should have acted, did not have the right interests at heart, and I think we can fix that prospectively.

On this issue of payments, one of the problems with these agreements that were put in place is that the way that servicers are paid gives them a bigger incentive to foreclose than to modify because they can access additional payments.

So what we are trying to do with these payments is to basically level the playing field for modifications, to make sure that a servicer who today does not get any compensation for a modifica-

tion, but does get compensation for a foreclosure, that we can tip the scales to try to help make modifications move more quickly.

On the reason for the \$1,000 payment, you know, no number is perfect, but we did a fair amount of research, talked to servicers, talked to a range of others in the mortgage industry to try to get to what we think the rough costs of the modification is, and that is how we arrived at the \$1,000 payment.

Senator SHELBY. Thank you, Senator Dodd.

Chairman DODD. Thank you very much, Senator.

Who came in first? Senator Menendez I guess was here before Senator Brown.

Senator MENENDEZ. Thank you, Mr. Chairman.

Mr. Secretary, let me ask you—I appreciate—and I read through your testimony. We hear this plan will only help “responsible homeowners.” Can you define that term for us? What universe does that include?

Secretary DONOVAN. First of all, let me just say how excited I am to work with you as the new Chairman of the Subcommittee. I will miss Senator Schumer as Chairman, of course, as my home State Senator. But your intelligence around these issues, your commitment to housing, it is very exciting.

Senator MENENDEZ. I look forward to working with you as well.

Secretary DONOVAN. I think there are a couple of components of this issue of how do we target responsible homeowners.

First of all, the plan, we have talked a lot about the modification proposal, but to make clear, the refinancing initiative as well as the increase in the backstop to Fannie Mae and Freddie Mac are both targeted at making sure this plan benefits every American homeowners. By keeping interest rates low, obviously borrowers with good credit are the ones—and who have made their payments are the ones who are going to be able to access the mortgage market today most easily for those low rates. The refinancing initiative to help 4 to 5 million existing owners with loans through Fannie Mae and Freddie Mac that are underwater is available only if you have made your payments on those.

And then, finally, for the modification plan, a couple things. We have targeted this to owner occupants, not to investor owners who may have bought a home as a speculation or in order to flip it quickly because of what was happening in the market. We have targeted this to reasonably priced homes by using the loan limits that I talked about in my testimony, up to \$730,000 as of yesterday when we implemented those increased limits from the Recovery Act.

And then, finally, I think we have to make sure that we do not fall into the traps that got us here in the first place. We will make sure that we verify income so that if a family lies about their income to try and get a modification, we will ensure not only that the servicers are checking that, but that we are auditing—we are drafting the contracts right now to implement this program—through auditing and a range of other features to make sure that we know people’s incomes, we can verify them, and we do not have the kind of fraud either on lenders’ parts or families’ parts that got us into this.

Senator MENENDEZ. On the income side, we are using the same ratios as we have in the past?

Secretary DONOVAN. We are using the 31-percent debt-to-income ratio, if that is what your question is. As I mentioned earlier, one of the concerns we have had about existing modification programs is that they have gotten to, say, 38-percent debt-to-income ratio. And, in fact, in many cases—and this is why the redefault rates have been so high—we see lots of modifications where payments actually increase rather than decrease. So we think the 31-percent debt-to-income standard is the right standard, widely accepted affordability standard in rental programs as well as homeownership. So we think it is the right standard to make sure that we have successful modifications.

Senator MENENDEZ. So as briefly as you can, what is your timeline on the proposal? What will happen first? What will take the longest? When are we going to see the first modifications as a result of this?

Secretary DONOVAN. Next Wednesday, March 4, we will release the detailed guidance to servicers and others about how exactly the program is going to work, and the implementation, and we would expect servicers to be able to begin modifying loans based on that almost immediately. As you know, a large number, the vast majority of servicing at this point, the servicers have held up on foreclosures subject to getting that guidance next Wednesday. So we expect them—they are very eager to see that guidance and are ready—I have talked to Jamie Dimon and others myself directly. They are prepared to implement that guidance as quickly as possible after it is released next Wednesday.

Senator MENENDEZ. Let me ask you one other thing. One of the biggest lessons I have learned over this period of time is that some of these institutions simply will not police themselves and lenders will not modify their own, in many cases. Voluntary efforts just do not work.

Are you confident that there are sufficient carrots and sticks that you have provided here that will work, specifically on the servicers? Are there too many carrots here and not enough consequences?

Secretary DONOVAN. Well, I think there are a couple of pieces to that, because this is a very important question.

First of all, a requirement that any new funding from TARP to any financial institution requires that they participate in this plan, and we will be looking to see that they are auditing very carefully, that they are applying this correctly, that they are using the guidance on every loan in their portfolio to figure out which can qualify and not.

I think it is also important to remember that we have the servicers themselves as well as the investors, and one of the reasons why the servicers had not acted—and this goes to Senator Martinez's point earlier—is concern that the investors will not allow them to act or will bring suits against them.

The guidance that we are releasing next week is critical in being able to set a standard, a standard for what is a reasonably foreseeable default which allows them to move ahead and modify those loans, and what is a reasonable modification. Those standards, issued by Treasury, applying to every financial institution, we be-

lieve will go a very, very long way to allowing the servicers to move beyond this concern around the investors, because we have got an industry standard that has the force of guidance from Treasury to allow them to move forward.

So we think we have the sticks. We also think we have the protection that is needed to allow these modifications to go forward.

Senator MENENDEZ. Thank you, Mr. Chairman.

Senator SHELBY. Senator Dodd asked me to recognize you. I have no power.

Senator MARTINEZ. Well, I appreciate your recognizing me, with or without power. I appreciate that very much.

Mr. Secretary, let me follow up on that very issue of—I have called it a “safe harbor.” I think others have as well. And I know you met with the servicers yesterday and the industry folks, and my understanding is that there continues to be concern about the lack of a legal safe harbor. What is your thought on that? What are your plans? Do you think you need such authority to have a legal safe harbor? Or will the servicers be satisfied not to have the legal protections that I am led to believe they insist upon?

Secretary DONOVAN. Well, let me say up front, Senator, there is more legal wisdom on that side of the room than here. I am not a lawyer. I am not a—

Senator MARTINEZ. Never admit it.

[Laughter.]

Secretary DONOVAN. I am not a tax lawyer. I am not an expert on some of the tax issues that surround these contracts. But it is a difficult issue because certainly some of the proposals for safe harbor go far enough that they effectively would be modifying existing contracts, which to my understanding there can be constitutional issues with. There are also provisions around changing tax laws that would be retroactive that there are significant certainly policy concerns if not legal concerns around.

So I know that we are engaged in discussions about this right now with a number of folks on the Hill to try to figure out what the best way to do this is. But let me be clear. We have looked at this. Our sense is that for 80 to 90 percent of the pooling and servicing agreements, with the guidance that we are going to issue next week, we feel very comfortable that that provides servicers with the comfort that they need to go ahead and start modifying the loans without significant fear about lawsuits. But there remain roughly 10 to 20 percent of these pooling and servicing agreements that have more restrictive language which potentially will still be problematic, and that is where I think we need to try to focus our effort and to see if there are other—whether it is legislative solutions—we think we are going as far as we can go under our existing power with these guidelines, which do have the force of guidelines from Treasury that apply to every financial institution, that we can solve a large piece of this problem through that.

Senator MARTINEZ. Well, I hope so. My sense is that—well, maybe the problem is not with all private servicers. I believe that anyone who is concerned about a private investor’s reaction to a modification might have a problem, but, anyway, I would like to know your thoughts on bankruptcy cramdown, essentially, as it is called, and you mentioned the constitutional issues with renegoti-

ating contracts. Obviously, in the legal context of a bankruptcy, perhaps those problems will be avoided. But I know we are going to be confronting that issue. Do you think that that is a necessary element to have in the arsenal available to be able to stave off continued foreclosures and, you know, the detrimental effect that has on the housing market?

Secretary DONOVAN. The President believes and I believe that carefully tailored bankruptcy reform is a piece of the solution. Clearly, making sure—and this is absolutely why we took action in the way that we did. We have to make sure that well before we ever get to a bankruptcy court or to foreclosure—and, in fact, even before borrowers get to 90 days delinquent—it is critical that we start to modify these loans in significant numbers. That avoids bankruptcy court. It avoids foreclosure. It avoids the terrible effects on the families themselves, but also their neighbors and the communities.

So we do not see bankruptcy court as the place to work out mortgages. We think that would be a terrible result, frankly, of what could be happening. But we do see that carefully tailored reform that includes the kind of things that I mentioned earlier—for example, having it be retrospective rather than prospective, applying only to existing loans rather than new loans; a limit on the size of loans, we have discussed as well, to, for example, the conforming loan limit so that we do not have millionaire homes that end up in bankruptcy court; provisions that would ensure that if a servicer has made good-faith efforts to modify the loan along the lines of our program, that they are protected, as well as making sure that there are provisions in the code that would allow us to protect against an example where it was coming through foreclosure and would be modified down to a level that was well below the market value of the home. We do not want, you know, arbitrariness or the unpredictability of a bankruptcy judge modifying, you know, to a level that is well below the value of the home, because we do not think that that is fair as well.

So those types of careful tailoring of it we think can make sure that it is done in the right way and not introducing stability into the process.

Senator MARTINEZ. My time is up. Thank you very much, Secretary.

Chairman DODD. Thank you very much.

Senator Merkley.

Senator MERKLEY. Thank you very much, Mr. Chair and Mr. Secretary. I want to follow up just a little bit of new information there that I had not heard before regarding your points about the tailored nature of bankruptcy. Can you expand just a little bit on the good-faith provisions, if I caught you correctly, that if a servicer proceeds to work with the administration's program and does so in good faith, then in that case modification and bankruptcy would not be on the table? Is that correct?

Secretary DONOVAN. Well, let's be clear. Bankruptcy reform is something obviously that Congress is going to make a decision about. There are discussions ongoing about ideas like this. So there is nothing in our modification plan that sets the detailed limits or lays out these ideas about bankruptcy reform. That is really going

to be part of a discussion with all of you, and those discussions are ongoing.

So what I am laying out are potential ideas for ways to target bankruptcy reform in a way that we think would be most effective.

Senator MERKLEY. Thank you. I will say that as I went through the details of the loan modification program, I think that your team and the Treasury team and Larry Summers' team are to be saluted for really wrestling with a lot of nitty-gritty details and trying to lay out a road map of how to make modifications work. So I do compliment you all on that.

I remain a bit of a skeptic about how easy this is going to be because of the enormous thicket of challenges: the issue of second mortgages, the issue of legal liability, the fact that the servicers have conflicting language over the range of their authority. Certainly we have seen in the past that there has been great reluctance to wade into those issues. I think you have done everything possible in laying out this plan to overcome that.

But is there a Plan B? If, in fact, all of these incentives and, in addition, the carrots and the sticks, the bankruptcy, if these things do not result in a significant number of loan modifications due to the problems we all have worked to overcome, is there a Plan B on how to take on using, if you will, the refinance strategy in addition to the loan modification strategy?

Secretary DONOVAN. Well, first of all, let me say you are absolutely right that this is a complicated problem, that we find ourselves in a very difficult situation. The complexity of these loans and the securities behind them, it is not simple, and we have done an enormous amount of work with our team to try to get through a lot of those issues, and I appreciate your recognizing that.

What I would say is that we have through this plan tried to provide a range of options: the refinancing proposal that will move forward with the GSEs for underwater borrowers; fixes to Hope for Homeowners to make sure there is an option that includes principal reduction; and getting folks into long-term, fixed-rate FHA loans. So we do have a couple of pieces to this that I think complement well the modification effort.

Obviously, to go to Senator Reed's comment, we will be watching this very closely, watching the results. If there are tweaks that we need to make to the program, we will do that. But I want to make very clear that we expect servicers to move quickly and not—one of the problems that we have had, I think, over the past year or so is a shifting target and a shifting set of programs. We want to send a very clear message that this is a comprehensive, full solution that we want to focus on today and make it work. We are working with the servicers, with the guidelines out next week. We expect to see a large number of modifications happen very quickly. And I do not want to engage in too much discussion about Plan C or Plan D because, frankly, we think this is the right program, and we think that it can be effective and that it will be effective with the set of options that we have provided.

Senator MERKLEY. Thank you for laying that out.

I held a conference in my State last week over the foreclosure mitigation issues, a wide range of participants. What came out of that meeting was—the single core message was how difficult, how

extraordinarily difficult it is for homeowners to reach anyone with whom they can actually negotiate. You can imagine the situation of going through the phone tree and finally getting somebody on the line after you have been waiting an hour or so, and the person says, "Well, I cannot address loan modifications. I can tell you what your balance is on your loan," or when your last payment was or whatever. And so they try to get through to somebody with authority, and after they have spent multiple hours, several days, they give up.

So anything that can be done—and I know my time is up, so I will just—but anything that can be done, whether it is a national hotline, whether it is the support you are considering providing to servicers to enable them to expand their training and their staff, their negotiation team. If there is not a channel of communication that ordinary people can get through to someone, it will greatly hinder the success of this. And I just encourage you, I bring you a message from frustrated homeowners in Oregon that they need help getting through to people that they can actually talk to. Certainly it is much less of an issue when loans are held in a portfolio, but when they have a servicer who loans—a servicer connected to a trust, and the trust has split up the cash-flows and sold them as derivatives, it just seems like the message is that when there is not a personal relationship with a local institution, it is very, very difficult. I think you know that.

Secretary DONOVAN. I could not agree more, Senator. I think it is a very, very important point, both to make sure that we have outreach from the servicers, and the compensation you talked about is an important part of them being able to staff up and really provide the service that we need.

We also need counselors out there, and as part of the Housing and Economic Recovery Act, a significant amount of funding that you provided through NeighborWorks. We have been meeting with NeighborWorks and making sure that all of this information is available, that they are reaching out and that that money is available as quickly as possible to help counselors.

And also Chairman Dodd had a terrific idea earlier about advertising, using campaigns. That is something that I think we will try to see if there are ways that we can get out there and inform people. And as I said earlier, 888-995-HOPE is the national hotline that has been set up that is available for borrowers who have questions about the plan, want to see if they are eligible, or go to our website at *www.hud.gov*.

Senator MERKLEY. Thank you very much.

Chairman DODD. Thank you very much, Senator.

I apologize to Senator Bayh, but we try to do this in the order that people arrive, so Senator Reed.

Senator REED. Thank you. Evan, do you need to—

Senator BAYH. No.

Senator REED. OK. Secretary Donovan, I have been arriving and leaving constantly, so thank you for keeping track. But Secretary Donovan, again, congratulations and we are extremely delighted and very confident of your role going forward.

The plan rests upon the effective actions of the GSCs, FHA, Veterans Administration, Fannie, Freddie, and there is an issue of ca-



capacity. Do they have the resources, the computer resources, the personnel? This is a program that has to work not only to help families, but also to be financially sound and well managed, and I wonder if you have any specifics relating to program improvements or additional resources you need. And I say that in the context that last year, Senator Shelby and Senator Dodd were very kind, because we included in FHA modernization language in the legislation. They have that, but we have to go beyond the language and make sure they have the resources. So any comments, I would appreciate.

Secretary DONOVAN. Well, it is very important both that the GSEs and FHA have adequate resources. The President is releasing our initial budget today and I think you will see that does focus extensively on building FHA capacity. You all have been very, I think, forward-looking in terms of recognizing the need to enhance staffing systems at FHA to handle the increasing volume, and that includes the modification efforts that we will undertake at FHA.

There is legislation that we hope would be part of the package that both has some improvements to Hope for Homeowners but also allows partial claims to happen at FHA so that FHA can participate in this modification program in a very consistent way with the plan that we have laid out.

And then on the GSE side, at the broadest level, the announcement as part of this plan that we would, as authorized by Congress, increase the Keep Well by \$200 billion ensures that Fannie and Freddie will have the resources to be able to implement this plan and continue to guarantee mortgages.

But we are, rest assured—I was talking to somebody this morning who was in meetings until 12:30 in the morning with the team that is implementing this. We are making very, very sure that there is adequate reporting, oversight, that the systems are there to be able to implement this plan. We are doing it very quickly and I can't promise that we won't make some mistakes, that we won't have to learn as we are going, but we are very focused on the implementation and making sure the GSEs have the resources and they are doing what they need to do.

Senator REED. Thank you very much, Mr. Secretary.

There is another issue, and this is part of the, not directly related to housing but part of the current crisis. There are many not-for-profit organizations, hospitals are just one example, who have been sort of squeezed out of the credit markets. Some hospitals participated in these option rate bond mechanisms. That option rate bond mechanism has essentially closed down and they are looking at serious financial issues.

Since 1978, in my understanding, HUD has the ability to allow hospitals without existing capital projects to refinance their debt into lower interest rate loans. I would ask you to look at this issue, and not just yourself but share it with your colleagues on the economic team, because I have a feeling that one of the repercussions of this crisis is that there are going to be some not-for-profit hospitals across the country who are going to be in difficult shape when their existing financing, which sometimes was as low as 3.5 percent, is now kicked up to 12 and 13 percent, just unaffordable.

So you have, I think, some authority and I wish you would look into that, if you would, please.

Secretary DONOVAN. Absolutely. I think we both need to do things to strengthen the bond markets in general, and that was part of what the President announced last week, was strengthening for HFAs, State HFAs who can be a real part of this solution with refinancing using the \$11 billion in tax-exempt bonds that was part of your Housing and Economic Recovery Act, but also the hospital program is key. Despite being from New York, it used to be that the portfolio in the hospital program was about 80 percent New York City hospitals and New York State hospitals. One of the great things about the program, it has now expanded significantly where it is providing financing for hospitals across the country and it is very, very important.

Senator REED. Thank you. One final point, because I have a few minutes. The Chairman has pointed out and my colleagues have echoed the need to communicate with the public these details, but I think there is another message that has to be continually communicated, not just by yourself but by the President, is that for those people who are paying their mortgages and feel the sense of, well, that they are torn because they want to help their neighbor but they are making their responsibilities, the fact that if we don't move aggressively with respect to these foreclosures, the market will deteriorate so that people a year ago or today who are making it won't be making it. They will be in the next wave of these foreclosures. I think that message has to be communicated, as well as the details of how one qualifies for this plan.

Secretary DONOVAN. A very important point. Our models based on the plan show that simply by modifying mortgages in the way that we are proposing, the \$75 billion dedicated to that, we will help to avert a loss of \$6,000 in value for the average homeowner, not the average homeowner in foreclosure, for the average homeowner that is making their payments across this country. So it does have a very tangible, concrete benefit to everyone.

Senator REED. I think that point has to be made over and over again, because frankly, people, they are struggling and they are doing their best and they have got to know that they are getting a benefit, too. Thank you.

Chairman DODD. Thank you, Senator.

Senator Bayh.

Senator BAYH. Thank you, Mr. Chairman.

Secretary, thank you for your service.

Secretary DONOVAN. Thank you.

Senator BAYH. I think your energy and your confidence will bring a breath of fresh air to the Department at a time when the country needs it, so thank you for that.

Two very brief questions about things of particular just to my State that are tangentially related to the topic at hand today. Last June 30, President Bush signed into law an Act that Representative Donnelly from my State worked with me on. It was called the FHA Manufactured Housing Loan Modification Act. If you have staff here, I hope they will make a note of that. It is particularly important to North Central Indiana, particularly Elkhart County, where the President made his first trip outside of Washington as

President of the United States. The unemployment rate there is 15.1 percent.

The changes called for in the Act, although signed into the law more than half a year ago now, have not been made. Can I get a report from your staff about when the Department intends to make those changes?

Secretary DONOVAN. Yes. Can I give you a report myself right here?

Senator BAYH. I am highly impressed. This is a well-briefed Secretary, Mr. Chairman.

Secretary DONOVAN. When we came into office about a month ago, there was a lot of concern on your part, Senator Corker, Representative Donnelly, and others, Chairman Frank reached out to me about this, that there had been potentially a determination within the Department that implementing this law needed full rulemaking, which would have delayed the implementation of it another—months, frankly, and that there were critical changes that needed to move quickly.

We have gone back with our legal team. We have made sure that we can go ahead and get this law into effect just with a mortgage e-letter, rather than going through the entire rulemaking process. That letter is being drafted as we speak. I can't tell you exactly what day it is going to be done, but I think within 30 to 60 days, we will have that out and the law will be implemented.

Senator BAYH. Thank you. I am very impressed. If you would let us know as soon as the letter is complete, I am sure the people of Elkhart would be very gratified to know the administration has moved this quickly in the face of previous inaction, so thank you for that.

The second thing will come as no surprise to you, either. We had mentioned sometime before your confirmation the situation in Gary, Indiana.

Secretary DONOVAN. Absolutely.

Senator BAYH. You know, they are very desirous, as are people outside of Gary in that part of our State. They have hundreds of derelict homes. It is keeping project capital from coming in. They become sites for the illegal activities and that sort of thing. They would like to have an aggressive program of tearing down those homes, rehabilitating the land, preparing it for private home construction, that sort of thing.

I was pleased to see that the administration is putting together something called the Affordable Housing Trust Fund, which might be eligible for this, or you already have in place in the Neighborhood Stabilization Fund. If I could just get a report at some point, Mr. Secretary, about what could be done through those avenues or others to help facilitate this process in Gary, because until we take care of those derelict homes, frankly, it is going to be very hard to generate much positive activity on the upside.

Secretary DONOVAN. Absolutely. When we talked about this, one of the points you made, which I think is right, I have been hearing this from smaller counties in California and Florida, as well, where the original formula for the \$4 billion in Neighborhood Stabilization funding, a large share of it went to States. It didn't necessarily reach, at least directly, lots of the locations, particularly smaller

areas, smaller towns that weren't eligible directly, to be able to deal with the problems of foreclosed homes, vacant homes.

I am very happy that as part of the recovery bill, there is an additional \$2 billion in Neighborhood Stabilization funding. Yesterday, the Vice President announced we were releasing allocations for 75 percent of all the HUD funding that was in the bill, over \$10 billion. We are now going to move to implementing the competitive aspects of it and we should have those competitions written within the next 30 days or so, and that includes this Neighborhood Stabilization funding. It is competitive and we want to really target the areas that have comprehensive strategies, that are working already well with Neighborhood Stabilization or didn't get access to it.

But I think in particular in Gary, where, for instance, in the Chicago metropolitan area there has been a very good, strong, coordinated effort around this issue, that we ought to be looking at innovative things like that—

Senator BAYH. They have such a concentrated problem that it really would pay huge dividends, so I thank you for your cooperation on that.

I have got 22 seconds left. Let me ask you this, my final question. Do you know what percentage of mortgages in the country are current, being paid on time? It has got to be 90 percent, something like that.

Secretary DONOVAN. Roughly 90 percent are—

Senator BAYH. Well, here is my question. I hear from people all the time who say, look, I did the right thing. I have lived my life prudently. I saved my money. I didn't buy a house that was too big for me. I didn't take on a loan that I couldn't afford. And now I see my tax dollars are being used to help those who made different decisions. How is that just? How is that fair to people who have lived within their means?

So my question to you would be, on behalf of the 90 percent of people who are current with their payments, how are we not, in essence, enabling unfortunate behavior through our activities? Now, I am playing a little bit of a devil's advocate here, as you can imagine, but that question is out there. People are angry. I think it needs to be addressed head on. What would you say, Mr. Secretary?

Secretary DONOVAN. It is a very important question. There is a lot of anger. There are a lot of things that are happening in this country that are unfortunate that are happening to families. I think it is very important, first of all, that we recognize the most significant part of our plan in many ways is to take the actions we need to take to keep interest rates at what are really generational lows. That benefits every single American family that owns a home or wants to buy a home. Twelve-hundred to \$1,600 a year, on average, we think just the actions we took to keep Fannie Mae and Freddie Mac interest rates low will have that benefit. So that reaches every homeowner in the country.

Refinancing, where a family has made every payment, they are current on their mortgage, and simply because housing values have dropped around them in their community, they may have a seven or an 8-percent mortgage rate, they can't take advantage of the re-

financing to today's low rates. We are going to change that through our initiative in the plan. Four to five million homeowners who can benefit, an average of about \$2,600 a year for those families to benefit.

All of those, good credit, paid their bills, done everything right, haven't made mistakes, they are all benefiting.

But I think the final thing that is perhaps most important for those concerned about are we providing money to people who overstretched, who shouldn't have gotten into homes that were too expensive to begin with, we are doing everything we can in that plan to target it to people who are paying their bills, that are working hard, but we have to recognize, first of all, there is a lot of job loss in this country. The number of people, because they have a medical emergency and they can't pay a bill.

We have to, I think, as Americans, rise to the occasion and say, yes, we are going to do everything we can in this program. We are not going to allow speculators to participate. We are going to check incomes carefully. We are going to make sure we don't have fraud. But we have got to help folks.

And, by the way, it is helping ourselves because 45 percent of all home sales in December were distressed sales. That drives everybody's home price down. Just through the modifications that we are doing, we think we can save the average homeowner in America, the ones who have played by the rules, making their bills, \$6,000 on their home value. So we have got to make sure that, I think, Americans understand that this crisis we are facing, the foreclosure crisis, is hurting everyone and we have got to stop it so that everybody benefits, as well.

Senator BAYH. Thank you, Mr. Chairman.

Chairman DODD. Those are excellent, excellent points. I would just point out on the same point that in my home State, I don't know if this is true of all States, but my community bankers—and I think one of the things we have got to be careful of is the language we use describing bankers because a lot of our bankers at the local level have been prudent lenders over the years. In Connecticut, they tell me, my community bankers, that the best month they have had on mortgage origination was the month of December, and the next best month for them was August of last year. I don't know what the January numbers look like.

But at a certain level, and obviously it is not everywhere, but there is good lending going on out there and there is activity. In fact, in credit markets, I think, what is it, a 5-percent, 30-year fixed-rate mortgage is available today, which is a pretty good indication that at least in that credit market, there is some level of activity that ought to be encouraging to people.

Secretary DONOVAN. And we need to get back to basics in lending the way a lot of community bankers did the right thing and those mortgages are performing well.

Chairman DODD. But your \$6,000 figure is a very important piece of information that I think needs to be transmitted, as Senator Reed said, over and over and over again to people that they understand that even though they are not in that category, they are a beneficiary by getting this back on its feet.

Senator Schumer, before, when you were in and out, I was saying that a lot of us got to know about Shaun Donovan because of you, and your best cheerleader up here in terms of your tremendous work in the city of New York was certainly trumpeted by Senator Schumer over and over again. So you have got a great ally and friend here in the Senator from New York.

Senator SCHUMER. Thank you, Mr. Chairman.

Secretary DONOVAN. Hear, hear.

Senator SCHUMER. Thank you, and I think, as you know because you are so on top of all these issues, as America gets to know Shaun Donovan the way New York has gotten to know him, they are going to realize we are going to have one of the best Housing Secretaries that we have ever had—

Secretary DONOVAN. Thank you.

Senator SCHUMER. —and so welcome, Shaun. We are glad to see you here.

First, just a point of reiteration. Senator Reed, Jack Reed, mentioned putting hospitals, seeing if they can be eligible for FHA.

Secretary DONOVAN. Yes.

Senator SCHUMER. You know, the problem of people getting financing is just everywhere, and sometimes I worry that we are not even as knowledgeable of it as we had—well, hospitals. I have heard many hospitals have the money, have the resources, have the ability to build and can't get any financing. So looking at FHA that way in terms of job creation without costing us much, please look at it.

But here is my main point. You know, I think the housing plan that you and Tim Geithner and, of course, the President put together is really a home run. The Bush administration sort of when it came to foreclosures watched all the fast balls go by—they are fast balls, they are hard to hit—and refused to even swing. You have stepped up to the plate, you are swinging, and I think you have knocked it out of the park.

And I don't think there is enough understanding of this, and so I would like to just reiterate—Senator Menendez touched on it. I would like to just elaborate on what he talked about. Sorry I couldn't be here while you were being asked all these other questions.

The real block, in my opinion, has been the servicers and the bond holders. It hasn't been the homeowner, even the homeowner who could afford to pay back. It has been the servicers and the bond holders. Now, the bond holders have their own economic interest sprayed all over the lot because very few home mortgages are held and the riskiest tranche holder has a different interest than the safest. The riskiest says, I am not doing this because I lose all my money if the house is 98 percent of its value. Well, you got the higher interest rate for that.

But the servicers are the ones who could do something. And unfortunately, the previous administration didn't really focus on the servicers. They said, go do it and we will protect you, but it was sort of vague. What you have done in your plan is laid out specific guidance that every regulator agrees to and that most legal experts say will protect the servicer as the servicer endeavors to refinance the mortgage so that it can be at a lower rate.

The plan also very intelligently, I mean, I know Evan asked the question, well, what about people who really got underwater, way over their heads? They are not going to be helped by this. But people who may have lost a job who had always paid, and maybe they are paying 50 percent of their income as mortgage, not 80, but 50, not 200, will really be helped by this and they are the right group to help.

But I think the most important thing is something you told me, and I would like to get that out here, and that is that many, many servicers have agreed to start refinancing the mortgages and they feel they are protected by the guidance that you have issued. That is a key, because if a large percent of their servicers say they are going to step up to the plate, you are going to see a lot of refinancing and a lot of homes that might have gone into foreclosure taken off that list in the next three or 4 months.

So could you elaborate a little on that? I think that is really important for the public to know.

Secretary DONOVAN. Thank you. As I said earlier while you were out of the room, I am very excited that Senator Menendez will be Chair of the Housing Subcommittee, but I will miss you as Chair there—

Senator SCHUMER. I am very excited that is the Chair of the DSCC.

[Laughter.]

Secretary DONOVAN. So that is very important. We have tried to work very closely with servicers. We believe, as you said, that we have tried to make sure we are covering all the issues around their compensation, their incentives, around these legal issues with the investors. But the proof of the pudding is that they are, first of all, they suspended foreclosures pending the plan, which clearly signals they think there is something in the plan that really helps them move forward on the modifications.

And I have already had commitments, Jamie Dimon himself said a million loans, they think they can do through this, just at JP Morgan Chase. We had a meeting yesterday with the servicers with President Wells and he said this will allow them to move forward and to do a very large number of loans.

Senator SCHUMER. I think the public has this view that the servicers are little entrepreneurs all over the lot. What percentage of the servicers come from the large banks who, say, have accepted significant money from the TARP?

Secretary DONOVAN. The largest banks cover about two-thirds of the servicing.

Senator SCHUMER. And you have a little leverage over them, I would say?

Secretary DONOVAN. And, in fact, we have made it explicit that any funding from TARP requires participation—any new funding from TARP requires participation.

Senator SCHUMER. So this means that right now, two-thirds of the servicers are likely to go along with this plan for those mortgages that meet the guidelines and the guidance that you have put out, is that right?

Secretary DONOVAN. We hope it goes well beyond those biggest—

Senator SCHUMER. But if it goes to two-thirds, shouldn't that be a real change in the housing markets and rates of foreclosure, and even shouldn't it help us find a floor? Couldn't the markets, the housing markets then say, hey, so many of these are being refinanced. We know now that there is going to be some floor to housing.

Secretary DONOVAN. Yes.

Chairman DODD. Let me ask, how about the previous recipients of TARP, as well, doing exactly what we described? How many more would you include if we added previous recipients of taxpayer money?

Secretary DONOVAN. To be honest, I don't know—I don't have the details. I don't know the numbers of going forward versus previous.

Chairman DODD. But it would be higher—

Senator SCHUMER. But I think, yes, and Mr. Chairman, I think most of the big banks that have already received TARP money who are servicers have agreed to be part of this, isn't that right?

Secretary DONOVAN. Absolutely.

Senator SCHUMER. So you have got them, I mean, the Citigroups and the JP Morgans and the Wells and all of them. And they are the servicers. That is the amazing thing. I didn't really know that until you told me.

Secretary DONOVAN. Yes.

Senator SCHUMER. So I really would say that your program is going to have a significant and deep effect on housing markets, improving them, and that can reverberate throughout the whole economy. You know, I am sort of surprised it hasn't gotten more focus and more attention. I don't know why, but—

Secretary DONOVAN. I think when we can show results, and we will very clearly be focused on auditing and making sure that we are getting the results that we—

Senator SCHUMER. One final question. When should we start seeing the results that this guidance, the effect it will have on the servicers?

Secretary DONOVAN. Well, next Wednesday, March 4, we are going to release the guidance. We, based on our discussions with servicers, believe that servicers will be able to almost immediately begin modifying loans under the guidance. It may take some of them a little bit of time to, you know, get the systems and all that going, but we are working on it with them already.

So I would hope that in March, but certainly in April, we start to see a significant decline in foreclosures. Again, 45 percent of all home sales in December were distressed sales, so there is no question that if we can lower the number of distressed sales of foreclosures that we can begin to stabilize the market and help it return to balance.

Senator SCHUMER. And that is going to mean some real stuff to the stability of the banks and of the whole financial markets, because they are still holding this paper. They don't know what the bottom is. So this is dramatic and significant and I would just commend to my colleagues, the public, everybody, pay a little attention to this because it is one of the first early bits of good news, I think, that I have heard about this, and I congratulate you, Secretary Geithner, and the President for coming up with it.



Secretary DONOVAN. Thank you.

Chairman DODD. Senator Warner.

Senator WARNER. Thank you, Mr. Chairman. Let me thank you and colleagues who have been here long before me for continuing to raise this issue, particularly in terms of the importance of finding relief for the housing sector and the fact that you have been a constant advocate on both sides. If we are going to spend TARP money, make sure some of it is directed here in the housing area.

Mr. Secretary, good to see you again. I have a couple of lines of questions and I will try to be brief. One, I know some of my colleagues when I was not here pressed somewhat on how we make sure that folks around the country understand these new programs and how they get access to it. One point that I am not sure that you fully addressed, though, is that I am getting folks calling our office, and Lord knows it is going to exponentially increase on the fourth, and they are saying they are calling their servicers and some of their servicers are actually not telling them who owns their loan at this point.

There seems to be some ambiguity in the law whether a servicer is actually required to disclose who the owner of the loan is, and we have had this on a number of occasions and it sure seems to me that we need to make sure that there is clarity on that, whether there needs to be regulatory change or at least guidance. I could see these servicers getting flooded with calls on March 4, and if there is still this ambiguity, some folks coming back even more confused if they can't even find out who actually owns the loan at this point. Have you heard—

Secretary DONOVAN. I appreciate your mentioning that. We are working in depth on the guidance now and we will ensure that that is an issue we look at.

Senator WARNER. Please look into that.

I am a little bit of a broken record, Senator Bennet and I are on this issue, and Senator Menendez and Senator Schumer have raised it in terms of hospitals, but I do think anything we can continue to do for this whole municipal bond market, and a piece of that, obviously, are our housing agencies that I think can play an important role, and have you given any more thought to how our State and local housing agencies will play a role in this real estate recovery?

Secretary DONOVAN. I am very glad you asked that. Virginia in particular has one of the strongest housing finance agencies in the country, and it has done great work.

The President actually mentioned in his speech last week that as part of this plan, we are going to provide some assistance to housing finance agencies who can really be part of the solution here. There was \$11 billion in new tax-exempt bond authority that was part of the Housing and Economic Recovery Act last summer. But because of the issues in the bond market that you rightly point to, they have not been able to fully utilize that funding to be able to take advantage of the refinancing they could provide and other benefits they could provide.

So we really have two lines that we have been working on with Treasury on this front. One is there are existing bonds that because of the lack of liquidity out in the marketplace—and many of

these are, you know, weekly resets or bonds in particular that have struggled, auction rate securities. My experience in New York, the market just dropped out on those. So making sure that there is adequate liquidity available for existing bonds that are out there so that we do not have, you know, real problems for the housing finance agencies on the loans that they are already holding. And then in addition, for new bonds that they are going to issue, looking at whether we can—what we can do to ensure that there is an adequate market out there.

Obviously this goes well beyond just HFA bonds, municipal bonds. There are lots of different issues in the market, and Treasury is looking at that issue more broadly. But we want to make sure on the housing front that there is an adequate market for these bonds going forward.

Senator WARNER. Well, Chairman Dodd has been very supportive and helpful to those of us who have raised this issue, and all I can make a request is when we have had Secretary Geithner and when we have had Chairman Bernanke in, we have not heard a lot of specificity. In fact, I believe Secretary Geithner said he had not seen any good ideas around how we could restart the muni markets. And I would hope that you would be the inside-the-administration advocate that this is directly helpful to not only the housing market, these are oftentimes shovel-ready projects. I know Senator Bennet has got a great interest in a number of school bonds. There are highway bonds. There is a whole host of municipal bonds out there that if we can jump-start that, these are truly projects that are ready to move forward and that would be very valuable.

Secretary DONOVAN. On the good news front as well, just to make sure you know, yesterday we released \$10 billion, about 75 percent of all HUD's funding from the Recovery Act. That included \$2 billion, over \$2 billion for housing finance agencies to help jump-start tax credit deals that are stalled. So very hopeful that by getting it out so quickly, we can make sure those projects move forward.

Senator WARNER. Mr. Chairman, could I ask one more question? I know my time has expired.

Chairman DODD. Because you missed your opening statement, take a little more time.

Senator WARNER. A Schumer 2 minutes or—

Chairman DODD. Don't press your luck.

[Laughter.]

Senator WARNER. I think you have laid out the framework of a good program. I am anxious to see more of the details. But a piece that I know the Chairman has been supportive of as well—and I have had my thinking change on it. If we are going to look at bankruptcy reform that would allow principal readjustment or so-called cramdown, my hope is that it does become the hammer of last resort. And it seems what has been missing—and I can understand perhaps timing-wise now why you did not include it in this initiative. But for those homeowners that are truly underwater, if we provide that bankruptcy reform, I would hope the administration would give some thought to, you know, what initiative or what program could be out there as the step before you have to take that. We should reserve that bankruptcy process as the ultimate last-re-

sort hammer, and I hope there will be some interim prerequisite of good faith acted by the homeowner to make sure that they have really tried and that the servicer and the lender have really made a real effort, and that we only push folks into using this tool in bankruptcy as the ultimate last resort. That has been kind of missing from the debate. I know you have received some comments that the program does not address those folks that are more than 105 percent below their loan-to-current-value ratio, those folks who are really deeply underwater. At some point, they are going to have to be part of the equation as well, or they are all just going to move into the bankruptcy provision if the reform is made.

Secretary DONOVAN. A couple of comments on that because it is very important. We completely agree that bankruptcy court should not be the place where, you know, millions of loans are worked out; that if that happens, that is a problem for everyone, and that we want to do everything we can to avoid that. And I do think there are other options in this program. The President did say as part of his speech, obviously it depended on legislation in Congress, that we do support tailored, targeted bankruptcy reform. But we do have options as well. Making sure Hope for Homeowners is a viable alternative which allows a mortgage to be re-underwritten at a reasonable level with principal writedown, make sure that program is effective.

As Chairman Dodd said earlier, none of us knew maybe where we would end up and that what was designed in Hope for Homeowners was based on what was happening at the time, and we are at a different place now so we need to adjust the program to make sure that that works. I think that is an important component.

The other thing I would say—and there has not been much attention on this, but it is important as well—we have added incentives for things like short sales or deed in lieu of foreclosure. You have lost your job, but you find a job in a new town, you have got to sell your home but it is underwater—you have got a problem, right? Because your only alternative really is bankruptcy or to go through a foreclosure, wreck your credit. And, frankly, the bank is not going to recover—if you are really underwater, they are not going to recover any more either. So the best solution there is often a short sale, which is where a bank takes less than the face value of the mortgage to satisfy the debt, and you can then move and leave your home. It does not restore all your equity, but it at least allows you to get on with your life. We have incentives for those kinds of alternatives so that you do not end up in bankruptcy. So there are a number of provisions we have tried—

Senator WARNER. Making clear what that bevy of options would be before bankruptcy. The last point I will make just is a comment, that I sure as heck agree with the Chairman and Senator Martinez that one piece on the servicers was to make sure we give them the right incentives to act. But the other piece I continue to believe—and Senator Schumer made a comment about this. Since we have sliced and diced these loans into so many tranches and because there will be an unwillingness of those folks who are at that top 2, 5, 10 percent, the discussion we had earlier, that are most exposed, and then we have got all of the side bets and credit default swaps that were made on that last tranche, you know, the more

we can clear out some of the legal hurdles and the more we can do some hold harmless or what the Chairman put forward in his amendment, it has got to be a piece of this mix or, you know, all these good intentions could still end us up in court.

Secretary DONOVAN. Yes.

Senator WARNER. Thank you.

Thank you, Mr. Chairman.

Chairman DODD. Before I turn to Senator Bennet and Senator Akaka, could I raise—just on that last point, take advantage of Senator Warner's question. This is about the safe harbor bankruptcy, the lenders that offer borrowers a loan consistent with your program. The second lien holders. There is an issue here that we are going to confront, and I do not know whether we address it or not, and there are some concerns that under the administration's proposal and the safe harbor—and this is a very important question. Are we adequately covering the second—are we going to be able to deal with the second lien holders? So many of these were piggyback loans, and whether or not they are going to be accommodated for that in this idea. Or are we giving the lender, in effect, veto power over all of that?

Secretary DONOVAN. I think it is important to make clear that there are two very different situations for second lien holders: a modification versus a refinancing. In a modification, you are keeping the existing first loan in place and changing the terms of it. A second lien holder has no ability to stop the modification or to—so for the modification program, the second liens really—and we have heard this consistently from servicers. They are not a significant problem. We are still looking at whether there are some enhancements to the program as part of the final guidance that we might, you know, deal with second liens even in that case to make sure that they stay silent and they are not an issue.

But I think the real issue is around where you have refinancings, where you are extinguishing the first lien, and then would you have to get explicit permission or resubordinate the second, what you do with those. And that is where we are looking at in more detail exactly what should be done and as part of the guidance. I think you will see next week that we have some ideas around that.

But, really, I want to make clear: On the modifications, everything we are hearing is that they are not a significant issue because the first—

Chairman DODD. I appreciate that, and obviously a lot of members on this side of the dais are very interested in how this moves forward. So we would love to stay in very close contact with you.

Secretary DONOVAN. Mr. Chairman, if I can just take one moment, I realize—

Chairman DODD. That is fine.

Secretary DONOVAN. Senator Warner made a point that I want to make sure is absolutely clear, because there has been some real confusion about this. The 105-percent loan-to-value restriction is only on the Fannie Mae and Freddie Mac refinancing initiative. For modifications, borrowers that are much more significantly underwater, up to typically about 150-percent loan-to-value, can participate in the modification.

Senator WARNER. But that is in the first—the Homeowner Stability Program I thought was the one that had the cap at 105.

Secretary DONOVAN. There is a portion of this which is a refinancing 4 to 5 million homeowners, existing Fannie Mae or Freddie Mac loans that are current on their mortgages, that are paying, and cannot refinance to today's low rates because they are at 80-percent to 105-percent loan-to-value. Those are the folks we are going to allow to refinance but they are current. Where somebody is more significantly underwater, having trouble paying their mortgage, you can be more deeply underwater to be able to participate in the modification.

There has been a lot of confusion about this in the press and otherwise, and I am happy you raised it because I want to make sure that that is clear.

Senator WARNER. So those folks can be at 150—

Secretary DONOVAN. More deeply underwater. We think generally 150-percent loan-to-value is as far as we can go, because for modifications to be successful you cannot be so deeply underwater that—

Senator WARNER. And that is the program where we are going to try to modify and buy down to 31 percent of income.

Secretary DONOVAN. Exactly.

Senator WARNER. Making that clear would, I think—I think there has been—the press has really—

Secretary DONOVAN. Yes, has been confused.

Senator WARNER. —not understood that.

Chairman DODD. Senator Shelby has something on the same question. I apologize to my colleagues.

Senator SHELBY. Along these lines, it is my understanding of the legal—you have got a first mortgage, then you have got a second mortgage. Of course, we know the first mortgage has priority over everything. But if you supersede that first mortgage with another mortgage, in other words, pay it off and modify it, lower the terms, couldn't you get into a dicey situation because the second mortgage—you know, you are the Secretary, and I am sure you have got lawyers everywhere. But the second mortgage then becomes the first mortgage in an ordinary situation. I guess that is what some of us—Senator Warner was kind of alluding to this. That is kind of dicey. I hope you are doing it right. I guess you could—I do not know this. It depends on—you can modify something, modify the note, but you start fooling with the mortgage, you know, especially if you pay off the mortgage and supersede it, that mortgage is gone. You know, and then you are in line behind the second mortgage, which comes to the front.

Secretary DONOVAN. That is exactly why—

Senator SHELBY. Does that make sense?

Secretary DONOVAN. You are exactly right, and that is exactly why in a refinancing where the first mortgage is actually extinguished.

Senator SHELBY. Absolutely.

Secretary DONOVAN. That is where the second lien becomes an issue, and that is what we are focused on dealing with.

Senator SHELBY. It would come to the front, wouldn't it?

Secretary DONOVAN. Right.

Senator SHELBY. In the priority.

Secretary DONOVAN. Whereas a modification, the first stays in place, and it does not—the second has no right to supersede the first.

Senator SHELBY. It has to be done right, though. You will have some lawsuits. I think Senator Warner was alluding to that.

Senator WARNER. Right. And if we are going to do this, we have got to not just create this whole new legal pile of trouble.

Senator SHELBY. Oh, no.

Senator WARNER. And I also think you have got the issue even on the first mortgage, if it has been securitized and chopped up so much, the challenge of those most at risk, the first 2, or 5, or 20-percent holders—a different issue, but it has got huge issues, too, since you have got all the—that is where a lot of the side bets were placed.

Chairman DODD. And that is where the safe harbor, I think, is critical. Whereas, in this one, the modification versus the refinancing, I think it is pretty clear. If you are modifying, the safe harbor is really, I do not think, as necessary as the first situation we talked about. If you are refinancing, as Senator Shelby points out, then you have crossed over a line, and then clearly you have got a problem with the—

Secretary DONOVAN. But even with the modifications, there have been concerns on the part of the investors. That is why this guidance that we are going to do next week, which from Treasury applies to all financial institutions, is critical. The pooling and servicing agreements say the servicer has a responsibility to act on behalf of the whole trust, but we think this guidance will provide them very clear, specific support for their being able to modify, except in the most extreme cases where pooling and servicing agreements had unusual language, only about 10 percent or so.

Chairman DODD. Let me thank Senator Warner and Senator Shelby for raising this point. We have taken a little time on it, but it is very worthwhile to have this exchange.

Secretary DONOVAN. Very helpful, yes.

Chairman DODD. Senator Bennet, welcome.

Senator BENNET. Thank you, Mr. Chairman. I appreciate it, and I apologize for coming in on the tail end, so I will be—

Chairman DODD. Well, Senator Akaka is here, too.

Senator BENNET. I will be very brief. I first wanted to come because I always like to see a local government guy make good. So congratulations, Mr. Secretary, on your confirmation, and I look forward to working with you.

I know there has been some discussion this morning about proactively communicating with our citizens on this, and I just want to underscore from my point of view how important that is. We in Colorado are fifth, we think, in foreclosures in the country by some measures, which is nothing to write home about, but we used to be first. And we have started to see these foreclosures decrease. The State a couple of years ago, with the cooperation of State, private enterprise, and nonprofits, put together a hotline I think along the lines of the one you are talking about, and what we have discovered is that four out of five of those calls resulted in something other than a foreclosure for the people that were call-

ing them. We think we roughly saved 4,200 homes by doing that. So I encourage you—and I know based on my travels during the recess that there is a profound lack of clarity out there about what it is we are trying to do. I want to congratulate the administration on your efforts here.

There was a reminder in the President's speech this week about how comprehensive these issues are, that it is not just one thing, there is not one silver bullet to deal with it.

I also know you testified that as this proceeds, you will continue to re-evaluate whether the program is being effective or not. And I would love it if you could tell us a little more about what kinds of triggers you are going to look at to assess progress with this plan and what sorts of metrics we should be thinking about as we evaluate your success.

Secretary DONOVAN. Well, obviously, the long-term metric on this is what happens in the housing market and can we help it to turn around. So clearly what this is aimed at is improving the housing market for everybody, not just those homeowners that are most at risk, but recognizing the terrible impact that foreclosure is having on everybody's home value in the country. So that is the long-term metric.

I think in the shorter term, we are going to be looking very carefully with the data we get back from the servicers and the auditing and other things that we are going to be doing, first of all, what do we see in terms of modifications increasing, and we certainly expect that that would lead to fewer foreclosures, so looking at the rate of foreclosures and what is going to happen there.

It is also going to be the quality of the modifications and how long they last, making sure that people have verified income, that we are getting to the 31-percent debt-to-income ratio. We have seen lots of modifications, frankly, where payments are required to go up rather than down, and so it is not just a modification. It is the right kind of modification, and the program sets very strong standards on that. We will be measuring to make sure that servicers are meeting that, that they are checking income adequately.

And then also to see how long those modifications last, that they are successful. One of the things that we think we have certainly tried to do and we hope we have got right is to pay for success rather than failure. So instead of guaranteeing any loss, which only happens with a redefault, we structured our payments so that if it only lasts 6 months, the modification, well, you only get the payment for those 6 months. If it last 5 years, you get a much more significant contribution. So we think we have structured it to pay for success, and we want to make sure that we see the redefault rates come down and that we have as many homeowners who can succeed with these modifications as possible.

So I think those are the key metrics we will be looking at.

Senator BENNET. Thank you, Mr. Chairman.

Chairman DODD. Thank you very much, Senator.

Senator AKAKA.

Senator AKAKA. Thank you very much, Mr. Chairman.

Let me add my welcome to Secretary Donovan to this Committee again. I remember your lovely family when you were here earlier. But I want to let you know that I really appreciate your efforts in

helping assist struggling families in trying to remain in their homes. I am impressed with your responses and look forward to continuing to work with you.

Secretary DONOVAN. Thank you.

Senator AKAKA. Let me be more focused on my concern in my questions, and that is, implementing housing policy in Native American communities and on trust land which often requires unique and innovative approaches.

Secretary Donovan, my question to you is: What will be done to assist homeowners in Native American, Native Hawaiian, Alaska Native communities?

Secretary DONOVAN. Well, first of all—and I think we started talking about this a little bit before—outreach and education on this issue is absolutely key. A national number, I will say it again at the risk of repeating myself, 888-995-HOPE, anyone anywhere in the country can call and get information, go on HUD's Web site, *www.hud.gov*, and get information about what is available, the options that are available.

We had a very good discussion yesterday with lots of counseling agencies and others who made it very clear ensuring broad geographic outreach, different languages, a whole range of things that we need to do to make sure that we are getting the word out as comprehensively as possible.

And then beyond that, what I would say in particular, there are a range of things we need to do for Native Americans, for Native Hawaiians. One of the things about the recovery bill that I think was so important is it recognized that. And, in fact, just yesterday we announced allocations of \$255 million for Native American block grant funding, and I believe it is \$10 million for Native Hawaiian funding. So we got that out within a week after the President signed the bill, and so those communities will know what they have available. They can come on in and start to sign the contracts to actually obligate that money in the next 30 days.

So those are some things I would say about dealing specifically with the issues in those communities.

Senator AKAKA. Well, thank you for that, Secretary. I appreciated your comments on that.

Let me then point to some loans on VA. In addition to serving on this Committee, I am Chairman of the Veterans Affairs Committee. The Department of Veterans' Affairs administers a successful home loan guarantee program. Lenders have expressed concern, however, about the possibility that the cramdown proposal may negatively impact VA's home loan guarantee program.

My question to you is: What will be done to mitigate any potential negative consequences that the proposal may have on the VA loan guarantee program?

Secretary DONOVAN. Excellent question, Senator. I am very glad you brought that up because it is something I had not mentioned before, but it is a critical issue.

Because of the way FHA insurance and VA insurance have been structured, whether it is in bankruptcy or even in a loan modification, there is not current authority to be able to pay partial claims in those situations. And so in addition to the changes for Hope for Homeowners, we have been working on language with the Commit-



tees here that would allow FHA and VA to pay partial claims in modifications as well as in bankruptcy that would ensure that lenders, when they made a loan relied on the full faith and credit of the U.S. Government can actually—can rely on that in those situations. So that is an important part of the legislative language that we have been working on with the Committees.

Senator AKAKA. Well, I appreciated your thoughtful comments, again, about this. And during your nomination hearing, the need to incorporate education in the home loan process, we talked about this. And I know that the Homeowner Affordability and Stability Plan focused on keeping mortgage rates low, supporting refinancing efforts, and assisting at-risk homeowners as we work to develop longer-term policies to better educate and empower prospective homeowners.

My question to you is: How should education be incorporated into the home-buying process? You mentioned outreach. You even gave the 888-995-HOPE. Are there other matters that we can think of in helping in the home-buying process?

Secretary DONOVAN. Very important question, and we do have to remind ourselves, I think, in the midst of this crisis that we need to look forward and, as I said earlier, get back to the basics in terms of lending. In New York, we had a program to create and preserve homeownership where we helped over 17,000 families, and we only had five foreclosures in that program. And the reason for that is because we did the education. We made sure it was affordable. We made sure the loan terms were acceptable. You know, really the basics. And education is an important part of that.

I think you will see—the President is releasing the first information about our budget proposal for 2010 today, and I think you will see that counseling is an important part of efforts going forward. HUD-approved counselors around the country are a critical resource, not just for helping work out foreclosures, but also for first-time homebuyers or homebuyers getting into a home to make sure that they are getting the right mortgage products, that they are prepared for homeownership. And I think that is a key thing we have got to focus on going forward as well.

Senator AKAKA. Thank you. Thank you very much for your excellent responses.

Mr. Chairman, thank you.

Chairman DODD. Senator Akaka, thank you very much, and as you will discover, if you have not already, Mr. Secretary, Senator Akaka has had—for as long as he has been on this Committee, and I suspect even pre-dating it—a deep interest in financial literacy issues, and we have talked about it extensively here. It is something we really need to focus on. I often wish that even at public elementary schools they would begin just teaching at the earliest grades math and so forth by utilizing examples of just balancing checkbooks and things like that. It could be helpful. I have often said as well, too—and I say this respectfully to all of us here—that a little financial literacy might even begin here. I say that respectfully to my colleagues, but I think we all appreciate that we do the best we can, but these are subject matters that all of us as lay people—most of us lay people—try to get our arms around to under-

stand as well as we should. And so I thank Senator Akaka for his deep interest in that subject matter.

Senator Merkley had some additional questions.

Senator MERKLEY. Thank you very much, Mr. Chair.

Secretary Donovan, thank you so much for your testimony. Your thorough knowledge of the topic and the details is refreshing and gives us a lot of confidence in the work that you are going to be doing.

Secretary DONOVAN. Thank you.

Senator MERKLEY. I wanted to put in one request with you as you go forward, and that is, in regard to the hotline that is being set up or has been set up, if it is possible to expand it beyond simply a description of existing programs, if you will, when folks calls, if they are able to be able to talk to a real person, if they are able to say, "I have a loan that is serviced by so-and-so. How can I get through to somebody ready to talk about renegotiation?" so that they can get through to a real person on the servicer end and bypass what will be numerous days, numerous hours of frustration, is there any way to utilize that hotline in a way to really help connect people to the servicers and to action. It would be a huge, just a monumental service to the homeowners of America.

Secretary DONOVAN. I could not agree more, and in the discussions that we have been having, we are trying to make sure that that centralized hotline can connect folks up to the servicers as well as counseling agencies in their neighborhoods that can help them stay in their homes and get the assistance they need. You are absolutely right.

Senator MERKLEY. Thank you so much.

Chairman DODD. Senator Shelby, any closing thoughts?

Senator SHELBY. I just want to tell the Secretary again we welcome him here. We look forward to working with you. We know you have great challenges, but we think you have the energy and you have got a great background, and I think you will be before this Committee a lot, and we will always welcome you back.

Secretary DONOVAN. I look forward to it. Thank you.

Chairman DODD. Let me echo those words as well, Secretary Donovan. You have been very impressive this morning. And on the Hope for Homeowners, I know you are doing this, but I will just publicly—we need to get as much information because, to the extent we can go back and make some fixes to that so it can work as well as we would all like it to, it would be very, very helpful. Senator Shelby and I would like to get that as early as we can, to the extent we can bring our members together, get around some of these ideas, and then go to our respective leaders, assuming we can reach that kind of understanding, which I believe we can, so that we can go forward and bring some of these matters up for the consideration of our colleagues on the floor of the Senate, it would be very helpful. There is a sense of urgency, obviously, in getting this stuff in place, so we would ask you to do that.

And, second, we have got other issues we need to talk about with you as well as obviously foreclosure issues, a lot of issues dealing with housing, and related matters of transit. This Committee has jurisdiction over urban mass transit issues. The surface transportation bill is going to come up this year, and so that is going to be

a matter which I am going to want to engage you in, along with the Secretary of Energy, the Secretary of Transportation, the Secretary of even Health to some degree, talk about how we might do a better job of coordinating these questions when it comes to surface transportation issues, where housing and energy, obviously transport, and environmental question—I said “health.” I meant environmental issues—can really come together and we get a working group on this so we think about it more holistically than just transit questions but, rather, how they interrelate with each other. And I know you have done a lot of work on that. I was very impressed in our conversation about your full understanding of that holistic approach to this question. So I am going to really draw upon those years of experience you have brought to the subject matter already.

Senator Shelby had a comment.

Senator SHELBY. Just along the same lines, the Secretary I am sure knows very well we have about—on transit-related stuff, about 20 percent of the highway budget, I believe, of the whole thing. So we will need to engage you because this Committee is going to be very active there.

Chairman DODD. And a lot of interest in the subject matter today. This is no longer just an East Coast–West Coast thing, but now places like Utah and Nevada and Idaho and—

Senator SHELBY. And Alabama.

Chairman DODD. Alabama, that is right, with the concentrations in urban areas. A great trivia question is which is the most urbanized State in America, and people are inclined to maybe say New York or Connecticut or Illinois or something. But the most urbanized State in the country is Nevada with the largest concentration of population in one county, and so we have a tendency to think of the West is not in need of transit issues in the past, but clearly the whole country needs to focus on this.

So I did not mean to digress from the subject matter this morning, but I wanted to tell you how much I appreciate your service and look forward to working with you.

Secretary DONOVAN. Thank you. And we have been doing some thinking around the budget, you know, based on our conversation and others, about how we can begin to do that. I would also just say we have been working with your staff on—we have announced the intent to nominate Ron Sims as Deputy for HUD, and I think you will find—I hope you will find in the hearing that he is very knowledgeable on these issues. He has been a real leader around bringing transit together in King County in Washington State with housing and a whole range of issues and I think could be a terrific resource on doing this. I hope you will find the same when he comes before the Committee.

Chairman DODD. We will try to move on that.

Thank you very much for being with us.

Secretary DONOVAN. Thank you.

Chairman DODD. The Committee will stand adjourned.

[Whereupon, at 12:38 p.m., the hearing was adjourned.]

[Prepared statements and response to written questions supplied for the record follow:]

**PREPARED STATEMENT OF SHAUN DONOVAN**  
SECRETARY,  
DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT  
FEBRUARY 26, 2009

Mr. Chairman, Senator Shelby, and distinguished Members of the Committee, thank you for the opportunity to appear before you today.

Homeowners and communities throughout the country have been devastated by the economic crisis. Many responsible families, making their monthly payments, have experienced falling home values that disqualify them from opportunities to refinance with today's low interest rates. Millions of American workers have been laid off, or forced to accept less work, and are grasping at every resource possible to make their mortgage payments.

In the absence of action, over 6 million families could face foreclosure in the next few years, with millions more struggling to stay above water. In the absence of action, we would have seen an intensifying spiral of more lenders foreclosing, pushing nearby home prices even lower, and putting more families underwater. In fact, when a family loses their home to foreclosure, nearby homes drop in value as much as 9 percent, causing harm to every homeowner—even those who make every payment—when foreclosures in their community increase.

On February 18, President Obama announced the Homeowner Affordability and Stability Plan, a plan to make help available to as many as 7 to 9 million homeowners who are fighting hard to make their payments and stay in their homes. The Plan will not provide money to speculators. It will target support to the working homeowners who have made every possible effort to stay current on their mortgage payments. The Homeowner Affordability and Stability Plan is part of the President's comprehensive strategy to get the economy moving in the right direction. Just as the American Recovery and Reinvestment Act works to save or create several million new jobs and the Financial Stability Plan works to get credit flowing, the Homeowner Affordability and Stability Plan will support a recovery in the housing market and ensure that these workers can continue paying off their mortgages.

The plan not only helps responsible homeowners at risk of losing their homes, but prevents neighborhoods and communities from decay, as defaults and foreclosures fuel falling home values, local business collapses, and further job loss.

- First, encourage homeownership by helping keep mortgage rates low.
- Second, support for refinancing to up to 4 to 5 million responsible homeowners to make their mortgages more affordable.
- Third, launch a \$75 billion homeowner stability initiative to reach up 3 to 4 million at-risk homeowners.

To help keep mortgage rates low and promote stability and liquidity in the marketplace, the Treasury Department will continue to purchase Fannie Mae and Freddie Mac mortgage-backed securities. In addition, the Treasury Department will increase its funding commitment to Fannie Mae and Freddie Mac to ensure the strength and security of the mortgage market and to help maintain mortgage affordability. This backing will bolster confidence in the mortgage market, allowing Fannie Mae and Freddie Mac to continue to provide mortgage affordability for responsible homeowners.

As noted, mortgage rates are currently at historically low levels. But under current rules, only families with conforming loans owned or guaranteed by Fannie Mae or Freddie Mac who owe less than 80 percent of the value of their homes are eligible for refinancing to these low interest rates. Unfortunately, given the recent decline in home prices, millions of responsible homeowners who made down payments and timely mortgage payments are unable to access these lower rates. The President's plan will help as many as 4 to 5 million of these homeowners refinance to lower interest rates through Fannie Mae and Freddie Mac, by opening eligibility to borrowers who owe, on their mortgage, 80 to 105 percent of the current value of their home.

Finally, the President has announced an initiative to reach millions of responsible homeowners who are struggling to afford their mortgage payments. In the current economy, millions of hard-working families have seen their mortgage payments rise to 40 or even 50 percent of their monthly income—particularly if they received subprime and exotic loans with exploding terms and hidden fees. The Homeowner Stability Initiative operates through a partnership of lenders, servicers, borrowers, and the government to help responsible borrowers stay in their homes, providing families with security and neighborhoods with stability. Based on estimates of the effects of foreclosures on the value of nearby homes, the Homeowner Stability Initia-

tive could protect the owner of an average-valued home in the United States from as much as a \$6,000 decline in home values.

Homeowners with high mortgage debt compared to income may be eligible for a loan modification as long as their home mortgage does not exceed GSE conforming loan limits. Further, the increase in GSE conforming loan limits (up to \$729,750 in some high-cost areas) as enacted in the ARRA will allow more borrowers to qualify.

Significantly, this program will not require homeowners to be delinquent in their payments to qualify for eligibility. Loan modifications are more likely to succeed if they are made before a homeowner becomes delinquent; thus, the plan will include households at risk of imminent default despite having not yet missed a mortgage payment.

Borrowers with large non-housing debts can qualify, but only if they agree to enter HUD-certified counseling. Specifically, homeowners with total “back end” debt (which includes not only housing debt, but other debt including car loans and credit card debt) equal to 55 percent or more of their income will be required to agree to enter a counseling program as a condition for a modification.

The Homeowner Stability Initiative should reach up to 3 to 4 million at-risk borrowers in all segments of the mortgage market, reducing foreclosures, and helping to avoid further downward pressures on overall home prices. The program has several key components:

- First, the government will partner with lenders to reduce the homeowner’s monthly payment to an affordable level. The lender is solely responsible for interest rate reductions and other changes necessary to lower the borrower’s monthly mortgage payment to 38 percent of his or her income. From that point, the government will match, dollar for dollar, any additional reductions the lender makes to lower that ratio to 31 percent. These adjustments could mean a monthly mortgage payment lowered by more than \$400 for a borrower with a \$220,000 mortgage. The lower interest rate arrived at must be kept in place for 5 years, at which point it can be gradually increased to the conforming loan rate at the time of the modification. Lenders will also have an option of decreasing monthly payments by reducing the principal owed on the mortgage, with the government sharing those costs.
- Second, servicers will receive \$1,000 for each eligible modification meeting initiative guidelines. They will also receive fees to reward them for continued success-awarded monthly as long as the borrower stays current on the loan-of up to \$1,000 each year for 3 years.
- Third, to encourage borrowers to stay current, the initiative will provide a monthly principal balance reduction payment. As long as a borrower stays current on his or her loan, he or she can get up to \$1,000 each year for 5 years.
- Fourth, because loan modifications are more likely to be successful if they are made before a borrower misses a payment, to keep lenders focused on reaching borrowers who are trying to stay current on their mortgages, an incentive payment of \$500 will be paid to servicers, and an incentive payment of \$1,500 will be paid to mortgage holders, if they modify at-risk loans before the borrower misses a payment.
- Finally, to encourage lenders to modify more mortgages and enable more families to keep their homes, the Administration-together with the FDIC-has developed an innovative home price decline reserve payment. The fund—which may be as large as \$10 billion—will provide holders of mortgages modified under the program with an additional payment in the event that home price declines—and therefore the risk of losses in cases of default is higher than expected.

As mentioned earlier, the Homeowner Affordability and Stability Plan is not a self-contained initiative but is intended to work in conjunction with other efforts such as the American Recovery and Reinvestment Act and the Financial Stability Plan to provide a comprehensive and multifaceted response to the current economic troubles.

As part of the American Recovery and Reinvestment Act signed by the President, the Department of Housing and Urban Development will award \$2 billion in competitive Neighborhood Stabilization Program grants for innovative programs that mitigate the impact of foreclosures by supporting innovative strategies to address the problem of vacant, foreclosed properties. Additionally, the Act includes an additional \$1.5 billion to provide assistance to renters facing displacement, reducing homelessness and avoiding entry into shelters. HUD allocated that \$1.5 billion of homelessness prevention funding to recipients yesterday, as part of our successful allocation of three quarters of Recovery Act funds for HUD programs only a week after President Obama signed the Act into law.

In addition to the already mentioned efforts, the President's overall economic recovery plan will seek careful changes to personal bankruptcy provisions. The Administration will work with Congress to ensure that legislation works well in conjunction with our voluntary modification approach.

Finally, the Hope for Homeowners program offers one avenue for struggling borrowers to refinance their mortgages. In order to ensure that more homeowners participate, we support changes to the program that will reduce fees paid by borrowers, increase flexibility for lenders to modify troubled loans, permit borrowers with higher debt loads to qualify, and allow payments to servicers of the existing loans.

Thank you, and I look forward to your questions.

**THE WHITE HOUSE**

Washington

July 8, 2009

**Support Under the Homeowner Affordability and Stability Plan: Three Cases**

**Family A: Access to Refinancing**

- **In 2006:** Family A took a 30-year fixed rate mortgage of \$207,000 on a house worth \$260,000 at the time. (The family put just over 20% down.) They received a Fannie Mae conforming loan with an interest rate of 6.50%.
- **Today:** Family A has about \$200,000 remaining on their mortgage but their home value has fallen 15 percent to \$221,000.
  - Their "loan-to-value" ratio is now 90%, **making them ineligible for a Fannie Mae refinancing.**
- **Under the Refinancing Plan:** Family A can refinance to a rate of 5.16%. **This would reduce their annual payments by nearly \$2,350.**

	<b>Existing Mortgage</b>	<b>Refinancing</b>
Balance	\$199,584	\$203,575
Remaining Years	27	30
Interest Rate	6.50%	5.16%
Monthly Payment	\$1,308	\$1,113
Savings		<b><i>\$196 per month, \$2,347 per year</i></b>

**Family B: Access to Refinancing**

- **In 2006:** Family B took a 30-year fixed rate mortgage of \$350,000 on a house worth \$475,000 at the time. (The family put just over 26% down.) They received a Fannie Mae conforming loan with an interest rate of 6.50%.
- **Today:** Family B has about \$337,460 remaining on their mortgage but their home value has fallen to \$400,000.
  - Their "loan-to-value" ratio is now 84%, **making them ineligible for a Fannie Mae refinancing.**
- **Under the Refinancing Plan:** Family B can refinance to a rate of 5.16%. **This would reduce their annual payments by nearly \$4,000.**

	<b>Existing Mortgage</b>	<b>Refinancing</b>
Balance	\$337,460	\$344,210
Remaining Years	27	30
Interest Rate	6.50%	5.16%
Monthly Payment	\$2,212	\$1,882
Savings		<b><i>\$331 per month, \$3,968 per year</i></b>

## THE WHITE HOUSE

Washington

July 8, 2009

**Family C: Eligible for Homeowner Stability Initiative**

- **In 2006:** Family C took out a 30-year subprime mortgage of \$220,000, on a house worth \$230,000 at the time (they put less than 5% down). Their mortgage broker – Mom & Pop Mortgage – sold their loan to Investment Bank. The interest rate on their mortgage is 7.5%.
- **Today:** Family C has \$214,016 remaining on their mortgage but their home value has fallen -18% to \$189,000. Also, in November, one parent in Family C was moved from full-time to part-time work, causing a significant negative shock to their income.
  - *Their loan is now 113% the value of their home, making them “underwater” and unable to sell their house.*
  - *Meanwhile, their monthly mortgage payment is \$1,538 and their monthly income has fallen to \$3,650, meaning the ratio of their monthly mortgage debt to income is 42%.*
- **Under the Homeowner Stability Initiative:** Family C can get a government sponsored modification that – for five years – will reduce their mortgage payment by \$406 a month. After those five years, Family C’s mortgage payment will adjust upward at a moderate, phased-in level.

	Existing Mortgage	Loan Modification
<b>Balance</b>	\$213,431	\$213,431
<b>Remaining Years</b>	27	27
<b>Interest Rate</b>	7.50%	4.42%
<b>Monthly Payment</b>	\$1,538	\$1,132
<b>Savings:</b>	<i>\$406 per month, \$4,870 per year</i>	

**Homeowner Stability Initiative: How the Program Works for the Lender, Government and Borrower**

- First, Investment Bank (working through a mortgage servicer) **reduces the interest rate so that the Family C’s monthly debt-to-income ratio drops** from 42% to 38%. This means that Investment Bank must reduce the interest rate from 7.50% to 6.38%, bringing down Family C’s monthly payment from \$1,538 to \$1,387.
- Second, the government and Investment Bank **share the cost of further reducing the interest rate** so that the Family C’s monthly debt-to-income level is lowered to 31%. Any dollar the bank spends is matched by the government. At this stage, Family C’s interest rate is reduced from 6.41% to 4.43%. In total, Family C’s monthly payment has fallen from \$1,538 to \$1,132.
- If Family C remains current on their payments, they will receive **incentive payments** up to \$1,000 a year, or \$5,000 over five years, that would go towards reducing the principal they owe. Additionally, the mortgage servicer can earn an up-front incentive fee of \$1,000, plus up to \$1,000 per year in “Pay for Success” fees for three years, so long as Family C remains current.

### HOMEOWNER AFFORDABILITY AND STABILITY PLAN

The deep contraction in the economy and in the housing market has created devastating consequences for homeowners and communities throughout the country. Millions of responsible families who make their monthly payments and fulfill their obligations have seen their property values fall, and are now unable to refinance to lower mortgage rates. Meanwhile, millions of workers have lost their jobs or had their hours cut, and are now struggling to stay current on their mortgage payments. As a result, as many as 6 million families are expected to face foreclosure in the next several years, with millions more struggling to stay current on their payments.

The present crisis is real, but temporary. As home prices fall, demand for housing will increase, and conditions will ultimately find a new balance. Yet in the absence of decisive action, we risk an intensifying spiral in which lenders foreclose, pushing home prices still lower, reducing the value of household savings, and making it harder for all families to refinance. In some studies, foreclosure on a home has been found to reduce the prices of nearby homes by as much as 9 percent—creating the potential that even borrowers who make every payment suffer from an increase in foreclosures in their community.

The Obama Administration's Homeowner Affordability and Stability Plan will offer assistance to as many as 7 to 9 million homeowners making a good-faith effort to stay current on their mortgage payments, while attempting to prevent the destructive impact of foreclosures on families and communities. It will not provide money to speculators, and it will target support to the working homeowners who have made every possible effort to stay current on their mortgage payments. Just as the American Recovery and Reinvestment Act works to save or create several million new jobs and the Financial Stability Plan works to get credit flowing, the Homeowner Affordability and Stability Plan will support a recovery in the housing market and ensure that these workers can continue paying off their mortgages.

By supporting low mortgage rates by strengthening confidence in Fannie Mae and Freddie Mac, providing up to 4 to 5 million homeowners with new access to refinancing and enacting a comprehensive stability initiative to offer reduced monthly payments for up to 3 to 4 million at-risk homeowners, this plan—which draws off the best ideas developed within the Administration, as well as from Congressional housing leaders and Federal Deposit Insurance Corporation Chair Sheila Bair—brings together the government, lenders and borrowers to share responsibility towards ensuring working Americans can afford to stay in their homes.

#### **Provide Access to Low-Cost Refinancing for Responsible Homeowners Suffering From Falling Home Prices**

- **Provide the Opportunity for Up to 4 to 5 Million Responsible Homeowners Expected to Refinance:** Mortgage rates are currently at historically low levels, providing homeowners with the opportunity to reduce their monthly payments by refinancing. But under current rules, most families who owe more than 80 percent of the value of their homes have a difficult time securing refinancing. (For example, if a borrower's home was worth \$200,000, he or she would have limited refinancing options if he or she owed more than \$160,000.) Yet millions of responsible homeowners who put money down and made their mortgage payments on time have—through no fault of their own—seen the value of their homes drop low enough to make them unable to access these lower rates. As a result, the Obama Administration is announcing a new program that will provide the opportunity for 4 to 5 million responsible homeowners who took out conforming loans owned or guaranteed by Freddie Mac and Fannie Mae to refinance through the two institutions over time.
- **Reducing Monthly Payments:** For many families, a low-cost refinancing could reduce mortgage payments by thousands of dollars per year. For example, consider a family that took a 30-year fixed rate mortgage of \$207,000 with an interest rate of 6.50 percent on a house worth \$260,000 at the time. Today, that family has \$200,000 remaining on their mortgage, but the value of that home has fallen 15 percent to \$221,000—making them ineligible for today's low interest rates that generally require the borrower to have 20 percent home equity. Under this refinancing plan, that family could refinance to a rate near 5.16 percent—reducing their annual payments by over \$2,300.

#### **A \$75 Billion Homeowner Stability Initiative To Prevent Foreclosures and Help Responsible Families Stay in Their Homes**

The Treasury Department, working with the GSEs, FHA, the FDIC and other federal agencies, will undertake a comprehensive multi-part strategy to prevent mil-



lions of foreclosures and help families stay in their homes. This strategy includes the following six features:

- A Homeowner Stability Initiative To Reach Up to 3 to 4 Million At-Risk Homeowners
- Clear and Consistent Guidelines for Loan Modifications
- Requiring That Financial Stability Plan Recipients Use Guidance for Loan Modifications
- Allowing Judicial Modifications of Home Mortgages During Bankruptcy When A Borrower Has No Other Options
- Require Strong Oversight, Reporting and Quarterly Meetings With Treasury, the FDIC, the Federal Reserve and HUD To Monitor Performance
- Strengthening FHA Programs and Providing Support for Local Communities

*A Homeowner Stability Initiative To Reach Up to 3 to 4 Million At-Risk Homeowners*

This initiative is intended to reach millions of responsible homeowners who are struggling to afford their mortgage payments because of the current recession, yet cannot sell their homes because prices have fallen so significantly. In the current economy, in which 3.6 million jobs have been lost over the past 14 months, millions of hard-working families have seen their mortgage payments rise to 40 or even 50 percent of their monthly income—particularly if they received subprime and exotic loans with exploding terms and hidden fees. The Homeowner Stability Initiative operates through a shared partnership to temporarily help those who commit to make reasonable monthly mortgage payments to stay in their homes, providing families with security and neighborhoods with stability. This plan will also help to stabilize home prices for homeowners in neighborhoods hardest hit by foreclosures. Based on estimates concerning the relationship between foreclosures and home prices, with the average house in the U.S. valued around \$200,000, the average homeowner could see his or her home value stabilized against declines in price by as much as \$6,000 relative to what it would otherwise be absent the Homeowner Stability Initiative.

Who the Program Reaches:

- Focusing on Homeowners At Risk: Anyone with high combined mortgage debt compared to income or who is “underwater” (with a combined mortgage balance higher than the current market value of his house) may be eligible for a loan modification. This initiative will also include borrowers who show other indications of being at risk of default. Eligibility for the program will sunset at the end of 3 years.
- Reaching Homeowners Who Have Not Missed Payments: Delinquency will not be a requirement for eligibility. Rather, because loan modifications are more likely to succeed if they are made before a borrower misses a payment, the plan will include households at risk of imminent default despite being current on their mortgage payments.
- Common Sense Restrictions: Only owner-occupied homes qualify; no home mortgages larger than the Freddie/Fannie conforming limits will be eligible. This initiative will go solely to supporting responsible homeowners willing to make payments to stay in their home—it will not aid speculators or house flippers.
- Special Provisions for Families With High Total Debt Levels: Borrowers with high total debt qualify, but only if they agree to enter HUD-certified consumer debt counseling. Specifically, homeowners with total “back end” debt (which includes not only housing debt, but other debt including car loans and credit card debt) equal to 55 percent or more of their income will be required to agree to enter a counseling program as a condition for a modification.

How the Program Works:

- The Homeowner Stability Initiative has a simple goal: reduce the amount homeowners owe per month to sustainable levels. This program will bring together lenders, servicers, borrowers, and the government, so that all stakeholders share in the cost of ensuring that responsible homeowners can afford their monthly mortgage payments—helping to reach up to 3 to 4 million at-risk borrowers in all segments of the mortgage market, reducing foreclosures, and helping to avoid further downward pressures on overall home prices. The program has several key components:
  - Shared Effort To Reduce Monthly Payments: Treasury will partner with financial institutions to reduce homeowners’ monthly mortgage payments.

- The lender will have to first reduce interest rates on mortgages to a specified affordability level (specifically, bring down rates so that the borrower's monthly mortgage payment is no greater than 38 percent of his or her income).
- Next, the initiative will match further reductions in interest payments dollar-for-dollar with the lender, down to a 31-percent debt-to-income ratio for the borrower.
- To ensure long-term affordability, lenders will keep the modified payments in place for 5 years. After that point, the interest rate can be gradually stepped-up to the conforming loan rate in place at the time of the modification. Note: Lenders can also bring down monthly payments to these affordability targets through reducing the amount of mortgage principal. The initiative will provide a partial share of the costs of this principal reduction, up to the amount the lender would have received for an interest rate reduction.
- "Pay for Success" Incentives to Servicers: Servicers will receive an up-front fee of \$1,000 for each eligible modification meeting guidelines established under this initiative. Servicers will also receive "pay for success" fees—awarded monthly as long as the borrower stays current on the loan—of up to \$1,000 each year for 3 years.
- Responsible Modification Incentives: Because loan modifications are more likely to succeed if they are made before a borrower misses a payment, the plan will include an incentive payment of \$1,500 to mortgage holders and \$500 for servicers for modifications made while a borrower at risk of imminent default is still current.
- Incentives to Help Borrowers Stay Current: To provide an extra incentive for borrowers to keep paying on time under the modified loan, the initiative will provide a monthly balance reduction payment that goes straight towards reducing the principal balance on the mortgage loan. As long as the borrower stays current on his or her payments, he or she can get up to \$1,000 each year for 5 years.
- Home Price Decline Reserve Payments: To encourage lenders to modify more mortgages and enable more families to keep their homes, the Administration—together with the FDIC—has developed an innovative partial guarantee initiative. The insurance fund—to be created by the Treasury Department at a size of up to \$10 billion—will be designed to discourage lenders from opting to foreclose on mortgages that could be viable now out of fear that home prices will fall even further later on. This initiative provides lenders with the security to undertake more mortgage modifications by assuring that if home price declines are worse than expected, they have reserves to fall back on. Holders of mortgages modified under the program would be provided with an additional insurance payment on each modified loan, linked to declines in the home price index. These payments could be set aside as reserves, providing a partial guarantee in the event that home price declines—and therefore losses in cases of default—are higher than expected.

#### How It Will Be Effective:

- Protecting Taxpayers: To protect taxpayers, the Homeowner Stability Initiative will focus on sound modifications. If the total expected cost of a modification for a lender taking into account the government payments is expected to be higher than the direct costs of putting the homeowner through foreclosure, that borrower will not be eligible. For those borrowers unable to maintain homeownership, even under the affordable terms offered, the plan will provide incentives to encourage families and lenders to avoid the costly foreclosure process and minimize the damage that foreclosure imposes on lenders, borrowers and communities alike. Moreover, Treasury will not provide subsidies to reduce interest rates on modified loans to levels below 2 percent.
- Counseling and Outreach To Maximize Participation: Under the plan, the Department of Housing and Urban Development will also make available funding for non-profit counseling agencies to improve outreach and communications, especially to disadvantaged communities and those hardest-hit by foreclosures and vacancies.
- Creating Proper Oversight and Tracking Data To Ensure Program Success: Fannie Mae and Freddie Mac will be responsible—subject to Treasury's oversight and the Federal Housing Finance Agency's conservatorship—for moni-

toring compliance by servicers with the program. Every servicer participating in the program will be required to report standardized loan-level data on modifications, borrower and property characteristics, and outcomes. The data will be pooled so the government and private sector can measure success and make changes where needed. Treasury will meet quarterly with the FDIC, the Federal Reserve, the Department of Housing and Urban Development and the Federal Housing Finance Agency to ensure that the program is on track to meeting its goals.

- **Limiting the Impact of Foreclosure When Modification Doesn't Work:** Lenders will receive incentives to take alternatives to foreclosures, like short sales or taking of deeds in lieu of foreclosure. Treasury will also work with the GSEs to provide data on foreclosed properties to streamline the process of selling or redeveloping them, thereby ensuring that they do not remain vacant and unsold.

*Clear and Consistent Guidelines for Loan Modifications*

A lack of common standards has limited loan modifications, even when they are likely to both reduce the chance of foreclosure and raise the value of the securities owned by investors. Mortgage servicers—who should have an interest in instituting common-sense loan modifications—often refrain from doing so because they fear lawsuits. Clear and consistent guidelines for modifications are a key component of foreclosure prevention.

- **Developing Clear and Consistent Guidelines for Loan Modifications:** Working with the FDIC, other federal banking and credit union regulators, the FHA and the Federal Housing Finance Agency, the Administration is in process of developing guidelines for sustainable mortgage modifications for all federal agencies and the private sector—bringing order and consistency to foreclosure mitigation. The guidelines will include detailed protocols for loss mitigation as well for identifying borrowers at risk of default; the Administration expects to announce these guidelines by Wednesday, March 4.
- **Applying Guidelines Across Government and the Private Sector:** Treasury will develop uniform guidance for loan modifications across the mortgage industry by working closely with the FDIC and other bank agencies and building on the FDIC's pioneering role in developing a systematic loan modification process last year. The Guidelines—to be posted online—will be used for the Administration's new foreclosure prevention plan. Moreover, all financial institutions receiving Financial Stability Plan financial assistance going forward will be required to implement loan modification plans consistent with Treasury guidance. Fannie Mae and Freddie Mac will use these guidelines for loans that they own or guarantee, and the Administration will work with regulators and other federal and state agencies to implement these guidelines across the entire mortgage market. The agencies will seek to apply these guidelines when permissible and appropriate to all loans owned or guaranteed by the federal government, including those owned or guaranteed by Ginnie Mae, the Federal Housing Administration, Treasury, the Federal Reserve, the FDIC, Veterans' Affairs and the Department of Agriculture. In addition, these guidelines will apply to loans owned or serviced by insured financial institutions supervised by the Office of the Comptroller of the Currency, the Office of Thrift Supervision, the Federal Reserve, the Federal Deposit Insurance Corporation and the National Credit Union Administration.

*Requiring All Financial Stability Plan Recipients To Use Guidance for Loan Modifications*

As announced last week, the Treasury Department will require all Financial Stability Plan recipients going forward to participate in foreclosure mitigation plans consistent with Treasury's loan modification guidelines.

*Allowing Judicial Modifications of Home Mortgages During Bankruptcy for Borrowers Who Have Run Out of Options*

The Obama administration will seek careful changes to personal bankruptcy provisions so that bankruptcy judges can modify mortgages written in the past few years when families run out of other options.

- **How Judicial Modification Works:** When an individual enters personal bankruptcy proceedings, his mortgage loans in excess of the current value of his property will now be treated as unsecured. This will allow a bankruptcy judge to develop an affordable plan for the homeowner to continue making payments. To receive judicial modifications in bankruptcy, homeowners must first ask

their servicers/lenders for a modification and certify that they have complied with reasonable requests from the servicer to provide essential information. This provision will apply only to existing mortgages under Fannie Mae and Freddie Mac conforming loan limits, so that millionaire homes don't clog the bankruptcy courts.

- **Bolster FHA and VA Authority to Protect Investors and Ensure Loan Modifications Occur:** Legislation will provide the FHA and VA with the authority they need to provide partial claims in the event of bankruptcy or voluntary modification so that holders of loans guaranteed by the FHA and VA are not disadvantaged.

*Strengthening FHA Programs and Providing Support for Local Communities*

- **Ease Restrictions in Federal Housing Administration Programs, Including Hope for Homeowners:** The Hope for Homeowners program offers one avenue for struggling borrowers to refinance their mortgages. In order to ensure that more homeowners participate, the FHA will reduce fees paid by borrowers, increase flexibility for lenders to modify troubled loans, permit borrowers with higher debt loads to qualify, and allow payments to servicers of the existing loans.
- **Strengthening Communities Hardest Hit by the Financial and Housing Crises:** As part of the recovery plan signed by the President, the Department of Housing and Urban Development will award \$2 billion in competitive Neighborhood Stabilization Program grants for innovative programs that reduce foreclosure. Additionally, the recovery plan includes an additional \$1.5 billion to provide renter assistance, reducing homelessness and avoiding entry into shelters.

**Support Low Mortgage Rates By Strengthening Confidence in Fannie Mae and Freddie Mac**

- **Ensuring Strength and Security of the Mortgage Market:** Today, using funds already authorized in 2008 by Congress for this purpose, the Treasury Department is increasing its funding commitment to Fannie Mae and Freddie Mac to ensure the strength and security of the mortgage market and to help maintain mortgage affordability.
  - **Provide Forward-Looking Confidence:** The increased funding will enable Fannie Mae and Freddie Mac to carry out ambitious efforts to ensure mortgage affordability for responsible homeowners, and provide forward-looking confidence in the mortgage market.
  - Treasury is increasing its Preferred Stock Purchase Agreements to \$200 billion each from their original level of \$100 billion each.
- **Promoting Stability and Liquidity:** In addition, the Treasury Department will continue to purchase Fannie Mae and Freddie Mac mortgage-backed securities to promote stability and liquidity in the marketplace.
- **Increasing the Size of Mortgage Portfolios:** To ensure that Fannie Mae and Freddie Mac can continue to provide assistance in addressing problems in the housing market, Treasury will also be increasing the size of the GSEs' retained mortgage portfolios allowed under the agreements—by \$50 billion to \$900 billion—along with corresponding increases in the allowable debt outstanding.
- **Support State Housing Finance Agencies:** The Administration will work with Fannie Mae and Freddie Mac to support state housing finance agencies in serving homebuyers.
- **No EESA or Financial Stability Plan Money:** The \$200 billion in funding commitments are being made under the Housing and Economic Recovery Act and do not use any money from the Financial Stability Plan or Emergency Economic Stabilization Act/TARP.

**RESPONSE TO WRITTEN QUESTIONS OF SENATOR KOHL  
FROM SHAUN DONOVAN**

**Q.1.** One of the major problems homeowners have been facing is getting in touch with their lender. In the new plan, homeowners are urged to contact their lender to determine eligibility. Are lenders going to be engaging in outreach to homeowners who are eligible for modifications or refinancing?

**A.1.** There are a number of different outreach activities that servicers are engaged in to contact distressed borrowers and provide information about the Making Homes Affordable Program. Many servicers participate in homeowner outreach activities in collaboration with the Hope Now Alliance, State and local governments and HUD-approved counseling agencies. For example, the Hope Now Alliance hosts foreclosure prevention events across the country and servicers actively participate with representatives that meet one-on-one with homeowners to help determine what are the best options to meet their needs. Also, servicers are actively engaged in letter writing campaigns to homeowners at risk of losing their homes which include information on the Making Home Affordable Program.

HUD is also working in partnership with Treasury and Fannie Mae and Freddie Mac to coordinate outreach to homeowners on the Making Home Affordable Program. For example nationwide outreach events are being organized with special emphasis on events in high default/foreclosure areas. FHA is assembling a team of senior staff members around the country who are trained on the details of the Making Home Affordable Program and will make presentations at borrower outreach events. A National Education Campaign is also being launched which will include public service announcements for TV and radio and in both English and Spanish. The purpose of the campaign will be to: educate borrowers on the new refinance and loan modification options; inform borrowers that counselors at HUD-approved agencies are available as trusted advisors and urge them to work with counselors; and how to avoid foreclosure rescue scams.

**Q.2.** The Administration has said that any financial institution which receives money from the Financial Stability Plan will have to participate in foreclosure mitigation plans. Does this requirement apply retroactively to institutions which have taken bailout money already? If not, are the Treasury and the Federal Reserve going to work with those institutions to remove troubled assets from their books so they can be modified?

**A.2.** The participation requirement is not retroactive. However, Treasury will work with all recipients to encourage participation. A separate plan to purchase assets from securitizations is being developed. It is premature to state what loans may be eligible for purchase.

**Q.3.** There are also very significant problems facing those who rent their homes. About one in eight households pays more than 50 percent of their income for housing. Hundreds of thousands of lower income Americans are on waiting lists for affordable rental housing, with little hope of their names being reached in the foreseeable future.

In light of these issues, and in light of the 10 percent and successful track record of the Low Income Housing Tax Credit in producing and preserving affordable rental housing, shouldn't the administration's plan also address incentives to re-invigorate investment in the housing credit program, which has seen a substantial reduction in investor activity over the past year?

**A.3.** The Department recognizes the need to better coordinate our multifamily rental housing programs with Low Income Housing Tax Credits to facilitate the production of more affordable rental housing. Specifically, in regards to FHA programs, prior to the passage of the Housing and Economic Recovery Act of 2008 (HERA), the Department took the following steps to address this need:

- Streamlining subsidy layering review requirements to expedite the approval of mortgage insurance applications by eliminating submission burden and duplicative reviews.
- Issuance of waiver authority to Multifamily Hubs permitting use of the Department's 223(f) program to facilitate developers' ability to obtain permanent financing for projects where construction has completed and the developer is unable to obtain conventional take-out financing. A number of these projects may have received equity from Low-Income Housing Tax Credits.
- Issuance of a Mortgagee Letter streamlining processing of FHA mortgage insurance applications when combined with Tax Credits. This Letter reduced upfront equity requirements and synchronized the FHA review process with the Tax Credit application and review process.
- Issuance of a Master Lease Policy in March 2008. Master Leases are a form of ownership structure used to fully leverage the benefits of LIHTCs, Historic Tax Credits and New Market Tax Credits. This guidance permits this form of ownership structure to be used in projects financed with the Department's mortgage insurance programs.

In addition to these steps, we are currently undertaking the following activities to improve coordination between multifamily rental housing programs and Low-Income Housing Tax Credits:

- Implementation of the 2008 Housing and Economic Recovery Act (HERA), which contained provisions to further streamline processing by eliminating Subsidy Layering Reviews and Cost Certification requirements for applications involving tax credits and by eliminating the requirement for Letters of Credit or any other form of security for the equity derived from LIHTCs for mortgage insurance applications.
- Establishment of a pilot program to demonstrate the effectiveness of streamlining FHA mortgage insurance applications with equity provided through Low-Income Housing Tax Credits.

The Department continues to explore ways to streamline and improve our Multifamily housing programs to make them work more effectively and efficiently with Low-Income Housing Tax Credits in order to encourage and maximize investor participation in the tax credit program.