H.R. 5579, THE EMERGENCY MORTGAGE LOAN MODIFICATION ACT OF 2008

HEARING

BEFORE THE

SUBCOMMITTEE ON CAPITAL MARKETS, INSURANCE, AND GOVERNMENT SPONSORED ENTERPRISES

OF THE

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U.S. HOUSE OF REPRESENTATIVES

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H.R. 5579, THE EMERGENCY MORTGAGE LOAN MODIFICATION ACT OF 2008

Tuesday, April 15, 2008

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON CAPITAL MARKETS,
INSURANCE, AND GOVERNMENT
SPONSORED ENTERPRISES,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 2:05 p.m., in room 2128, Rayburn House Office Building, Hon. Paul E. Kanjorski [chairman of the subcommittee] presiding.

Members present: Representatives Kanjorski, Sherman, Moore of Kansas, Miller, Scott, Davis of Tennessee, Donnelly; Hensarling, Castle, and Brown-Waite.

Also present: Representative Watt.

Chairman KANJORSKI. This hearing of the Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises will come to order.

Without objection, all members' opening statements will be made a part of the record.

Good afternoon. We meet today to examine H.R. 5579, the Emergency Mortgage Loan Modification Act of 2008.

I worked with Congressman Castle on revising his initial proposal and introducing this new bill. Nearly 6 percent of all loans on single family properties outstanding in the fourth quarter of 2007 were delinquent, which is the highest total delinquency rate in 20 years. Moreover, slightly more than 2 percent of the homes are already in the process of foreclosure. That is the highest level ever. These numbers, coupled with the general anxiety and unease brought on by the housing crisis and the ongoing credit crunch underscore the importance of this hearing and the need for our bipartisan legislation.

Many in Washington and throughout the country are preoccupied with playing the blame game and performing postmortems as to what caused the subprime fiasco. I believe that such exercises must wait for another day. We can try to figure out how it all went wrong some other time. The immediate problems faced by many borrowers demand our attention. The search for innovative solutions in an increasingly complex financial world should be our priority. This afternoon's hearing represents part of that search.

One of the main obstacles that we face in attempting to decrease the number of mortgage foreclosures is the reluctance of servicers to modify loans and conduct workouts because they fear investor lawsuits. The legislation under consideration today will provide servicers a safe harbor from legal challenges. If the servicers meet certain conditions, a safe harbor should embolden servicers to ramp up loan modifications. Without the fear of litigation, servicer efforts toward loss mitigation should also greatly increase.

Some contend that adoption of this legislation will result in the abrogation of existing contracts. In drafting this new legislation, however, we addressed these concerns and sought to create a bill that honors the terms of existing contracts. Those parties who remain opposed to loan modifications on these grounds should remember that rigid principles sometimes must yield to urgent solutions that demand immediate action. This situation is one such instance.

For every mortgage that does not fail but rather is saved by the servicer through loss mitigation, the value of the underlying loan pool should increase. After all, mortgages in foreclosure amount to much less than a modified loan. But more importantly, these modifications by the private sector will keep more families in their homes. To me, these benefits considerably outweigh the costs.

Some may, however, continue to question certain provisions of this bill in good faith and on fair grounds. My mind is by no means closed on these matters. If a better way exists to address this issue or to write this legislation, I want to hear it. This hearing provides us with a forum for a thoughtful exchange of ideas and, I hope, a productive series of questions and answers.

In closing, I look forward to hearing the thoughts of our witnesses on these matters. I also want to thank each of them for appearing. Their views will assist us as we navigate our way through this complicated situation.

We must act where we can to lessen the severity of this crisis. Moreover, we should do so in a way that respects the efficiency of the capital markets, but which is not afraid to find solutions to redress its excesses.

I yield back the balance of my time and recognize the gentleman from Delaware, Governor Castle, for an opening statement.

Mr. CASTLE. Mr. Chairman, first, thank you very much for holding this hearing today, first, and second, I agree with your comments entirely, that we need to be as open-ended as possible about whatever changes are necessary to put into effect what we all think is in the best interest of everybody, which is to deal with the mortgage crisis which we have in our country today. I am anxious to hear what our panelists have to say, so I will be brief.

The goal of this legislation has been straightforward from the very beginning to provide added assurance and thus safer legal footing for servicers modifying mortgage loans. To that end, it has been my belief that homeowners and investors alike could benefit by finding terms and conditions that would allow at-risk homeowners the opportunity to stay in their homes while providing the investors some rate of return on their investments.

Today's economic conditions are very challenging for both borrowers and investors. Borrowers didn't enter homeownership and the mortgage market in the expectation of losing their home, and investors purchased mortgage-backed securities with anticipated rates of return. That was then and this is now. All along, I worried that lawsuits could become a drag on the loan modification process, or worse, bring it to a complete stop. Thankfully, we have not seen that materialize.

However, the risk of that occurring still exists. In fact, the risk may be greater in the coming months as servicers move on to modify marginally more difficult loans.

In closing, Mr. Chairman, I want to thank you, Chairman Frank, and Deb Silberman of the committee staff for assistance with this bill. I look forward to the testimony and suggestions for further improvement from the servicer and investment witnesses.

Chairman KANJORSKI. Thank you very much, Mr. Castle. The gentleman from Georgia, Mr. Scott.

Mr. SCOTT. Thank you, Mr. Chairman. And I want to thank you, Mr. Chairman, and the ranking member for holding this important hearing. I am pleased that we have chosen to again address the mortgage meltdown and credit crunch in our markets, and as I have said repeatedly, I think it is very important that we move with the same urgency and aggressiveness to help homeowners and families as we have to help Wall Street and specifically Bear Stearns, which I concurred with.

There are 2.2 million homeowners in this country who could lose their homes in the next few years. Many people are just barely hanging on by their fingernails. This is a call to all involved that we have to work together in a hurry with great urgency to find positive ways and long-term solutions to those facing foreclosures. We must have a policy that is grounded on, first and foremost, keeping people in their homes. We have to refinance, we have to restructure, we have to do what is necessary to keep people in their homes.

I would like to know again, as I have asked before, why it has taken regulators, who were well aware of the subprime mortgage crisisand issue early on, long before it hit a peak, why it took them so long to act, despite the clear evidence of problems in the markets, evidence that was pointed out time and time again, if I may say so, Mr. Chairman, by this very committee in areas dealing with predatory lending, in areas dealing with extending credit to people who should not have gotten that credit, and in the lack of accountability and responsibility within the lending market.

As more and more of our creditors are now cracking down on certain lending practices, we must ensure that there are sound underwriting of these loans, and that sound underwriting on these loans is rewarded, and those players who continue to prey on individuals with predatory practices realize that there are consequences. We have to put them out of business, and we should ensure that credit continues to be available to those who qualify, and are feasible candidates for home loans, such as first-time buyers, lower income households, and African-American and other minority families and communities.

Not only are foreclosures causing problems for families financially, but they are placing undue pressures on city and local, municipal, and county services such as code enforcement. In my own district in Georgia, for example, there are certain neighborhoods with an inordinate number of foreclosures, and they have become magnets for crime. That is why we have to keep people in their homes. Vacant buildings bring about crime. They bring added downward pressures on local governments.

I am concerned about the foreclosure numbers in Georgia, especially. We have a high rate of foreclosures. We rank 8th in the Nation, and one or two of our counties are right there within the top 5 in terms of overall foreclosures and delinquencies.

We must be alert to economic indicators and I hope to hear today more detail about the risk of a prolonged housing slump and potential ideas and solutions to the problems.

I am very pleased that the Emergency Loan Modification Act will remove the legal liability roadblock for servicers that provide for specified loan modifications and workouts and will help borrowers to restructure and refinance their loans at a faster pace. That is the key, ladies and gentlemen: restructuring and refinancing at a faster pace with the underlying move at all costs to keep people in their homes.

Thank you very much, Mr. Chairman. I look forward to the distinguished witnesses and their testimony.

Chairman KANJORSKI. Thank you, Mr. Scott.

We now move to our witnesses, and without objection, all witnesses' written statements will be made a part of the record. Each of you will be recognized for a 5-minute summary of your testimony.

First, we have Mr. Ralph Daloisio of Natixis Structured Finance Group, testifying on behalf of the American Securitization Forum. We have reserved 5 minutes for you, sir.

STATEMENT OF RALPH DALOISIO, MANAGING DIRECTOR, NATIXIS STRUCTURED FINANCE GROUP, ON BEHALF OF THE AMERICAN SECURITIZATION FORUM

Mr. DALOISIO. Chairman Kanjorski, Congressman Castle, and distinguished members of the subcommittee, as chair of the investor committee of the American Securitization Forum, I have been asked to share my views on H.R. 5579.

I have reviewed a March 11th draft of the bill, and I can see great care was exercised in its construction. Those who were involved in this drafting should be commended for their thoughtfulness. There are, however, certain elements of the bill that give me pause, and I would like to share those with you today.

The bill establishes a standard of care for servicers when effecting mortgage loan modifications, or workout plans, and a safe harbor for performing a qualified loan modification, or workout plan, provided there are no specific contractual provisions to the contrary. The contractual standards to which the bill relates, the duties of servicers with respect to modifying or otherwise mitigating losses on distressed mortgage loans are typically established through general provisions and securitization contracts rather than specific ones. Though the provisions are often framed in general terms, they create legally enforceable expectations of conduct by the parties to whom the provisions pertain, including duties and responsibilities of servicers to investors when engaging in loss mitigation activities. To the extent the bill would supersede these general provisions, it would be, in effect, overruling the contracts.

Furthermore, the standard of care prescribed by the bill in its Section 2(a) may be weaker and less protective of investor interests than that found in most servicing contracts today, whereas the bill requires a servicer to compare the net present value of defaulted loan assuming foreclosure, with its net present value assuming modification. Typical servicing contracts require the net present value analysis to be performed across a wider range of modification and loss mitigation alternatives with the servicer being bound to choose action based on the alternative that maximizes MPV among the other alternatives, not just one of them.

Finally, the bill would protect servicers complying with its standard of care who grant a qualified loan modification, or workout plan. By designating one kind of loan modification over other kinds of loan modifications, the bill creates a clear incentive for servicers to make only the protected modifications rather than other modifications which might be more beneficial to the securitization trust and to investors. That incentive itself would be contrary to the contractual standard of care to which servicers are generally bound by their contracts and would again introduce the possibility of a legislative overruling of preexisting contractual provisions.

Overall, if the intent of the bill is to clarify the existing and customary contractual servicing standards and incentivize servicers to apply those standards to minimize losses and avoid foreclosures, I see nothing fundamentally wrong with that from an investor's perspective. If this is the case, then some relatively simple drafting revisions to the bill would better align its wording to its intent.

If, however, the intent is to replace the legal duties and commercial expectations of transaction parties with a different set of duties and expectations supplied by Congress, I am concerned that the passage of this bill would represent a de facto modification of existing contracts. Since all parties to a contract, including investors, rely on legal, valid, binding, and enforceable provisions of the governing contracts, any legislation that would dilute, amend, or modify such contractual obligations or prejudice how the obligor fulfills its obligations is considered by the American Securitization Forum and by a consensus of the investor constituency within the American Securitization Forum to represent dangerous policy.

Legislative intervention into otherwise valid legal contracts could potentially threaten the stability and predictable operation of the contractual legal framework supporting our capital markets system, and carried to its logical conclusion, could have a chilling effect on the willingness of investors to make investments in our markets.

Beyond the comments I have made, I would actually go so far as to question the premise and also the need for the bill. The underlying premise of the legislation appears to be the view that mortgage loan servicers are inhibited by a fear of investor lawsuits from doing more to avoid foreclosures. However, servicers are already reasonably well-protected from such lawsuits, since under typical servicing contracts, they are liable only if they are negligent in performing their duties. Usually, one of these duties is the duty to reduce losses by avoiding foreclosures wherever possible. I therefore generally believe that servicers have adequate legal protections for granting modifications and are uninhibited from doing so. The bill would neither change such duty nor would it allow servicers to avoid liability for their own negligence in performing that duty.

If there are cases where the servicers do need to minimize loss by avoiding foreclosure is not clearly established, then servicers and investors would have an alignment of interest in making the necessary amendments and would seemingly have sufficient economic motivation for doing so, especially since foreclosure is usually the most costly means of resolving a defaulting mortgage loan, it is in everyone's interest, including investors', to avoid foreclosures wherever possible and the damage that foreclosure is causing to our balance sheets and to our communities.

I hope that my comments here today will prove to be helpful to you, and I thank each of you for inviting me to share them and for taking the time to listen.

[The prepared statement of Mr. Daloisio can be found on page 28 of the appendix.]

Chairman KANJORSKI. Thank you very much, Mr. Daloisio.

Next we will hear from Mr. Robert E. Story, Jr., president of the Seattle Financial Group and vice chairman of the Mortgage Bankers Association.

Mr. Story.

STATEMENT OF ROBERT E. STORY, JR., PRESIDENT, SEATTLE FINANCIAL GROUP, AND VICE CHAIRMAN, MORTGAGE BANKERS ASSOCIATION, ON BEHALF OF THE MORTGAGE BANKERS ASSOCIATION (ABA)

Mr. STORY. Mr. Chairman, and Congressman Castle, thank you for the opportunity to appear before you. MBA appreciates your attention to this important issue, and in particular, we appreciate the work of Congressman Kanjorski and Congressman Castle. We are all focused on the same goal: keeping people in their homes.

H.R. 5579 would protect servicers from litigation risk if they engage in certain loss mitigation efforts. MBA identified litigation risk as a barrier to workouts some months ago, and we have been working as an industry to address this issue. We are focused on improving clarity between investors and servicers. Significant strides have already been made and continue to be made.

The industry formed HOPE NOW to help homeowners avoid foreclosure. We are funding counseling and promoting the HOPE NOW hotline for borrowers, 1–888–995–HOPE. We have improved and standardized our servicing practices.

The investor community has stepped up in many ways. For example, investors have created guidelines to define the term "foreseeable default" that helps us help more borrowers. This was a major advance. Many servicers have also instituted foreclosure pauses to help give borrowers and lenders more time to work out a solution that keeps borrowers in their homes.

These industry practices allow servicers to do to more to help borrowers. Nearly 1.2 million repayment plans and modifications were executed from July 2007 through February 2008, according to HOPE NOW. This is an unprecedented response by the mortgage industry. Given what the industry has done already, we recognize that more needs to be done. H.R. 5579 is a thoughtful proposal to help us do more.

Our concern, however, is that the potential harm may outweigh the potential benefits. Borrowers and mortgage companies desperately need greater stability and liquidity in the market. The best way to improve liquidity is through investor confidence. Any effort that increases investor risk, including protecting servicers from liability, hampers this goal. We are concerned this bill may create investor uncertainty similar to recent bankruptcy proposals, despite the care the drafters took in trying to balance the interests of investors and servicers.

MBA believes policy efforts should be focused on giving lenders and borrowers more options to work together such as new loan products to allow borrowers behind on their payments or upside down on their mortgages to refinance. The committee is currently working on such a proposal, and we look forward to participating constructively throughout that process. MBA is also eager to partner with Congress to finish work on FHA modernization, GSE oversight reform, housing tax incentives, and expanded mortgage revenue bond authority.

The Mortgage Bankers Association appreciates your efforts to help borrowers stay in their homes. Servicers will continue to use their contractual authority to perform loss mitigation to the extent permissible and prudent. It remains unclear to us, however, whether the benefits of H.R. 5579 outweigh the potential harm the bill may cause the mortgage market overall.

Thank you for the opportunity to appear before you, and I look forward to answering your questions.

[The prepared statement of Mr. Story can be found on page 44 of the appendix.]

Chairman KANJORSKI. Thank you, Mr. Story.

And now we will hear from Marlo Young, partner, Thacher Proffitt & Wood, LLP. Mr. Young.

STATEMENT OF MARLO A. YOUNG, PARTNER, THACHER PROFFITT & WOOD LLP

Mr. YOUNG. Chairman Kanjorski, Congressman Castle, and distinguished members of the subcommittee, good afternoon and thank you for the opportunity to testify here today. I am honored to be here representing Thacher Proffitt & Wood to discuss the Emergency Mortgage Loan Modification Act of 2008 and ways to prevent foreclosures and mitigate losses. We commend you for calling this hearing and look forward to offering our views on these important matters.

Although a substantial number of loans have been modified to date, servicers have been unable to complete the desired amount of loan modifications, primarily due to operational challenges. The servicers must choose among a variety loss mitigation alternatives to achieve a sustainable arrangement with the borrower that is also in the best interest of investors. This can be a very labor-intensive and time-consuming endeavor for the servicer and unfortunately, there is not one particular type of loan modification that is suitable in every circumstance.

The loan modification process would benefit from more streamlined approaches and enhanced automation. The ASF framework released last December was a worthy attempt at streamlining the loan modification process. However, the recent reduction in short term rates lessened the anticipated payment shock and has resulted in a smaller number of adjustable rate loans that are eligible for modification under the streamline framework.

We do not believe there are major legal or contractual impediments to making loan modifications. Rather, our study of typical servicing agreement provisions for the ASF concluded, generally, servicers of loans and securitizations have the authority to implement loan modifications and other forms of loss mitigation alternatives when the loan is in default, or default is reasonably foreseeable, provided that the action taken is in accordance with accepted service and practices and it is in the best interest of investors.

The provisions of Section 2(a) of the Emergency Mortgage Loan Modification Act of 2008 employ concepts that are consistent with the servicing provisions found in most agreements. We support the inclusion of the provision in Secion 2(a) of the bill that reads, "Absent specific contractual provisions to the contrary, removing any requirement that a loan modification or other loss mitigation not contradict the terms of the servicing agreement may interfere with the existing contractual terms of servicing agreements and result in actions that are not necessarily in the best interests of investors." We think Section 2(a) should clarify that the servicer should select from all available loss mitigation alternatives, the one that maximizes recovery, and not compare the alternative selected solely to foreclosure.

In addition, as long as the servicer's procedures for evaluating the net present value of a particular loss mitigation alternative are reasonable, the servicer's decision should not be challenged on the grounds that other evaluation procedures might have led to a different result.

We question whether the safe harbor in Section 2(b) is necessary or desirable if the standards in Section 2(a) are adopted. As Section 2(a) requires that any loss mitigation action not contradict any terms in the servicing agreement, and sets forth standards that are generally consistent with existing servicing provisions, the safe harbor contained in Section 2(b) does not appear to be necessary. In fact, the safe harbor provision may interfere with existing contractual provisions and bring into question the rights of investors on the servicing agreements.

We believe that portions of the bill, in particular Section 2(a), will be helpful in providing certainty regarding appropriate loss mitigation standards. Section 2(a) would clarify that the phrase "in the best interest of investors" refers to all investors in the given securitization trust in the aggregate without regard to the effect of any specific class. This would make the servicers task of determining the appropriate loss mitigation more manageable.

We believe that a major impediment to a servicer utilizing the full range of loss mitigation alternatives is the absence of an available loan product for funding a short refinancing, or a refinancing that pays off only a portion of the existing first lien for borrowers who are in default or are in immanent default. Accordingly, we think that proposals to expand FHA Secure or create a new FHA program for this purpose can serve as a key role in reducing foreclosures. My testimony includes some recommendations for such a program that I hope this committee will consider.

I thank you for the opportunity to participate in today's hearing. Finding solutions to the current mortgage and housing crises and preventing foreclosures should be a high priority for all market participants in our communities.

Again, I commend your leadership on these important matters. Thank you.

[The prepared statement of Mr. Young can be found on page 49 of the appendix.]

Chairman KANJORSKI. Thank you, Mr. Young, and all the members of the panel.

Before I get into my questions, I ask unanimous consent that Mr. Watt be considered, for the purpose of this hearing, as a full member of the committee with all the rights and privileges thereto. Is there any objection? Hearing none, Mr. Watt is so recognized. Mr. Watt, do you have an opening statement?

Mr. WATT. No, Mr. Chairman.

Chairman KANJORSKI. Very good. It seems to me that the three witnesses, if I am hearing you correctly, really do not feel there is a need for this legislation. Is that a reasonable conclusion?

Mr. DALOISIO. From what I have said, and what I have heard the others say, I think that is where we are coming out.

Chairman KANJORSKI. Well, I think that is interesting. But the reason I am interested in seeing a safe harbor and other encouragements to redo modifications in the mortgage field is that, what kind of a signal are we sending? Just go along as we have gone along over the last year? And catch as catch can. How are we going to really encourage a lot of people who are working with failing mortgages at this point to do something about restructuring and modification of those mortgages? What would you suggest we do, in other words?

Mr. STORY. One of the suggestions that mortgage bankers have is to find more products and new programs available so people who may be delinquent or upside down can refinance. We commend the House's approval of the FHA modernization bill, as well as GSE reform, and that is one of the ways we can help this problem.

Chairman KANJORSKI. Would you not think, though, that the easiest and fastest way to handle a million, million-and-a-half, or two million mortgages is to have the servicers contact these mortgage holders and say, "Look, before you get any further in, before we run into any further problems, come on down, we want to talk, we can do things to keep you in your home, reduce the price, reduce the strain, and get you there." I mean, testimony that I am hearing from people and just general statements is that 40, 50, or 60 percent of the people never contact the holder of their mortgage before they go into default and foreclosure. How are we going to encourage the servicer to get more aggressive and to work with these people who are tending to go toward default?

Mr. STORY. Well, we actually have a couple of issues there. One is that there have been 1.2 million repayment plans and modifications that the servicers have accomplished at this point. Also, the servicers are actively trying to help this problem. They are sending letters, they are actually going out to people's homes and knocking on doors. There is a number of people who choose not to respond to the calls that the servicers make to them because they are afraid of having to have that discussion with the mortgage company. That is one of the reasons that the HOPE NOW initiative has been put together, to help people so that they can call that number if they don't want to talk to the servicer, they can also look on a Web site, the Mortgage Bankers' homelearningcenter.org, which has numbers of all the servicers in there where they can make a phone call.

Our goals, from the Mortgage Bankers Association, are pretty simple. You know, one is we want to stabilize the market. The second is obviously, to help homeowners stay in their homes. We also want to ensure that this doesn't happen again, and we don't want to do anything that would be a permanent damage as we go forward during this situation.

Chairman KANJORSKI. Well, I am sure there is nobody on this committee or in the Congress or in the general public who wants to see it happen again. Going to that issue, I am astounded that it happened the way it happened, to be quite honest with you. I had the CEO of a monoline insurance company in my office a couple of weeks ago, and he showed me a study that his insurance company had undertaken of his five competitors in monoline insurance. In 2006, he found that, of the securitized loans or securitized mortgages that his competitors had written policies on, as many as 18 percent of the mortgages did not have a first installment payment.

Now, that is last year or 2 years ago, 2006. And why did a "tilt" bell not go off? Why did something not go up in the sky, fireworks or something to indicate, "We have a problem."

Before I got to Congress, I served on a little bank board, and when our default rate used to get up above one-half of one percent, we used to start sweating. When it got above 1 percent, blood was coming out. Why did the organizations and associations not start yelping? Why did the regulators not run in and shut some of these things down?

I was hearing in 2007 that there were a bunch of cowboys out there selling any garbage that they can put together because Wall Street has all the money in the world. Come down with any packages and sell them.

Now I know everybody did not do that. And I know there were very good operators, and they all should not get tarnished with the same brush, and I have a tendency to do that. But what I am saying is, we are in a situation now where we have the potential to surgically prevent what I would consider a depression or a meltdown of the financial system. I am all in favor of—and that is why I supported Mr. Castle's position when he came up with the idea—making sure that all the encouragement in the world is out there for people who are servicers of these mortgages to get involved to try to contain the problems. And if we just do what you are talking about, handling the things as they normally occur, letting the marketplace and the general market rules prevail, it seems to me we are going to end up probably with a tougher situation than we have right now or at least as bad as we have right now. I think that is intolerable. So how do you respond to that?

Mr. STORY. Well, first of all, those are all very important comments, and the MBA isn't opposed to this bill; we are more concerned about the possible litigation that may occur in the future, so it is a balancing act, it is a fine line in terms of our Association's agreement as we go forward.

Chairman KANJORSKI. Very good. And I know I am taking up all of my time now. Mr. Castle.

Mr. CASTLE. Thank you, Mr. Chairman. You know, I don't mean to speak for everybody else, but I would imagine everybody here, and probably all of you, are of the mind that we would like to save people from going through the foreclosure process. I don't know who wins in the foreclosure process, and we are all looking for answers to that, and I don't think any of us are married to any particular proposal; we are just looking for the best solutions possible in order to reach that.

I appreciate some of the suggestions which you made in your testimony. While I don't necessarily agree with your full conclusions, I think you made some positive suggestions that we need to look at in terms of what we are doing.

Mr. Story, in answer to the question Mr. Kanjorski asked you, you indicated the advantage of new products, but we all know that there are a couple million people who are facing foreclosure processes right now, and that is a matter of concern to all of us, not just how we might fix things as far as the future is concerned, and it seems to me, I am in favor of those proposals too, FHA and GSE or whatever, but all of that is going to be a little bit down the road in terms of getting both done and in place.

But we are concerned about those who are going into default now, is what we are trying to deal with. Do you all have ideas as to how to deal with this beyond what we have already heard? I mean, we have heard about the servicers, and I don't frankly put as much credence in what some of you said about the servicers going out and trying to accommodate people or whatever it may be. I am from Delaware and I have not seen a lot of that at home at this point. We don't have a particularly significant percentage problem with this compared to other jurisdictions, but it is there, we see it, it has increased a great deal, and it just seems to me that we are doing a lot of sitting on our hands with respect to this, so we need to be more proactive.

My question is, is there anything that Congress could be doing immediately, or anything further that can be done in the servicing banking community at this time, that would provide immediate help to those who may already be in default and getting ready for foreclosure? Any one of you can answer that.

Mr. STORY. Well I think this, and I go back to what I said earlier, getting that FHA reform bill passed and approved as quickly as possible will help the whole market. Specifically, if there are some opportunities for people to refinance out of some of these situations. And secondly, I would offer new homeowners, new home buyers an opportunity to qualify for loans and therefore we need to work on the depreciation of home prices in the marketplace as well, which is causing some of these problems. So if we can get that to level out, and get new people into homes, that would help as well.

Mr. CASTLE. I don't mean to argue with you, but I am not really talking about new homeowners. I understand that, and that is one reason I am for the bill. But I am most concerned about those who are presently in default, and I am not sure all of that is, even if we move quickly through the Senate or whatever, all that is going to happen quickly enough to really be able to help and rescue those particular people in that circumstance. Some are in foreclosure, some are in default getting ready to go into foreclosure or whatever.

What we are trying to do is do something that is much more immediate than that and deal with people on a faster basis, because we think that is needed at this point.

Mr. STORY. I appreciate that. We feel that the 1.2 million people we have already helped is a significant positive stride moving forward, and we hope that we can help more people as we move forward.

Mr. CASTLE. Well, I don't know the exact numbers, but my estimates, based on what I have heard, would be that would be about ⅓ of the people who might be having some problems, so that would mean ⅔ or a couple million have not yet been helped. And it seems to me that it has slowed down, and I am not sure what is happening now with respect to that. It seems to me we all have a responsibility to try to do something about it.

And I would think the investor community would care a great deal about that. I don't understand the investor community on the downside of mortgages. I always thought you took a mortgage out, and your bank held it forever, and then you find out about assigning mortgages and the securitization of them or whatever it may be, but I would think on the security aspect of it, you would be vitally concerned about the defaults and the foreclosures. I would assume, unless it is some sort of insured situation, that is a loss of principal on the investment, so I am a little concerned that the attitude is, "Let's leave it alone, it is okay the way it is."

If you have problems with our legislation, I don't mind fixing it. If you have problems with the concept, the way we are going, I don't mind changing that, but I think the idea that these sort of longer term things we are talking out will eventually bail us all out, that may be true of the economy in a couple of years. In the meantime, another million people may have gone into foreclosure, which is, I think, our underlying concern.

Mr. DALOISIO. If I may, I think the investor community is very concerned, you know, with the direction that things are moving right now within the free market system. Even though free markets do tend to self-correct, if allowed to self-correct, the pain of self-correction here may be more than most are willing or able to bear.

The question becomes what are the most appropriate and most effective measures to implement. The question also becomes if implementing those measures would even be able to bring about a turn of events sooner. I think overall, there is a lot of focus on the direction home prices, and I have heard it said by others and I believe this myself, that I don't think we will see a natural turn in events until we see expectations that home prices are falling change.

And to the Congressman from Georgia's point earlier, one of the concerns that investors have is exactly the kind of domino effect that we are seeing in communities where you have not just one or several foreclosures, but multiple foreclosures, which has the impact of reducing the willingness of others in that community to stay in their home, so even if they were given an affordable option to stay in that home, they may no longer have the desire to stay in that home.

How we address that, I am not entirely sure. I definitely agree that servicers need to be encouraged to provide as much modification activity as is economically sensible. In the current environment, the economics of foreclosure cannot be superior to the economics of modifying to a payment or series of payments which in the aggregate are economically superior, and I don't believe investors stand in the way of that happening, and I also don't believe that it is the threat of litigation that is preventing servicers from doing that by and large. Maybe infrastructure issues, adaptation issues. I think the wave that has come upon us has come upon us so quickly that the time required to adapt to that is a bit longer than we had hoped.

Mr. CASTLE. My time is up, and I will yield back, but I don't disagree with you necessarily. I do feel that the threat of litigation is part of the problem, and the other things you mentioned are also, I think, a part of the problem. I don't expect you to answer this, but I just remain vitally concerned about the issuance of mortgages in a market in which the appreciation of real estate was going up tremendously, and I think a lot of mortgagors were basically issuing mortgages without paying as much attention as they should have to the background of individuals on the basis that it doesn't make any difference. The property will go up, and that is our asset, that is our lien, and so we are going to be okay. I think, hopefully, there is a lesson in all of this in terms of how we have to issue mortgages in the future. I yield back, Mr. Chairman, thank you.

Chairman KANJORSKI. Thank you very much, Mr. Castle. The gentleman from Georgia, Mr. Scott.

Mr. SCOTT. Thank you very much, Mr. Chairman. I have a couple of questions. First, I would like to deal with what some of the opponents of this bill are saying, because I think it is good to make sure that we get the full perspective from you. What are your thoughts on opponents of the bill, when they claim it would abrogate the terms of existing contracts, but without providing legal recourse which they believe would have a detrimental effect on investors and set bad precedent? Do you believe this to be true, why, or why not, and further, they have noted that servicers already have a duty to engage in loss mitigation as part of the mortgages they oversee, and so they believe the legislation is unnecessary. Would you give me your thoughts on that please, quickly. Then I have another question.

Mr. YOUNG. Congressman, I can first speak to the second point, which is that, in our review of most securitization documents, there is already the ability of servicers to look at all loss mitigation alternatives as well as foreclosure in trying to fulfill their obligation as I see it, which is to maximize proceeds to the investor. So I do believe that there are times where the documentation may not be clear and so there may be points and parts of the bill that may be worthy of implementing.

Certainly, there was a concern at some point, what it meant to do what is best in the interest of the holders, the investors. And given the various interests of the investors at every part capital structure and the securitization, that raised concerns for investors that they would be subject to liability from those that would suffer most of the losses in these securitization structures. But I think given the volume of defaults and the magnitude of the losses that these investors are facing, I do not believe that is as much of a concern because I think that a lot of investors at all parts of the capital structure are being affected.

However, I do believe that there are positives in clarifying exactly what it means to be acting in the best interest of investors as a whole as well as maybe pointing out what is reasonably foreseeable default or imminent default. I think those are positives in the bill in clarifying where there is a need for interpretation in these various documents, which there is a lot of variation.

Mr. SCOTT. So basically, you see a need for the bill, but not as much of a need that is in the bill currently?

Mr. YOUNG. Well, I think to the extent the bill advocates for a safe harbor from liability, servicers are already performing loan modifications, so I suspect that in doing so, that is not the main concern for servicers. As I noted, I think it is more about dealing with the large volume of defaults and modifications that need to be done that seems to be the focus now.

Mr. SCOTT. Okay. That is fine. My time is ticking away, and I did have another question I wanted to get a response to, and that is, on the issue of moratoriums on foreclosures, very select, maybe 60 days, what is the value of that? And it is particularly true because in some parts of the country, some move closer to have your home foreclosed in the county courthouse in a month or 2 months, you miss one payment, or 2 months' payment, that there may be some value to that.

I would like to get your thoughts on imposing a selected moratorium on foreclosures and mortgage payment resets for owner-occupied homes and what you believe would be an adequate time span, and wouldn't this provide some time for establishing a well-rounded plan which would include establishing some sort of board to deal with this, which includes Secretary Paulson, the Fed Chairman, and financial experts and consumer groups?

Mr. STORY. One of the concerns we have about the foreclosure moratorium is that would just increase the amount owed after that period of time, so it would create a more difficult situation for that person to deal with after the moratorium was over. And secondly, the uncertainty from the investor market whether or not this could happen in the future that would cause some liquidity issues that we are having right now. Thank you.

Chairman KANJORSKI. The gentleman from California, Mr. Sherman.

Mr. SHERMAN. Thank you. One of the major aspects of the bill we have under consideration is to clarify existing contracts between those who invest in mortgages and those who serve them. I will ask all three gentlemen here, are you confident, in the absence of this bill, that every servicer will understand with every pool they are administering whether their obligation is a separate fiduciary obligation to each class or investor or whether their obligation is to the pool as a whole? I will go right down the list starting with the gentleman here. In other words, in the absence of this bill, is everybody going to be really clear about what their fiduciary duties are?

Mr. YOUNG. Congressman, I think the efforts of the ASF and other industry groups have provided some guidance about what it means to be—

Mr. SHERMAN. If I can back off, I used to be a lawyer, some of my best friends are lawyers, I still admit it, and I can't imagine you getting out of liability by waving around a paper from a private industry group and saying, "Hey, we meet these standards." So, do you have any legal opinion that says that an unclear servicing contract or an unclear trust agreement can be made clearer by an ASF statement?

Mr. YOUNG. No, Congressman. As I was going to proceed and say, I do believe, and I have stated in my testimony that I do think there is worth in part and portions of the bill being enacted, specifically that point, to clarify that when the servicers are acting in the best interest of investors, that they are acting in the best interest of investors as a whole, namely all the investors in that particular transaction. So I do believe there is worth in that particular portion of the bill.

Mr. SHERMAN. I will ask the other two witnesses whether they disagree with your comments.

Mr. STORY. We think that not everything is clear in some of these situations, and we would be supportive of this bill if the investor community was also supportive of the bill.

Mr. DALOISIO. To answer your question, I think there is likely a group of contracts out there that could benefit from increased clarity that would be aligned with the interest of investors. There was a time, early in the development of this crisis, where I thought servicers would be more concerned whether or not their action would benefit a certain part of the capital structure at the expense of another part and therefore open themselves up to liability to the disadvantaged part of the capital structure.

However, I think the losses that have been crystallized so far and the losses that are near certain to crystallize themselves as RIO converts into losses which are posted into these securitization structures are of sufficient magnitude to cause the permanent cash flow triggers in these deals to fail, and once they fail, that would be more of a permanent fail rather than a temporary one, and therefore that structural operation itself should cause servicers to think solely along the lines of what is in the best interest in the aggregate to the economics of the trust rather than to any class of investors because it is out of their hands.

Mr. SHERMAN. I thank you for the tremendous compliment of assuming that I understand all the jargon that you just included. The record will reflect that I understood every word you said and every jargon.

So I am trying to figure out what harm this bill would do, and I realize I may be taking up the time of my colleagues here, but

I will just ask the third witness here, since this bill basically clarifies the rights of servicers to do things in the best interest of the investors as a community, how would this bill deter future investment in mortgage pools?

Mr. DALOISIO. Yes, I am not saying that it would deter future investment in mortgage pools. I think what I am saying or what I am trying to say is that it runs the risk of deterring future investments in mortgage pools, and I think as Chairman Kanjorski opened, he opened with remarks that gave consideration to the practicality of doing something over the principle of not when it comes to looking at the contract law and legislative solutions that could be in partial opposition to the contract law.

Mr. SHERMAN. I would just point out that if you want to deter investment in mortgage pools, just do nothing. Allow my friends, the lawyers, to sue on behalf of each of the different investor groups with regard to each of the different contracts. And I assure you that there will be more investment in law schools and less investment in mortgage pools as the years go forward.

I realize with every bill there is a risk of having a bad effect, but I think doing nothing and leaving these contracts to be determined through litigation and determine the rights and the obligations of the trustees through litigation strikes me as also posing a risk.

And I will ask—I have my reading glasses on, so I am just going to point to, I guess it is Mr. Young, on this end. I can't read your name, believe it or not, because the reading glasses are that strong. Do you have any comment on how this bill, which is designed to simply clarify the rights and the duties of trustees and those doing the servicing, how this would deter investment in mortgage pools?

Mr. YOUNG. Well, I think, as some of the other witnesses alluded to, the risk that legislation can be enacted after a contract has been affected runs the risk of uncertainty going forward for future investors in those particular transactions and so, given that, and given moratoriums on foreclosures and other legislation that will basically interfere with the understandings under the contract may have a chilling effect on future investment.

Mr. SHERMAN. Well, I will point out there are a lot of bills that have been introduced in the House and the Senate that I could see investors really hating and State legislatures changing their foreclosure laws, etc. But I don't know why you would oppose this bill because you are afraid of other bills. If anything, if we do this bill, we are less likely to pass bills that are more extreme.

But the other thing that I will point out to you is, yes, you can say it is extraordinary for Congress to pass a law that defines vague elements of contracts. Usually that is done by the courts. As an investor, I would be more afraid of the courts redefining my contract or influencing how vague terms would be defined than the Congress, and I know that if somebody is going to have to define the rights and obligations of trustees, and if we do it, my lawyer friends will be considerably less wealthy, so I will yield back.

Chairman KANJORSKI. Ms. Brown-Waite.

Ms. BROWN-WAITE. Thank you, Mr. Chairman. Just this morning, my district office called and said that they had two constituents who were trying to work with the lenders and they were not getting very much response. These are people trying to avoid foreclosures, and I would just ask, do you think that the industry has done enough to work with property owners?

Mr. STORY. I think they are trying very hard to help everyone, and obviously they can do more. Some people discuss some issues with probably some technology issues maybe, or some staffing issues. It is a big concern for everyone in the mortgage industry. Nobody wins in a foreclosure. It is the worst-case scenario that nobody wants to get to, so there is always room for improvement.

Ms. BROWN-WAITE. I certainly always thought that myself, sir, but when the property owner makes an attempt to pay off at least half the delinquent payments, and the servicing company won't even accept it, they want everything or nothing, and this is someone who had previous loans and never ever was foreclosed on.

Mr. STORY. Well, I can't comment on an individual company's procedures, but as I said earlier, there is a huge effort on the part of mortgage servicers to try to work with people as much as possible. There have been 1.2 million repayments and modifications since this last summer, so there is an effort out there, I can guarantee you, that people want to help these people out.

Ms. BROWN-WAITE. Well, when they won't return phone calls, and they won't accept a large amount of the back money due, well over half, it certainly doesn't appear that way to the taxpayer and the homeowner out there and certainly the neighbors who would not want foreclosed property in their neighborhood. I know I don't. I have a neighbor who is very close to foreclosure. All that does is drive down the price of neighboring real estate at a time when we certainly cannot afford it.

Can Congress' approach to the loan modification issue address the concerns of individuals came to Congress who believe we need less government involvement in our lives, because that certainly is a philosophical conflict?

Mr. STORY. That is a good question. I think that in certain times there are certain situations that need help from the Congress. As I discussed earlier, things like the FHA modernization bill, the GSE reform, all those things are very important for industry moving forward and hopefully helping the existing situation as well.

Ms. BROWN-WAITE. I have a question which maybe Mr. Young or—I must need to wear my glasses because I apologize, I can't read your name, Mr. Daloisio?

Mr. DALOISIO. Close enough.

Ms. BROWN-WAITE. I apologize. I always murder names, I apologize. Are we creating a situation of an echo problem. In other words, those who are in adjustable rate mortgages now don't have the ability to go to a 30-year fixed so they enter into another adjustable loan. Are we going to have an echo problem when those ARMs come due again because I know a large number are going to the ARMs because they cannot afford to go to the traditional 30 year?

Mr. DALOISIO. I think there is a chance of that. It seems to me the way the rate markets have aligned with the property markets we are seeing home prices fall and short term interest rates come down. It might be likely to believe that as home prices stabilize and start rising, so too might interest rates then do that. But then the ability of those people in those homes to service an adjustable as it is resetting higher, I think would have a concomitant as well.

Ms. BROWN-WAITE. So, is that "No, there won't be an echo financial problem?"

Mr. DALOISIO. It is not a "no," because I think there is risk there. I think an increasing number of homeowners elected to take out an adjustable rate mortgage because it had the benefits of a lower initial rate. They left themselves with the risk that if rates went higher, they may end up in an unstable product.

I think one thing we need to consider very carefully is making sure that the product offering is well-suited to the ability of the homeowner and the intention of the homeowner and whether or not they intend to stay in the home for a long period of time or whether or not they intend to move in a short period of time.

Ms. BROWN-WAITE. Thank you. I yield back the balance of my time.

Chairman KANJORSKI. Mr. Miller of North Carolina.

Mr. MILLER. Thank you, Mr. Chairman, and I apologize for having missed the bulk of this hearing. I have a couple of questions based upon just the few minutes that I have heard.

Mr. Story, you mentioned the cost of foreclosure as being something that would be a strong disincentive to your industry. And foreclosure, of course, is governed by State law. I don't know the law in all States, but I am familiar with North Carolina law, and I understand it is similar to that of other States in that the cost of foreclosure is actually recoverable by the mortgagee out of the proceeds of the foreclosure sales so that if there is equity in the home, the mortgagee recovers their cost. Is that not correct?

Mr. STORY. I believe that is correct.

Mr. MILLER. Okay, so as long as there is equity in the home, it really isn't an economic problem for the mortgagee, isn't that right?

Mr. STORY. That is correct, but most people who have equity in their homes don't go into foreclosure because they can sell their home because they have equity in their home and they can reduce the price.

Mr. MILLER. Right. It is only when a substantial number of mortgages are underwater, when people have more mortgage than they have house or have relatively little equity, that there is an economic problem for foreclosure. Let me put it differently: In an appreciating market, foreclosure cost is not really a problem for the lenders or for the mortgagees, is it?

Mr. STORY. Most likely not.

Mr. MILLER. And Mr. Daloisio?

Mr. DALOISIO. Yes.

Mr. MILLER. Okay. You said that the borrowers understood that they were getting a low rate initially, and it was an unstable product, but they couldn't afford anything but the initial rate. The Wall Street Journal estimated that 55 percent of the people who took out or got subprime mortgages in 2006 and 2007 qualified for prime mortgages. Do you have any information that contradicts that?

Mr. DALOISIO. I don't necessarily have information that contradicts that, although I think there may have been preferences in those situations that led the borrower to elect a higher rate of interest over a lower rate of interest, and although that sounds like it doesn't make sense, for example, they may have qualified for a conforming prime mortgage given some of the criteria, but maybe they wanted a loan or a debt service amount that was larger than what would otherwise have qualified them because they were looking to buy a bigger home. It is very difficult to tell simply based on the kinds of surveys that are being performed in the marketplace today exactly what led those particular individuals into products that were non-prime products.

Mr. MILLER. Quickly, you said buying a home. Isn't it the case that more than 70 percent or about 70 percent, 72 percent I think is the statistic based on the Mortgage Bankers statistic, 72 percent of subprime loans are not home buyers, but are for refinance. Isn't that correct?

Mr. DALOISIO. Maybe you were looking at 18 percent were non-owner occupants, is a number that we have. So 18 percent of those loans were for investors.

Mr. MILLER. The statistic I have heard on that is 6 percent. What is the origin of this 18 percent are non-owner occupants? Where does that come from?

Mr. DALOISIO. It comes from a third quarter 2007 survey that the mortgage bankers do.

Mr. MILLER. Mr. Daloisio, the Federal Trade Commission, among others, has done a study of people who had just gone through closing and then quizzed them with their closing documents in front of them. Essentially, very few people knew anything about their closing. Most people have observed this as an intentionally opaque process. So I know that you said that people chose, but in fact all the evidence to the contrary. The point that I really wanted to ask about, and I have used up most of my time, I hope there is some indulgence from the Chair. In the proposal, all of the justification for providing some certainty or some protection from liability is as against investors in the mortgage pools. Is there any justification or any other arguments that would apply to any kind of shield from borrower lawsuits, and do you understand that the legislation would apply to any kind of insulation from liability by borrowers?

Mr. DALOISIO. Just to make sure we understand the question, you are asking if we are aware that this piece of legislation would insulate servicers and securitization trusts from litigation brought by borrowers?

Mr. MILLER. Right. All of the justification has been that it is needed for insulation from liability by investors. And there has been not a word about insulation from liability by borrowers. Do you understand that it applies to borrower lawsuits?

Mr. DALOISIO. I had not focused on that particular dimension of this legislation.

Mr. MILLER. Have any of the justifications given for it, would any those extend to litigation by borrowers?

Mr. DALOISIO. Any of the justifications for this legislation, you are asking if those justifications, in our view, are valid?

Mr. MILLER. Or do they extend to borrowers?

Mr. DALOISIO. Do they extend to borrowers?

Mr. MILLER. Right. The justifications have all been why servicers need some assurance that they will not be liable to investors. Investors have different interests, they have different tranches, whatever, different risks and they may be affected differently by any kind of modification. None of those justifications appear to have applied to any kind of lawsuit by borrowers, isn't that right?

Mr. YOUNG. I did not focus on that particular aspect of the bill, but I do realize that there is protection for servicers for various parties, including borrowers. But we did not focus on that particular point. I think there was—

Mr. MILLER. When you say you didn't focus, you haven't talked about that in terms of justifying the bill or explaining the need for it, but it isn't part of your intent? What do you mean when you say haven't focused?

Mr. YOUNG. That was not a focus in my testimony. I did not focus on that particular aspect in my testimony.

Mr. MILLER. Well, should the legislation then clarify that the limitation from liability is insulation from liability to investors, not to borrowers?

Mr. YOUNG. I think most of the concern that at least has been publicized is the servicers' concern against, or liability to the investor community. I think that is why the focus of my testimony was mainly on that particular aspect. And I do believe that the particulars of the bill speak to clarification of the servicing agreements as they related to obligations between the servicer and the investor, and so that was why my particular focus was on that aspect of the bill.

Mr. DALOISIO. I might just add, in being able to consider it a bit, that it doesn't seem like there would be a natural line of responsibility between the borrower and the servicer that would give rise to the need for that kind of protection in this piece of legislation since it does appear that the servicer is well within its rights to collect all principle and interest due from the borrower.

Mr. MILLER. Okay. Thank you, Mr. Chairman.

Chairman KANJORSKI. Thank you. Finally, Mr. Watt of North Carolina.

Mr. WATT. Thank you, Mr. Chairman, and let me express my thanks to the Chair for allowing me to participate in today's hearing as if I were a member of this subcommittee.

I came because I knew this was a sensitive subject, but I am glad I came because after 16 years of service on the Judiciary Committee, I think this is the first time I have heard business groups say that they oppose limiting litigation against business groups, and after 16 years of service on the Financial Services Committee, I think it is the first time I have heard a business group say that they don't support a safe harbor for business groups, so this is kind of a first for me. It leads me to a realization that litigation and legislation and politics is primarily about self-interest, so perhaps we have the wrong witnesses here. Who are these servicers? Are they members of the American Securitization Forum?

Mr. DALOISIO. Yes, some of them are.

Mr. WATT. Are they members of the Mortgage Bankers Association?

Mr. STORY. Yes.

Mr. WATT. Do they have their own organization?

Mr. STORY. Some of them have members of other organizations as well. Banks—

Mr. WATT. I mean, is there something called a servicers organization that would have—so, some of them are the same people who actually make the loans, they service the loans, some of them are securitizers of loans, is that what the case is?

Mr. DALOISIO. That is correct.

Mr. WATT. Okay. Alright. So, in a sense, this bill would be protecting servicers from lenders, one in the same person, left pocket, right pocket.

Mr. DALOISIO. The bill would protect them in accordance with the provisions of the bill, yes.

Mr. WATT. So if a lender was made a loan and the servicer was a subsidiary of that lender, basically it would be protecting liability against the lender side of the organization as opposed to the servicer side?

Mr. DALOISIO. I don't believe that is correct, because I think the protection would only be afforded to the servicer, not to an affiliated lender of the servicer for an act that took place prior to servicing.

Mr. WATT. So you are saying a servicer in this case is always somebody other than the lender?

Mr. DALOISIO. Well, I think the servicer in this case is the entity acting in its capacity as a servicer. They may have acted in another capacity as lender, but I don't believe—

Mr. WATT. Well, sir, I think we are saying the same thing. If a servicer is a subsidiary of a lender, it might be one and the same institution, expect that one is a subsidiary, but it is the same corporate entity and the bill would protect the servicer side from potential liability from the lender side.

Mr. DALOISIO. I don't think the bill would end up protecting the lending aspect, I think it would only protect the servicing aspect.

Mr. WATT. Yes. I think we are saying the same thing.

Mr. DALOISIO. Okay.

Mr. WATT. Okay. Actually, I am on your side of this issue. I am not much on limiting liability, and I get suspect every time we have the legislative process interfere with the legal process, so you might find an ally on this, so I am glad to hear you say that you don't like the bill. Because I am not sure if you don't like it the servicers don't like it—you are speaking for the servicers here, right?

Mr. DALOISIO. I am not speaking for the servicers; I am speaking for investors.

Mr. WATT. You are speaking for investors. You are speaking for servicers, Mr. Story?

Mr. STORY. Yes. As I said before—

Mr. WATT. You are not speaking for the mortgage lenders, the bankers side, you are speaking for the servicers side?

Mr. STORY. Well they are the same, in a sense.

Mr. WATT. Well, who are you here representing?

Mr. STORY. The mortgage bankers who have members that are servicers and are also lenders—

Mr. WATT. And your servicers oppose this bill too?

Mr. STORY. Not necessarily, no. They have some concerns about parts of the bill, but as I said before, we would support the bill if the investors supported the bill.

Mr. WATT. Investors are Mr. Daloisio's group, so if they supported it, you all would support it?

Mr. STORY. That is correct.

Mr. WATT. Okay. Mr. Young is going to profit either way because he is in a law firm, so he is smiling regardless of how this comes out.

So Mr. Daloisio, does the fact there may be some protection against borrower liability, that will make you go back and look at this a second time, won't it?

Mr. DALOISIO. I will go back and look at that, although I don't—

Mr. WATT. It might change your opinion.

Mr. DALOISIO. I don't think it will because in giving it consideration here and now—

Mr. WATT. As I recall, you all weren't too keen on any kind of potential liability vis-a-vis borrowers when we were doing the predatory lending bill.

Mr. DALOISIO. Right. That is correct, and the concern there was investors are by and large passive recipients of the economics that are passed through these securitization trusts, they really had no active hand in whatever—

Mr. WATT. But they had a responsibility to look at what they were buying, didn't they?

Mr. DALOISIO. It depends on which type of investors you are speaking of. If you are speaking of investors in asset-backed securities, by the time those loans are packaged in security format, what investors are looking at are somewhat different than what investors will be looking at—

Mr. WATT. Which level is in your organization? All levels?

Mr. DALOISIO. Within my organization, all of them are within the part of the organization that I am involved with, just the securities.

Mr. WATT. So that is the secondary tertiary further down the line, not the original buyers of the loans.

Mr. DALOISIO. That is correct.

Mr. WATT. Okay, so that was your concern in the predatory lending bill, that we might be talking about some potential liability against secondary tertiary buyers of loans, not the people who should have had responsibility for looking at the loans themselves or the responsibility for looking at the quality of the loans that they were buying, only first purchase basis.

Mr. DALOISIO. That is correct.

Mr. WATT. That's fine. That helps me because I have been trying over a long period time to understand what your concern was and how to address it since you all wouldn't talk to me in that process.

I will yield back. This has been helpful in a number of respects, so I thank the chairman for allowing me to participate.

Chairman KANJORSKI. Thank you very much, Mr. Watt.

Mr. Castle, do you have any further questions?

Mr. CASTLE. I really don't, but I will ask just one of Mr. Story. I am confused about who is in your organization or who you represent when you said that you were speaking for servicers. Are you speaking for pure servicers, or are you speaking for servicers who are also investors, or are you retracting that altogether as to whom—

Mr. STORY. I am speaking for members of the Mortgage Bankers Association who are servicers.

Mr. CASTLE. Are you saying 100 percent of them are servicers?

Mr. STORY. No, I am saying—

Mr. CASTLE. If the answer to that is "no," are you saying that 100 percent of the servicers you are speaking for are in opposition to this bill?

Mr. STORY. No, I didn't say that we were in opposition of this bill. I said we had some concerns about this bill, but we were not opposed to it. But I am only speaking for the members of the Association that are servicers. There are some servicers that are not members of our association.

Mr. CASTLE. What would be the criteria for a servicer to be a member of your organization?

Mr. STORY. Basically, a mortgage banking firm or a bank that wanted to be a member of our Association that paid dues based on the size of their company. They range from small companies to Bank of America, to big companies. My company used to be a servicer for a number of years. We were in the mortgage business since the 1940's, and we serviced loans until probably 2000 or 2001, so that was an example of a smaller company doing it. Most of the servicers now, the economy of scale and the business anymore, servicers are mostly larger mortgage banks, bank sorts of companies.

Mr. CASTLE. Okay. I thank you. I am not sure I totally understand it, but that is something for me to work out.

Mr. STORY. Well we can help you out if you have some more questions, certainly we can help you with that.

Mr. CASTLE. Thank you very much. I yield back.

Chairman KANJORSKI. Thank you, Mr. Castle.

I want to thank the panel for helping us out today. I think you certainly straightened out Mr. Watt's questions. We appreciate your presence and your offering all the good testimony that you did. Before we wind this up though, I have a statement addressed to the Chair from the National Association of Realtors, dated April 3, 2008. Without objection, I am going to make it a part of the record.

With that, we thank the panel for their participation and close the hearing. The chairman notes that some Members may have additional questions for today's witnesses which they may wish to submit in writing. Without objection, the hearing record will remain open for 30 days for members to submit written questions to any of today's witnesses and to place their responses in the record.

The panel is dismissed and this hearing is adjourned.

[Whereupon, at 3:31 p.m., the hearing was adjourned.]

A P P E N D I X

April 15, 2008

OPENING STATEMENT OF
CHAIRMAN PAUL E. KANJORSKI

SUBCOMMITTEE ON CAPITAL MARKETS, INSURANCE, AND GOVERNMENT SPONSORED ENTERPRISES

SUBCOMMITTEE HEARING ON H.R. 5579, THE EMERGENCY MORTGAGE LOAN MODIFICATION ACT OF 2008

APRIL 15, 2008

Good afternoon. We meet today to examine H.R. 5579, the Emergency Mortgage Loan Modification Act of 2008. I have worked closely with Congressman Castle on revising his initial proposal and introducing this new bill.

Nearly 6 percent of all loans on single-family properties outstanding in the fourth quarter of 2007 were delinquent, which is the highest total delinquency rate in 20 years. Moreover, slightly more than 2 percent of homes are already in the process of foreclosure. That is the highest level ever. These numbers, coupled with the general anxiety and unease brought on by the housing crisis and the ongoing credit crunch, underscore the importance of this hearing and the need for our bipartisan legislation.

Many in Washington and throughout the country are preoccupied with playing the blame game and performing post-mortems as to what caused the subprime fiasco. I believe that such exercises must wait for another day. We can try to figure out how it all went wrong some other time. The immediate problems faced by many borrowers demand our attention. The search for innovative solutions in an increasingly complex financial world should be a priority. This afternoon's hearing represents part of that search.

One of the main obstacles that we face in attempting to decrease the number of mortgage foreclosures is the reluctance of servicers to modify loans and conduct workouts because they fear investor lawsuits. The legislation under consideration today will provide servicers a safe harbor from legal challenges, if the servicers meet certain conditions. A safe harbor should embolden servicers to ramp up loan modifications. Without the fear of litigation, servicer efforts toward loss mitigation should also greatly increase.

Some contend that adoption of this legislation will result in the abrogation of existing contracts. In drafting this new legislation, however, we addressed these concerns and sought to create a bill that honors the terms of existing contracts. Those parties who remain opposed to loan modifications on these grounds should remember that rigid principles sometimes must yield to urgent situations that demand immediate action. This situation is one such instance.

For every mortgage that does not fail but rather is saved by the servicer through loss mitigation, the value of the underlying loan pool should increase. After all, mortgages in foreclosure amount to much less than a modified loan. But more importantly, these modifications by the private sector will keep more families in their homes. To me, these benefits considerably outweigh the costs.

Some may, however, continue to question certain provisions of this bill in good faith and on fair grounds. My mind is by no means closed on these matters. If a better way exists to

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Financial Services Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises
Hearing "H.R. 5579, The Emergency Loan Modification Act of 2008"
Opening Statement for Congressman André Carson
April 15, 2008

Thank you, Chairman Kanjorski and Ranking Member Pryce for holding this important hearing today on ways to further mitigate foreclosures by clarifying servicers' responsibilities in managing loans in the secondary market. This bill is an important part of the Financial Services Committee's comprehensive effort to help homeowners keep their homes.

Given the complex mortgage environment, borrowers have had trouble negotiating the terms of their loan as many of them were securitized and the subsequent servicers were slow to react to borrower requests to modify their loans. There are over 7,300 homes in my district in the preforeclosure phase today and I believe the provisions in this bill would better enable these individuals to work out new terms and retain their homes.

This bill would ensure that servicers who proactively engage in loss mitigation are given a safe harbor from potential litigation. It is important that we recognize that preventing foreclosure in the borrowers' interest but also the servicers' and investors'. This bill is a responsible measure that will remove disincentives to working out these loans.

I look forward to your testimony today and the chance to work with my colleagues on this issue facing mortgage consumers.

American SECURITIZATION FORUM®

TESTIMONY OF
RALPH DALOISIO
CHAIRMAN
AMERICAN SECURITIZATION FORUM
INVESTOR COMMITTEE

BEFORE THE
SUBCOMMITTEE ON CAPITAL MARKETS, INSURANCE AND GOVERNMENT SPONSORED ENTERPRISES

UNITED STATES HOUSE OF REPRESENTATIVES

HEARING ON
H.R. 5579, THE EMERGENCY MORTGAGE LOAN MODIFICATION ACT OF 2008

APRIL 15, 2008

Chairman Kanjorski, Ranking Member Pryce, Congressman Castle and distinguished Members of the Subcommittee:

My name is Ralph Daloisio. I am a managing director with Natixis, a French banking institution with investment and other operations in the United States. My professional responsibilities include managing investment portfolios that comprise investments in mortgage-backed and asset backed securities, including subprime mortgage securities. I am pleased to be here today to share the views of the American Securitization Forum (ASF) on H.R. 5579, the Emergency Loan Modification Act of 2008, though I must caveat that these are not necessarily the views of Natixis. I serve as Chairman of ASF's Investor Committee and I am a member of the ASF Board of Directors.

Background

The American Securitization Forum (ASF) is a broad-based, not-for-profit professional forum that advocates the common interests of the securitization market and its participants. ASF has more than 375 member firms, including issuers, investors, financial intermediaries, trustees, rating agencies, financial guarantors, legal and accounting firms, mortgage insurers, and data analytics vendors, among others. ASF's mission and goals are to: (1) build consensus on best practices in the market; (2) advocate on behalf of our members; and (3) provide high quality educational events for industry participants and policymakers. ASF is an affiliate of the Securities Industry and Financial Markets Association (SIFMA)[1].

No securitization market constituency -- including lenders, servicers and investors -- benefits from subprime loan defaults and foreclosures. Foreclosure is usually the most costly means of resolving a loan default. As a result, it is typically the least-preferred alternative for addressing a defaulted loan whether or not the loan is held in a securitization trust. ASF therefore strongly supports the policy goal of avoiding foreclosures wherever reasonable alternatives exist.

Overview of Typical Securitization Document Modification Provisions

A basic principle underlying the servicing of non-performing subprime (or other) loans in securitization transactions is to maximize recoveries and minimize losses on those loans. This principle is embodied in the contractual servicing standards and other provisions that set forth the specific duties and responsibilities of servicers in securitizations. In turn, these contractual provisions, and the duties they impose on servicers and other securitization transaction participants, are relied upon by investors in mortgage-backed securities who depend primarily upon cash flows from pooled mortgage loans for the return on their investment.

Servicing of subprime residential mortgage loans included in a securitization is generally governed by either a pooling and servicing agreement (PSA) or by a servicing agreement (SA). Typical PSA and SA provisions require servicers bound by those contracts to follow accepted servicing practices and procedures as they would employ "in their good faith business judgment" and that are "normal and usual" in their general mortgage servicing activities.

Most subprime securitization transactions authorize the servicer to modify loans that are in default or for which default is imminent or reasonably foreseeable. Generally, permitted modifications include changing the interest rate on a prospective basis, capitalizing arrearages, extending the maturity date, and forgiving principal, among other actions. The "reasonably foreseeable" default standard derives from the restrictions imposed by the Real Estate Mortgage Investment Conduit (REMIC) sections of the Internal Revenue

[1] The Securities Industry and Financial Markets Association brings together the shared interests of more than 650 securities firms, banks and asset managers locally and globally through offices in New York, Washington D.C., and London. Its associated firm, the Asia Securities Industry and Financial Markets Association, is based in Hong Kong. SIFMA's mission is to champion policies and practices that benefit investors and issuers, expand and perfect global capital markets, and foster the development of new products and services. Fundamental to achieving this mission is earning, inspiring and upholding the public's trust in the industry and the markets. (More information about SIFMA is available at http://www.sifma.org.)

Code of 1986 on modifying loans included in a securitization for which a REMIC election is made. Market participants interpret the two standards of future default—"imminent" and "reasonably foreseeable"—to be substantially the same.

Contractual loan modification provisions in securitizations typically also require that the modifications be in the best interests of the security holders or not materially adverse to the interests of the security holders, and that the modifications not result in a violation of the REMIC status of the securitization trust. ASF and market participants generally interpret the standards "in the best interest of" or "not materially adverse to the interests of" investors or securityholders in a securitization to refer to investors in that securitization in the aggregate, without regard to the specific impact on any class of investors or any class of securities.

Consistent with typical contractual provisions governing servicing activities in securitizations and applicable law and regulation, ASF believes that a loan modification may be appropriate where the loan is either in default or where default is reasonably foreseeable, and if the latter, where there is a reasonable basis for the servicer to determine that the borrower is unlikely to be able to make scheduled payments on the loan in the foreseeable future. The servicer must also have a reasonable basis for concluding that the borrower will be able to make scheduled payments on the loan as modified, and for modifying the loan in a manner that is likely to be sustainable, but that does not reduce required payments beyond the magnitude required to return the loan to performing status, or beyond the anticipated period of borrower need.

ASF believes that loan modifications meeting the above criteria are generally preferable to foreclosure where the servicer concludes that the net present value of the payments on the loan as modified are likely to be greater than the anticipated net recovery that would result from foreclosure. Whichever action is determined by the servicer to maximize recovery should be deemed to be in the best interest of investors in the aggregate.

In addition to the authority to modify the loan terms, most subprime PSAs and SAs permit other loss mitigation techniques, including forbearance, repayment plans for arrearages and other deferments which do not reduce the total amount owed but may extend the term of payment. In addition, these arrangements typically permit loss mitigation through non-foreclosure alternatives to terminating a loan, such as short sales or deeds-in-lieu.

Although most PSAs and SAs in subprime securitizations either expressly permit or do not restrict loan modifications, some agreements do impose restrictions. For example, certain transactions limit the total number of permitted occurrences of modifications for any individual loan. Other transactions may limit the amount of modifications to a certain percentage of the initial size of the mortgage loan pool. Some agreements require prior consent (for example, from a rating agency or bond insurer) to allow the amount of modifications to exceed a specified percentage of the initial size of the mortgage pool. In a more limited number of cases, governing agreements may restrict the types of modifications that can be effected, or limit the amount by which the mortgage interest rate may be changed. However, it does not appear that any securitization requires investor consent to a modification that is otherwise authorized under the operative documents.

Based upon the economic and contractual principles outlined above, and consistent with applicable governing documents and regulatory and accounting standards, ASF has supported the use of loan modifications (along with other loss mitigation tools) by servicers in securitization transactions in appropriate circumstances. In general, "appropriate circumstances" would include situations where a servicer has concluded that a particular loan is in default or that default is reasonably foreseeable, and that the loan modification or other loss mitigation action contemplated by the servicer is likely to maximize recovery and minimize loss on that loan.

As part of its efforts to inform members of the industry and promulgate relevant guidance in light of the widespread challenges currently confronting the securitization market, ASF has published several recommended market standards and practices. One such set of recommendations relevant to the topic of this hearing is ASF's June 2007 *"Statement of Principles, Recommendations and Guidelines for the Modification of Securitized Subprime Residential Mortgage Loans."* This document (attached hereto as Exhibit A) is designed to provide guidance to servicers modifying subprime residential mortgage loans that are included in securitization transactions, and to provide a common framework for interpreting loan modification standards and contractual provisions, thereby promoting greater uniformity, clarity and certainty of application of these standards and provisions throughout the industry. Our testimony here incorporates by reference the more detailed analysis and discussion set forth in that Statement.

H.R. 5579, Emergency Mortgage Loan Modification Act of 2008

The Emergency Mortgage Loan Modification Act of 2008 establishes a standard of care for servicers when effecting mortgage loan modifications or workout plans, and a safe harbor for performing certain "qualified" loan modification or workout plans, "absent specific contractual provisions to the contrary." While we appreciate and support the need for clarity and legal certainty for servicers in performing loss mitigation functions, we have several concerns with the legislation as introduced.

The contractual standards to which the bill relates -- the duties of servicers with respect to modifying or otherwise mitigating losses on distressed mortgage loans -- are as discussed above typically established through general provisions in securitization contracts rather than specific ones. Though the provisions are often framed in general terms, they create legally enforceable expectations of conduct by the parties to whom the provisions pertain, including duties and responsibilities of servicers to investors when engaging in loss mitigation activities. To the extent the bill would supersede these general provisions, it would, in effect, overrule securitization contracts.

The underlying premise of the legislation appears to be that servicers of securitized mortgage loans are not sufficiently engaging in loan modification and workout activity due to fear of investor lawsuits and related legal exposure. However, it is worth noting that servicers today face potential legal exposure from overly conservative, as well as overly aggressive, loss mitigation activity, to the extent that a servicer may be accused of not fulfilling its obligations to maximize recoveries on mortgage loans. In addition, servicers are already reasonably well-protected from legal action by investors, since under typical servicing contracts they are liable only in the event of their negligence in performing their duties. Thus, we question the need to give servicers additional protection, as well as the premise that doing so will stimulate a significant expansion of the number and/or type of loan modifications taking place.

It is important to recognize that servicers are already engaged in expanded loan modification and loss mitigation efforts, consistent with their existing contractual obligations and in response to the challenges presented by current housing market turmoil. Servicers have been increasing their investments in loss mitigation personnel and have developed enhanced processes and procedures to expedite delivery of loan workout, modification and home retention alternatives wherever feasible. Data collected by industry participants involved in the HOPE NOW alliance supports these observations, and indicates that an increasing number and accelerating pace of workouts and modifications are taking place. For example, HOPE NOW recently reported that from July 2007 through February 2008, mortgage servicers have provided loan workouts that have enabled approximately 1.2 million homeowners to stay in their homes. In 2008, loan modifications represent 48% of all subprime loan workouts, which is more than double the rate in 2007.

The standard of care prescribed by the bill in Section 2(a) may be weaker and less protective of investor interests than that found in most servicing contracts today. This legislation states that a servicer is acting in the best interests of all investors "to the extent that the servicer reasonably believes the modification or workout plan or other mitigation actions will maximize the net present value to be realized on the loan over that which would be realized through foreclosure." This language suggests that a servicer satisfies the standard if any particular modification strategy yields a higher expected recovery than foreclosure. Whereas this language requires only that a servicer compare the net present value of a defaulted loan assuming modification with its net present value assuming foreclosure, typical servicing contracts require this analysis to be performed across a wider range of modification and loss mitigation alternatives, with the servicer being bound to choose action based on the alternative that maximizes net present value among these other alternatives, not just one of them. To clarify this intent, we suggest striking the words "over that which would be realized through foreclosure" at the end of Section 2(a).

In addition, the bill would protect servicers complying with its standard of care who grant a "qualified loan modification or workout plan." The definition "qualified loan modification or workout plan" in Section 2(d)(1) includes, among other things, only those that would remain in place for at least five years and those that do not provide for a repayment schedule that results in negative amortization. These limitations on the types of modifications that qualify for the safe harbor (and thus for legal protection) could create artificial incentives for servicers to pursue those types of modifications at the expense of others that might generate a greater recovery for securitization investors, contrary to servicers' existing duties. For example, a servicer could reasonably conclude that a loan modification of only three years is necessary to return a loan to performing status, or may conclude that a capitalization of arrearages would be successful in establishing affordable payments going forward. It is therefore inappropriate to specify particular types of modifications as being eligible for the safe harbor, to the exclusion of others. Doing so could skew servicer decision making to pursue legal immunity at the expense of alternatives that might yield a greater total recovery for the securitization trust. Creating such incentives would be contrary to the contractual standard of care to which servicers are generally bound by their contracts, and would introduce the possibility of a legislative overruling of pre-existing contractual provisions.

As a general matter, we have concerns with any legislation that would abrogate or interfere with previously established, private contractual obligations. PSAs typically require that the actions of the servicer, among other requirements, not be materially adverse to the interests of the certificate holders. Changing this standard would alter the commercial expectations of investors and could undermine the confidence of investors in the sanctity of agreements which are central to the process of securitization, which could consequently discourage investment in markets that need liquidity -- both now and over the longer term.

If the intent of the bill is to clarify servicing standards in a manner that is consistent with customary contractual provisions and thereby incentivize servicers to apply those standards to minimize losses and avoid foreclosures wherever possible, there is nothing fundamentally wrong with that from an investor or market perspective. The revisions we suggest would ensure that the legislation merely clarifies the servicing standards.

If, however, the intent is to replace the legal duties and commercial expectations of transaction parties with a different set of duties and expectations supplied by Congress, ASF is concerned that the passage of this bill would represent a de facto modification of existing contracts. Since all parties to a contract, including investors, rely on the legal, valid, binding and enforceable provisions of the governing contracts, any legislation that would dilute, amend, or modify such contractual obligations or prejudice how the obligor fulfills its obligations is considered by the ASF, and by a consensus of the investor constituency within the ASF, to represent dangerous policy. Legislated intervention into otherwise valid legal contracts could potentially threaten the stability and predictable operation of the contractual legal framework supporting our capital markets system, and could have a chilling effect on the willingness of investors to participate in our markets.

Conclusion

Thank you for the opportunity to participate in today's hearing. We believe that the interests of secondary mortgage market participants continue to be aligned with borrowers, communities and policymakers to help prevent foreclosures. To that end, ASF stands ready to assist, and commends your leadership on these important matters.

American SECURITIZATION FORUM

Exhibit A

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American Securitization Forum

American Securitization Forum

Statement of Principles, Recommendations and Guidelines for the Modification of Securitized Subprime Residential Mortgage Loans

June 2007

I. Introduction

The American Securitization Forum (ASF)[1] is publishing this Statement as part of its overall efforts to inform its members and promulgate relevant securitization industry guidance in light of the widespread challenges currently confronting the subprime residential mortgage markets.

Current subprime residential mortgage market conditions include a number of attributes of concern that impact securitization transactions and the broader environment for subprime mortgage finance: an increase in delinquency, default and foreclosure rates; a decline in home price appreciation rates; a prevalence of loans with a reduced introductory rate that will soon adjust to a higher rate; and a reduced availability of subprime mortgage lending for refinancing purposes. In light of these concerns, the ASF is of the view that loan modifications, for subprime mortgage loans that are in default or for which default is reasonably foreseeable, are an important servicing tool that can both help borrowers avoid foreclosure and minimize losses to securitization investors.

Moreover, the ASF recognizes that it is an important goal to minimize foreclosure and preserve homeownership wherever possible. Higher than normal rates of foreclosure may harm borrowers and their communities, and may adversely affect housing values and therefore collateral values on both performing and non-performing loans. Accordingly, the ASF recommends the use of loan modifications under appropriate circumstances as described in this Statement.

The overall purpose of this Statement is to provide guidance for servicers modifying subprime residential mortgage loans that are included in a securitization. It is our hope that publication of these principles, recommendations and guidelines will help to establish a

[1] The American Securitization Forum is a broad-based professional forum of over 350 organizations that are active participants in the U.S. securitization market. Among other roles, ASF members act as insurers, investors, financial intermediaries and professional advisers working on securitization transactions. ASF's mission includes building consensus, pursuing advocacy and delivering education on behalf of the securitization markets and its participants. This statement was developed principally in consultation with ASF's Subprime Mortgage Finance Task Force and Loan Modifications Working Group, with input from other ASF members and committees. Additional information about the ASF, its members and activities may be found at ASF's internet website, located at www.americansecuritization.com. ASF is an independent, adjunct forum of the Securities Industry and Financial Markets Association.

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common framework relating to the structure and interpretation of loan modification provisions in securitization transactions, thereby promoting greater uniformity, clarity and certainty of application of these provisions throughout the industry. As a consequence, ASF hopes that this guidance will facilitate wider and more effective use of loan modifications in appropriate circumstances.

While this Statement addresses certain legal, regulatory and accounting matters, it does not constitute and should not be viewed as providing legal or accounting advice.

This Statement is focused on modifications of first lien subprime residential mortgage loans. Many of the principles reflected in this Statement would also apply to modifications of other types of residential mortgage loans. This Statement does not address modifications of second lien residential mortgage loans.

II. Overview of Typical Securitization Document Modification Provisions

Servicing of subprime residential mortgage loans included in a securitization is generally governed by either a pooling and servicing agreement or servicing agreement. These agreements typically employ a general servicing practice standard. Typical provisions require the related servicer to follow accepted servicing practices and procedures as it would employ "in its good faith business judgment" and which are "normal and usual in its general mortgage servicing activities" and/or certain procedures that such servicer would employ for loans held for its own account.

Most subprime transactions authorize the servicer to modify loans that are either in default, or for which default is either imminent or reasonably foreseeable. Generally, permitted modifications include changing the interest rate on a prospective basis, forgiving principal, capitalizing arrearages, and extending the maturity date. The "reasonably foreseeable" default standard derives from and is permitted by the restrictions imposed by the REMIC sections of the Internal Revenue Code of 1986 (the "REMIC Code") on modifying loans included in a securitization for which a REMIC election is made. Most market participants interpret the two standards of future default – imminent and reasonably foreseeable – to be substantially the same.

The modification provisions that govern loans that are in default or reasonably foreseeable default typically also require that the modifications be in the best interests of the securityholders or not materially adverse to the interests of the securityholders, and that the modifications not result in a violation of the REMIC status of the securitization trust.

In addition to the authority to modify the loan terms, most subprime pooling and servicing agreements and servicing agreements permit other loss mitigation techniques, including forbearance, repayment plans for arrearages and other deferments which do not reduce the total amount owing but extend the time for payment. In addition, these agreements typically permit loss mitigation through non-foreclosure alternatives to terminating a loan, such as short sales and short payoffs.

Beyond the general provisions described above, numerous variations exist with respect to loan modification provisions. Some agreement provisions are very broad and do not have any limitations or specific types of modifications mentioned. Other provisions specify certain types of permitted modifications and/or impose certain limitations or qualifications on the ability to modify loans. For example, some agreement provisions limit the frequency with which any given loan may be modified. In some cases, there is a minimum interest rate below which a loan's rate cannot be modified. Other agreement provisions may limit the total number of loans that may be modified to a specified percentage (typically, 5% where this provision is used) of the initial pool aggregate balance. For agreements that have this provision: i) in most cases the 5% cap can be waived if consent of the NIM insurer (or other credit enhancer) is obtained, ii) in a few cases the 5% cap can be waived with the consent of the rating agencies, and iii) in all other cases, in order to waive the 5% cap, consent of the rating agencies and/or investors would be required. It appears that these types of restrictions appear only in a minority of transactions. It does not appear that any securitization requires investor consent to a loan modification that is otherwise authorized under the operative documents.

III. Loan Modification Principles

Based upon extensive consultation with its members and other securitization market participants, ASF believes that the following principles articulate widely-accepted industry views regarding the use of loan modifications in connection with securitized subprime residential mortgage loans:

1. For subprime mortgage loans that are in default or where default is reasonably foreseeable, loan modifications are an important loss mitigation tool that should be used in the circumstances described in this Statement. Modifications may include changing the interest rate on a prospective basis, forgiving principal, capitalizing arrearages and extending the maturity date. Other loss mitigation alternatives include forbearance, repayment plans for arrearages and other deferments which do not reduce the total amount owing, and also non-foreclosure alternatives to terminating a loan, such as short sales and short payoffs. Unlike other loss mitigation alternatives, loan modifications have the additional advantage that they can be used prior to default, where default is reasonably foreseeable.

2. Establishing early contact with borrowers is a critically important factor in the success of any loss mitigation initiative. Servicers should be permitted and encouraged to reach out affirmatively and proactively to borrowers for whom default is more likely, determine whether default is reasonably foreseeable, and

then explore modification possibilities. In particular, such outreach should be permitted and encouraged prior to an upcoming first adjustment date on a hybrid ARM loan.

3. Loan modifications should be considered and made on a loan-by-loan basis, taking into account the unique combination of circumstances for each loan and borrower, including the borrower's current ability to pay. The ASF is opposed to any across-the-board approach to loan modifications, and to any approach that would have all modifications structured in a particular manner. The ASF is also opposed to any proposals that would provide an across-the-board moratorium or delay period on foreclosures.

4. Generally, the ASF believes that loan modifications should only be made:

    a. Consistently with applicable securitization operative documents (including amendments that can be made without investor or other consents);

    b. In a manner that is in the best interests of the securitization investors in the aggregate;

    c. In a manner that is in the best interests of the borrower;

    d. In a manner that, insofar as possible, avoids materially adverse tax or accounting consequences to the servicer and, to the extent known, to the securitization sponsor or investors;

    e. Where the loan is either in default or default is reasonably foreseeable, and if the latter, where there is a reasonable basis for the servicer determining that the borrower is unlikely to be able to make scheduled payments on the loan in the foreseeable future;

    f. Where there is a reasonable basis for the servicer concluding that the borrower will be able to make the scheduled payments as modified; and

    g. In a manner that is designed to provide sustainable and long-term solutions, but does not reduce the required payments beyond the magnitude required to return the loan to performing status, or beyond the anticipated period of borrower need.

5. The ASF believes that loan modifications meeting the criteria in Loan Modification Principles point 4 above are generally preferable to foreclosure where the servicer concludes that the net present value of the payments on the loan as modified is likely to be greater than the anticipated net recovery that would result from foreclosure.

6. In considering loss mitigation alternatives that reduce the interest rate prospectively, servicers should consider whether to make the rate reduction temporary (such as a relatively short term extension of the initial fixed period on a hybrid ARM), or permanent, based on the anticipated period of borrower need. For temporary rate reductions, servicers should re-evaluate the borrower's ability to pay, and the continued need for a rate reduction, at the end of the temporary period.

7. Any loan modification that reduces otherwise lawful, contractually required payments of principal or interest must be understood to be a financial concession by the securitization investors. There is no basis for requiring such concessions from investors unless the modification is determined to be in the best interests of the investors collectively. Loan modifications should seek to preserve the originally required contractual payments as far as possible.

8. Reasonable determinations made by servicers with respect to loan modifications, where made in good faith and in accordance with generally applicable servicing standards and the applicable securitization operative documents, should not expose the servicer to liability to investors and should not be subject to regulatory or enforcement actions.

IV. Loan Modification Interpretive Guidance

The ASF endorses the following interpretive positions on specific issues arising in connection with loan modifications:

1. The ASF believes, based on prevailing existing practice, that standard and customary servicing procedures for servicing subprime mortgage loans included in a securitization, as typically used as an overarching servicing standard in securitization operative documents, should be interpreted to allow the servicer to: a) permit loan modifications (including prospective interest rate reductions which may be either temporary or permanent, forgiveness of principal, capitalizing arrearages, or maturity extension not beyond the securitization maturity date) for loans that are in default or for which default is reasonably foreseeable, so long as the modification is in the best interests of investors in the aggregate, and b) engage in other loss mitigation alternatives including forbearance, repayment plans for arrearages and other deferments which do not reduce the total amount owing, and also non-foreclosure alternatives to terminating a loan, such as short sales and short payoffs. The ASF believes that existing securitization pooling and servicing agreements should be interpreted, to the maximum extent possible, to authorize the servicer to take the actions referenced above.

2. With respect to existing pooling and servicing or other operative agreements that expressly prohibit or restrict the servicer from taking the actions referenced above, the ASF believes that amendments to those agreements authorizing such actions should be approved by all parties required to consent to such amendments, as and when requested to do so.

3. The ASF believes that securitization operative documents should not impose numerical limitations on loan modifications, such as limits based on the percentage of the pool that may be modified.

4. The modification standards "default is imminent" and "default is reasonably foreseeable" should be interpreted to have the same meaning.

5. The modification standard "default is reasonably foreseeable" should be deemed to be met where there has been direct contact between the servicer and the borrower, where the servicer has evaluated the current ability to pay of the borrower, and has a reasonable basis for determining that the borrower is unlikely to be able to make scheduled payments on the loan in the foreseeable future. (This interpretation is intended to provide guidance only as to a set of circumstances where the standard would generally be viewed to be met, and not to reflect any view that the standard would not be met in other circumstances.)

6. In evaluating whether a proposed loan modification will maximize recoveries to the investors, the servicer should compare the anticipated recovery under the loan modification to the anticipated recovery through foreclosure on a net present value basis. Whichever action is determined by the servicer to maximize recovery should be deemed to be in the best interests of the investors.

7. The standards "in the best interests of" or "not materially adverse to the interests of" investors or securityholders in any securitization should be interpreted by reference to the investors in that securitization in the aggregate, without regard to the specific impact on any particular class of investors, and in a manner that is neutral as to the effect on the cash flow waterfall or any particular class of securities.

V. Loan Modification Recommendations

The ASF recommends the following further actions in respect of loan modifications:

A. Existing and future securitizations:

1. The ASF endorses and encourages the adoption of the position articulated in the Mortgage Bankers Association position paper titled "FAS 140

Implications of Restructurings of Certain Securitized Mortgage Loans", dated May [24], 2007 (the "MBA Position Paper").

2. Servicers should maintain policies, procedures and guidelines that are reasonably designed to identify and manage any actual or perceived conflicts of interest that may arise in connection with their loan modification activities and decision making. Such policies, procedures and guidelines should address, among other topics, situations in which a servicer (a) has an ownership interest in one or more classes of bonds supported by principal and/or interest collections on subprime mortgage loans that it services; (b) receives servicing fees or other compensation that is tied to various attributes of subprime mortgage loans that it services (e.g., outstanding principal balance, delinquency/default status); and (c) is not reimbursed for the costs of loan modifications from collections on subprime mortgage loans that it services.

3. Securitization operative documents should clearly state, for purposes of "delinquency triggers" or "cumulative loss triggers" which control whether excess cash flow may be released to the residual, the following: (a) whether and under what conditions a modified loan is to be considered "current", and (b) whether and how any interest rate reduction or forgiveness of principal resulting from a loan modification should be treated as a realized loss.

4. As an urgent, high priority matter, the ASF should develop guidelines under which delinquency triggers and cumulative loss triggers in securitization operative documents, which control whether excess cash flow may be released to the residual, should be interpreted in a manner consistent with the parties' intent and in a manner that appropriately reflects any loan modifications that have occurred. It is the sense of investors that (a) any partial forgiveness of principal should be treated as a loss for purposes of cumulative loss triggers, and (b) a modified loan performing in accordance with its modified terms should be treated as delinquent for purposes of delinquency triggers for some appropriate period of time.

5. Greater clarity, transparency and consistency should be established regarding how any interest rate reduction or forgiveness of principal resulting from a loan modification should be reflected for purposes of investor reporting, and for purposes of allocating payments for the cash flow waterfall.

6. Consistent with the foregoing recommendations, servicers should not make decisions to use or not use loan modifications for the purpose of

manipulating the application of delinquency triggers or cumulative loss triggers which control whether excess cash flow may be released to the residual.

7. The ASF will conduct a survey of typical document provisions and interpretations, on the question of whether and under what conditions a modified loan is to be considered current for purposes of investor reporting, and for purposes of delinquency triggers and cumulative loss triggers which control whether excess cash flow may be released to the residual. Additional guidelines should be developed and recommendations should be made and evaluated regarding amendments to securitization transactional documents, based on the results of this survey.

B. *Future securitizations:*

1. The ASF will develop standard, uniform model contractual provisions governing the servicer's ability to provide loan modifications for use in future securitizations. Such provisions should expressly authorize the actions referenced in Loan Modification Interpretive Guidance point 1 above.

2. Use of an increased or supplemental servicing fee should be considered for loans that have been modified to defray the additional costs of administering modifications.

3. The ASF will develop standard, uniform model contractual provisions, both as to timing and priority, to govern the servicer's ability to obtain reimbursement for P&I advances and servicing advances made in respect of loans where there has been a loan modification, or where other types of loss mitigation have been used.

MORTGAGE
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Investing in communities

Statement of Robert E. Story, Jr., CMB

Vice Chairman,
Mortgage Bankers Association

before the

Subcommittee on Capital Markets, Insurance and Government Sponsored Enterprises

Committee on Financial Services

United States House of Representatives

Hearing on

"H.R. 5579, the Emergency Mortgage Loan Modification Act of 2008"

April 15, 2008

Chairman Kanjorski, Ranking Member Pryce, members of the Subcommittee, I am Rob Story, Jr., CMB, President of Seattle Financial Group and Vice Chairman of the Mortgage Bankers Association (MBA).[1] I appreciate the opportunity to appear before you today on behalf of MBA and the mortgage industry to discuss H.R. 5579, the Emergency Mortgage Loan Modification Act of 2008.

H.R. 5579 would provide a safe harbor to servicers who execute certain loss mitigation actions from litigation risk. MBA appreciates Representative Castle's and Kanjorski's efforts to reduce the contractual and fiduciary risks servicers face in providing the full range of loss mitigation options. However, MBA continues to be concerned about how the alteration of contracts would impact future borrowers and liquidity in the marketplace.

Constraints of Legislative Action

MBA appreciates Congressional efforts to relieve servicers from risk of litigation for performing more loss mitigation activities. Any efforts that can help more borrowers save their homes or provide alternatives to foreclosure in a consumer friendly manner are welcomed. However, it is unclear whether the benefits of this proposal outweigh the potential harm. Borrowers and mortgage companies desperately need greater stability in the secondary mortgage markets. Without greater liquidity, the ability to refinance and make new loans will be significantly constrained by lenders' portfolio capacity, rather than the broader national and international capital markets. Given the lowered risk tolerance of lenders, portfolio capacity is severely limited.

The best way to improve liquidity is through investor confidence. This comes from greater clarity as to the risk undertaken when purchasing whole loans or mortgage backed securities (MBS), as well as, continued confidence that credit enhancements and waterfall distributions will not be disrupted. Unfortunately any statutory effort that increases investor risk or limits their maximum recovery, including protecting servicers from contractual liability, hampers this goal. We are concerned this bill may create investor uncertainty, similar to recent bankruptcy proposals, despite the care the drafters took in trying to balance the interests of investors and servicers.

This legislation appears to be designed to protect investor interests, as evidenced by the bill's controls over unrestricted modifications and work outs. In particular, H.R. 5579 continues to constrain servicers to the pooling and servicing agreements (PSAs). The bill also recognizes and restates common contractual and business limitations on servicer activities, including the fact that:

[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 370,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,400 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

(1) servicers are duty bound to maximize, or to not adversely affect, the recovery of total proceeds to the benefit of all investors and holders of beneficial interests in a pool in the aggregate and not to any individual party or group;

(2) servicer activities are limited to borrowers who are in payment default or in imminent or reasonably foreseeable risk of default; and

(3) servicers reasonably believe their loss mitigation actions, including accepting short payments or partially discharging principal, will maximize the net present value to be realized on the loan over foreclosure.

Because these limitations are generally consistent with the intent of current PSAs, the bill does not offer significant additional authority to perform loss mitigation beyond existing contracts. While MBA is not advocating abrogating contractual provisions, we do question whether the safe harbor will have the anticipated affect of materially increasing modifications. Instead, the bill may create a new federal duty to protect investor interests that goes beyond the contractual relationship and statutory loss mitigation preferences.

For perfectly reasonable causes, the bill does not override specific contractual restrictions found in PSAs that limit servicers' ability to perform loss mitigation. For example, some PSAs limit the amount of modifications that can occur in a pool. A smaller percentage expressly prohibit modifications altogether. Others limit the ability to extend maturity dates while others limit the length of repayment plans. This bill, of course, would not overcome these obstacles to loss mitigation and, therefore, should be viewed as protective of investors.

Conversely, the bill appears to establish statutory preferences for certain modifications over other types of loss mitigation tools, such as repayment plans, which could impact whether cash flows go to senior bondholders or junior bondholders. Preferences for modifications over repayment plans could also impact delinquency assumptions that would falsely trigger reduction or elimination of credit enhancements tied to the deal. If these modifications then perform badly, investors would take larger losses than expected. Reaction to any perceived change in how the securities and cash flows behave will affect investor confidence.

Other Industry Efforts

The servicing and investor communities have worked together through the current financial crisis to provide latitude in and clarity to contractual provisions. Significant strides have been made and will continue to be made, as servicers, attorneys and investors advance and test new concepts. It is important to reflect on some of the key industry efforts that have brought about record loss mitigation activity.

The industry coalesced to form the HOPE NOW[2] alliance to improve efforts to help homeowners avoid foreclosure, through funding of national home retention counseling, improved standardization, improved advertising and outreach to explain loss mitigation opportunities and the introduction of enhanced servicing practices.

Industry and Congress also worked together to address accounting issues that stood in the way of helping borrowers. MBA approached the Financial Accounting Standards Board to suggest treatment of current loans in foreseeable risk of default to bring about modifications of current loans. Following a letter from the Chairman Frank, Chairman Kanjorski and other members of the House, the Securities Exchange Commission's concurrence statement created confidence in the market that investors could permit the modification of current loans that are in imminent or foreseeable risk of default. This resulted in the American Securitization Forum's recommended standards for "Fast Track" modifications, which allow for more wholesale modifications of certain adjustable rate mortgages where borrowers are current, but at risk of defaulting in the future.[3]

Other actions by the investor community were also significant, including clarification that servicers can act in the best interests of the pool as a whole, rather than those investors that have first dollar risk.

Many servicers have also instituted a policy to "pause" foreclosure actions where reasonably possible and appropriate to allow processing and approval of loss mitigation requests.

We believe these industry practices have allowed servicers to do more loss mitigation and help keep borrowers in their homes.

The willingness of stakeholders to address alternatives to foreclosure has resulted in 1,178,000 repayment plans and modifications executed from July 2007 through February 2008, according to HOPE NOW. This is an unprecedented response by the mortgage industry and investor community.

Recommendations

To the extent that a safe harbor could hamper liquidity in the mortgage markets, MBA believes that public and private policy efforts should be focused on providing lenders and borrowers more options to work together to refinance people out of mortgages they have trouble paying. Therefore, we believe policy makers should focus on efforts that will help create new loan products and support a secondary market for those loans. These products should:

(1) allow borrowers behind on their payments to refinance their mortgage obligations to a lower rate or more favorable terms, thus overcoming the

[2] See: http://www.hopenow.com/members/members.html for current HOPE NOW members

[3] American Securitization Forum, *Streamlined Foreclosure and Loss Avoidance Framework for Securitized Subprime Adjustable Rate Mortgage Loans*, Dec. 6, 2007.

financial stress that caused the delinquency (whether job loss, mortgage interest rate increase, health emergency or other unanticipated increase in expenses); and

(2) allow borrowers who are "upside down" on their mortgages (their mortgage balance is now higher than their property value) the opportunity to refinance to a more affordable rate or term.

Chairman Frank, together with members of this Subcommittee, is currently working on such a proposal, and we look forward to working cooperatively and constructively throughout that process. We also applaud the Federal Housing Administration (FHA) for their recent announcement to increase access to FHASecure for more borrowers experiencing financial difficulties.

While Congress, government entities and the mortgage industry cannot save every homeowner from foreclosure, an appropriately designed refinance program will help many homeowners by overcoming some of the contractual and "interpretational" issues that are obstacles to work outs and modifications and with which H.R. 5579 is meant to assist.

An ideal refinance program and one that would ensure the greatest execution would limit principal write downs, allow investors to recover write downs, be eligible to delinquent borrowers (within certain limitations) and assist borrowers who are upside down on their mortgages (again within certain limitations).

Conclusion

The Mortgage Bankers Association appreciates your efforts to assist servicers in their efforts to help borrowers stay in their homes. Servicers will continue to use their contractual authority to perform loss mitigation to the extent permissible and prudent. It remains unclear to us, however, whether the benefits of H.R. 5579 outweigh the potential harm that the bill may cause the mortgage market overall. Efforts to amend consummated contracts by statute, without investor approval, may cause investors to avoid the mortgage market.

MBA continues to believe that helping the market create and offer innovative products will significantly help borrowers avoid default and foreclosure. Refinance programs, if structured properly, can benefit the borrower while avoiding the "investor approval" problem. Refinancings can also tap the significant capacity of lenders' production departments to more quickly help more borrowers.

Thank you for the opportunity to address the Subcommittee today. I will be happy to address any questions you may have.

Thacher
Proffitt

TESTIMONY OF MARLO YOUNG
PARTNER
THACHER PROFFITT & WOOD LLP

BEFORE THE
HOUSE SUBCOMMITTEE ON CAPITAL MARKETS,
INSURANCE, AND GOVERNMENTAL SPONSORED ENTERPRISES

UNITED STATES HOUSE OF REPRESENTATIVES

HEARING ON H.R. 5579, THE EMERGENCY MORTGAGE LOAN MODIFICATION ACT OF 2008

APRIL 15, 2008

Chairman Kanjorski, Ranking Member Pryce, Congressman Castle and distinguished Members of the Subcommittee:

Good afternoon and thank you for the opportunity to testify here today. My name is Marlo Young and I am honored to be here representing Thacher Proffitt & Wood to discuss the Emergency Mortgage Loan Modification Act of 2008 and ways to prevent foreclosures and mitigate losses. We commend you for calling this hearing, and look forward to offering our views on these important matters.

Background

I am a partner with Thacher Proffitt & Wood, a financial services law firm whose practice includes the representation of various banking and financial institutions in connection with the securitization of various asset types including residential mortgage loans. Thacher Proffitt also recently served as outside counsel to the American Securitization Forum (ASF) for its loan modifications task force. In that role we helped to prepare a number of ASF statements and publications, including the streamlined loan modification framework developed by the ASF and the HOPE NOW Alliance that was announced by President Bush in December 2007 (ASF Framework).

Impediments to Loan Modifications

Although a substantial number of loans have been modified to date, servicers have been unable to complete the desired amount of loan modifications due to operational challenges, including technological challenges presented in administering large volumes of loan modifications. The servicer must choose among a variety of loss mitigation alternatives to achieve a sustainable arrangement with the borrower that is also in the best interest of investors. This can be a very labor intensive and time consuming endeavor for the servicer, and unfortunately there is not one particular type of loan modification that is suitable in every circumstance.

Establishing early contact with borrowers is important to the success of loan modifications. In most cases, such contact is necessary for a servicer to determine the appropriate loan modification and the borrower's ability to pay under the modified loan terms. Although borrowers have expressed frustration in contacting lenders to modify the payment terms of their loan, many servicers have reported difficulties communicating with borrowers.

The loan modification process would benefit from more streamlined approaches and enhanced automation. The ASF Framework released last December was a worthy attempt at streamlining the loan modification process. However, one of the criteria developed to support the determination that a streamlined loan modification is in the best interest of investors was based on the magnitude of the payment shock experienced when the mortgage rate resets. Ironically, the recent reduction in short term rates lessened the anticipated payment shock and has resulted in a smaller number of adjustable rate loans that are eligible for modification under the streamlined framework.

Servicing agreements do not create disincentives for servicers to make loan modifications nor do they create incentives to choose to foreclose over making a loan modification. Servicers are only entitled to their servicing fee so long as the loan is outstanding and there are no additional fees or other entitlements for pursing a foreclosure. The servicer is entitled to out-of-pocket costs whether it forecloses or makes a loan modification.

H.R. 5579, Emergency Mortgage Loan Modification Act of 2008

We do not believe there are major legal or contractual impediments to making loan modifications. Rather, our study of typical servicing agreement provisions for the ASF concluded that generally, servicers of loans in securitizations have the authority to implement loan modifications and other forms of loss mitigation alternatives, when the loan is in default or default is reasonably foreseeable, provided that the action taken is in accordance with accepted servicing practices and is in the best interest of investors.

The provisions of Section 2(a) of the Emergency Mortgage Loan Modification Act of 2008 employ concepts that are consistent with these servicing provisions. Although most servicing agreements generally permit loan modifications, some agreements may provide for some limitations on modifications, such as a limit on the number of loans that can be modified or a minimum modified mortgage rate. However, we do not think the standards set forth in Section 2(a) would conflict with the general standards of typical servicing agreements.

We support the inclusion of the provision in Section 2(a) of the bill that reads "Absent specific contractual provisions to the contrary." Removing any requirement that a loan modification or other loss mitigation not contradict the terms of the servicing agreement may interfere with the existing contractual terms of servicing agreements, and result in actions that are not necessarily in the best interest of investors.

We think Section 2(a) should clarify that the servicer should select from all available loss mitigation alternatives the one that maximizes recovery, and not compare the alternative selected solely to foreclosure. We believe that "accepted servicing practices" is an evolving standard and that the servicer should be able to rely on reasonable policies and procedures that it adopts over time. It should also be recognized that such policies and procedures may not be the same for each servicer. In addition, as long as the servicer's procedures for evaluating the net present value of a particular loss mitigation alternative are reasonable, the servicer's decision should not be challenged on the grounds that other evaluation procedures might have led to a different result.

We question, however, whether the safe harbor in Section 2(b) is necessary or desirable, if the standards in Section 2(a) are adopted. As Section 2(a) requires that any loss mitigation action not contradict any terms in the servicing agreement and sets forth standards that are generally consistent with existing servicing provisions, the safe harbor contained in Section 2(b) does not appear to be necessary. In fact, the safe harbor provision may interfere with existing contractual provisions and bring into question the rights of investors under servicing agreements. Finally, we question whether the concept of "qualified loan modification" contained in Section 2(d)(1) of the bill is too limiting. Imposing a five-year modification term, for example, may conflict with the applicable servicing standard and hinder the servicer's ability to maximize proceeds and do what is in the best interest of investors.

Policy Options For Facilitating Loan Modifications

We believe that portions of the bill, in particular Section 2(a), would be helpful in providing certainty regarding appropriate loss mitigation standards. In addition, Section 2(a) would clarify that the phrase "in the best interest of investors" refers to all investors in a given securitization trust in the aggregate, without regard to the effect on any specific class, which would make the servicer's task of determining the appropriate loss mitigation more manageable.

We believe that a major impediment to a servicer utilizing the full range of loss mitigation alternatives is the absence of an available loan product for funding a short refi, or a refinancing that pays off only a portion of the existing first lien, for borrowers who are in default or imminent default. There presently is not a suitable loan product in the mortgage industry for this purpose. Accordingly, we think that proposals to expand FHA Secure, or create a new FHA program for this purpose, could serve as a key role in reducing foreclosures.

However, we would suggest that an FHA product targeted to short refis for borrowers in default or imminent default, should be available to refinance any type of loan, not just adjustable rate subprime loans at the time of the first rate adjustment. Given that reduced short term rates have had a mitigating effect on ARM rate increases, property value decline may now be a more significant cause of default than rate shock.

In addition, any FHA product developed to support short refis of defaulted loans should be one that servicers may be able to select, in a significant number of cases, as the alternative that maximizes recoveries to investors. In this regard, the servicer should be able to compare the short refi against other alternatives such as a rate reduction modification, which might result in no reduction of principal, or a short sale that would result in a recovery much closer to 100% of current loan-to-value than would a foreclosure. Proposals for any FHA product that result in short refis in the range of 85% of current value may not provide the servicer with a short refi alternative that it can reasonably determine maximizes recoveries to investors.

Finally, we think any such proposals for FHA products for short refis of defaulted loans should not mandate that any upside which might result from improved future property values go to either the FHA or to the borrower. Rather, these proposals should leave open the possibility that any such excess go back to the investors in the existing loans, to the extent of the loan amounts originally funded by them.

Conclusion

I thank you for the opportunity to participate in today's hearing. Finding solutions to the current mortgage and housing crises and preventing foreclosures should be a high priority for all market participants and our communities. Again, I commend your leadership on these important matters.

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Walter J. Witek, Jr., Vice President
Gary Weaver, Vice President

April 3, 2008

The Honorable Paul Kanjorski
2188 Rayburn House Office Building
Washington, DC 20515

Dear Representative Kanjorski:

On behalf of more than 1.3 million members of the National Association of REALTORS® (NAR), I am writing in support of legislation to address a serious problem in today's mortgage market—reluctance by some servicers to modify problematic mortgage loans.

The National Association of REALTORS® is America's largest trade association, including NAR's five commercial real estate institutes and its societies and councils. REALTORS® are involved in all aspects of the residential and commercial real estate industries and belong to one or more of some 1,500 local associations or boards, and 54 state and territory associations of REALTORS®.

H.R. 5579, the "Emergency Mortgage Loan Modification Act of 2008," would establish standards for loan modifications by servicers. Your bill would clarify that the duty servicers owe to maximize benefits for investors is a duty owed to all investors, in the aggregate, and not any individual investors or groups of investors. It would also include standards for loan modifications. Servicers that act in accordance with the standards would be protected from lawsuit in connection with the loan modification. Your bill would not override any inconsistent conditions in the contract between the servicer and the investors.

This approach shows promise for addressing one of the most serious problems faced by homeowners facing foreclosure. While we are not taking a position on the specifics of the bill at this time, and will be most interested in hearing of any concerns raised by servicers and investors, we hope that this approach can become a significant part of the solution for borrowers struggling to keep their homes.

Thank you for the opportunity to address this important issue.

Sincerely,

Richard F. Gaylord, CIPS, CRB, CRS, GRI
2008 President, National Association of REALTORS®