CONGRESSIONAL OVERSIGHT PANEL

DECEMBER OVERSIGHT REPORT *

A REVIEW OF TREASURY'S FORECLOSURE PREVENTION PROGRAMS

DECEMBER 14, 2010.—Ordered to be printed

* Submitted under Section 125(b)(1) of Title 1 of the Emergency Economic Stabilization Act of 2008, Pub. L. No. 110–343

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CONGRESSIONAL OVERSIGHT PANEL

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CONTENTS

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EXECUTIVE SUMMARY *

In April 2010, in its most recent report on Treasury's foreclosure prevention programs, the Panel raised serious concerns about the timeliness, accountability, and sustainability of Treasury's efforts. As the Panel noted at the time, "It now seems clear that Treasury's programs, even when they are fully operational, will not reach the overwhelming majority of homeowners in trouble . . . . Treasury is still struggling to get its foreclosure programs off the ground as the crisis continues unabated."

In the intervening eight months, Treasury has tweaked its main foreclosure prevention effort, the Home Affordable Modification Program (HAMP), but the changes have not resolved the Panel's core concerns. The Panel now estimates that, if current trends hold, HAMP will prevent only 700,000 to 800,000 foreclosures—far fewer than the 3 to 4 million foreclosures that Treasury initially aimed to stop, and vastly fewer than the 8 to 13 million foreclosures expected by 2012. Because Treasury's authority to restructure HAMP ended on October 3, 2010, the program's prospects are unlikely to improve substantially in the future.

In some regards, the program's failure to make a dent in the foreclosure crisis may seem surprising. HAMP's premise was straightforward: Because the foreclosure process allows lenders to recover only a small fraction of the value of a mortgage loan, lenders should generally prefer to avoid foreclosure by voluntarily reducing a borrower's monthly payments to affordable levels. Through HAMP, Treasury attempted to sweeten this deal by offering incentive payments to all parties to a mortgage loan modification. Yet despite the apparent strength of HAMP's economic logic,

* The Panel adopted this report with a 5–0 vote on December 13, 2010.

the program has failed to help the vast majority of homeowners facing foreclosure.

A major reason is that mortgages are, in practice, far more complicated than a one-to-one relationship between borrower and lender. In particular, banks typically hire loan servicers to handle the day-to-day management of a mortgage loan, and the servicer's interests may at times sharply conflict with those of lenders and borrowers. For example, although lenders suffer significant losses in foreclosures, servicers can turn a substantial profit from foreclosure-related fees. As such, it may be in the servicer's interest to move a delinquent loan to foreclosure as soon as possible. HAMP attempted to correct this market distortion by offering incentive payments to loan servicers, but the effort appears to have fallen short, in part because servicers were not required to participate. Another major obstacle is that many borrowers have second mortgages from lenders who may stand to profit by blocking the modification of a first mortgage. For these reasons among many others, HAMP's straightforward plan to encourage modifications has proven ineffective in practice.

While HAMP's most dramatic shortcoming has been its poor results in preventing foreclosures, the program has other significant flaws. For example, despite repeated urgings from the Panel, Treasury has failed to collect and analyze data that would explain HAMP's shortcomings, and it does not even have a way to collect data for many of HAMP's add-on programs. Further, Treasury has refused to specify meaningful goals by which to measure HAMP's progress, while the program's sole initial goal—to prevent 3 to 4 million foreclosures—has been repeatedly redefined and watered down. Treasury has also failed to hold loan servicers accountable when they have repeatedly lost borrower paperwork or refused to perform loan modifications. Treasury has essentially outsourced the responsibility for overseeing servicers to Fannie Mae and Freddie Mac, but both companies have critical business relationships with the very same servicers, calling into question their willingness to conduct stringent oversight. Freddie Mac in particular has hesitated to enforce some of its contractual rights related to the foreclosure process, arguing that doing so "may negatively impact our relationships with these seller/servicers, some of which are among our largest sources of mortgage loans." Treasury bears the ultimate responsibility for preventing such conflicts of interest, and it should ensure that loan servicers are penalized when they fail to complete loan modifications appropriately.

Many of the problems now plaguing HAMP are inherent in its design and cannot be resolved at this late date. Other problems, however, can still be mitigated. For instance, Treasury should enable borrowers to apply for loan modifications more easily—for example, by allowing online applications. Treasury should also carefully examine HAMP's track record to pin down the factors that define successful loan modifications so that similar modifications can be encouraged in the future.

Perhaps most critically, Treasury should carefully monitor and, where appropriate, intervene in cases in which borrowers are falling behind on their HAMP-modified mortgages. Preventing redefaults is an extremely powerful way of magnifying HAMP's impact, as each redefault prevented translates directly into a borrower keeping his home. Delinquencies that are flagged in their early stages can potentially be brought current through a repayment plan, but delinquencies that are left unchecked have the potential to undermine even the modest progress made by HAMP. Worse still, each redefault represents thousands of taxpayer dollars that have been spent merely to delay rather than prevent a foreclosure.

Finally, Treasury should accept that HAMP will not reach its original goals and provide a meaningful framework for evaluating the program in the future. Treasury continues to state that HAMP will expend $30 billion in Troubled Asset Relief Program funding, yet the Congressional Budget Office recently estimated that all of Treasury's foreclosure programs combined will spend only $12 billion. Given the Panel's cost estimates for Treasury's other foreclosure-related efforts, HAMP thus appears likely to spend only around $4 billion. Had Treasury acknowledged this reality before its crisis authority expired, it could have made material changes to HAMP or reallocated the money to a more effective program. Now, that option is gone.

For this reason, Treasury's reluctance to acknowledge HAMP's shortcomings has had real consequences. Absent a dramatic and unexpected increase in HAMP enrollment, many billions of dollars set aside for foreclosure mitigation may well be left unused. As a result, an untold number of borrowers may go without help all because Treasury failed to acknowledge HAMP's shortcomings in time.

SECTION ONE

Introduction

The Emergency Economic Stabilization Act (EESA), the October 2008 legislation that granted Treasury the authority to create the Troubled Asset Relief Program (TARP), included a mandate that TARP funds be used in a manner that "protects home values" and "preserves homeownership."[1] To fulfill that mandate, Treasury in 2009 allocated $50 billion in TARP funds for a new mortgage modification program called the Home Affordable Modification Program (HAMP).

The same legislation established the Congressional Oversight Panel, along with a specific charge to issue periodic reports on TARP foreclosure mitigation efforts. The Panel's first foreclosure mitigation oversight report was issued in March 2009, concurrent with the announcement of HAMP. The report established numerous standards for evaluating the Administration's foreclosure mitigation program, including: (1) whether it resulted in affordable monthly payments; (2) whether it dealt with negative equity; (3) whether it addressed second liens; and (4) whether it counteracted incentives for mortgage servicers not to modify troubled loans. Seven months later, in October 2009, the Panel examined the Administration's implementation of HAMP. This report identified three main concerns with the program: (1) that it lacked sufficient scope to prevent many foreclosures, including those caused by unemployment and negative equity; (2) that it was not achieving scale quickly enough; and (3) that it was not providing a permanent solution to homeowners who needed help.

The Panel again assessed HAMP in April 2010. Foreclosures were continuing at a rapid pace, and the report found that Treasury's response continued to lag the crisis. The Panel articulated three major concerns with HAMP: (1) the failure of the program to deal with the foreclosure crisis in a timely way; (2) the unsustainable nature of many HAMP modifications, given the large debt load and negative equity that many participating homeowners continued to carry; and (3) the need for greater accountability in HAMP, particularly with regard to the activities of participating servicers.

Treasury's foreclosure mitigation programs have grown and evolved since the initial announcement in March 2009. More TARP-funded foreclosure prevention initiatives were announced shortly before the release of the Panel's most recent foreclosure report; those programs are discussed in Section B.4 of this report.[2] However, this month's report focuses primarily on HAMP, since it is Treasury's marquee foreclosure prevention initiative, and be-

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[1] 12 U.S.C. § 5201(2)(A), (B). For a discussion of the authority of the Secretary of the Treasury to use TARP funds to create a program such as HAMP, see Congressional Oversight Panel, *April Oversight Report: Evaluating Progress on TARP Foreclosure Mitigation Programs,* at 147–171 (Apr. 14, 2010) (online at cop.senate.gov/documents/cop-041410-report.pdf) (hereinafter "April 2010 Oversight Report").

[2] Treasury has since created two additional foreclosure prevention programs under the TARP: the Hardest Hit Fund (HHF), which provides foreclosure prevention funding to 19 states and the District of Columbia, and the Federal Housing Administration (FHA) Short Refinance Program, which will allow for the refinancing of certain mortgages by the FHA.

cause many of the other initiatives remain in early stages, with no record of results on which to be assessed.[3]

Part One: Where HAMP Stands Today

A. Background

Despite government and private sector efforts to modify troubled loans and thus stop "preventable" foreclosures, the number of foreclosures remains extremely high, with approximately 250,000 foreclosure starts and over 100,000 foreclosure completions per month.

Figure 1 below shows the number of foreclosure starts and completions each month.

FIGURE 1: FORECLOSURE STARTS AND COMPLETIONS BY MONTH (JULY 2007–SEPTEMBER 2010)[4]

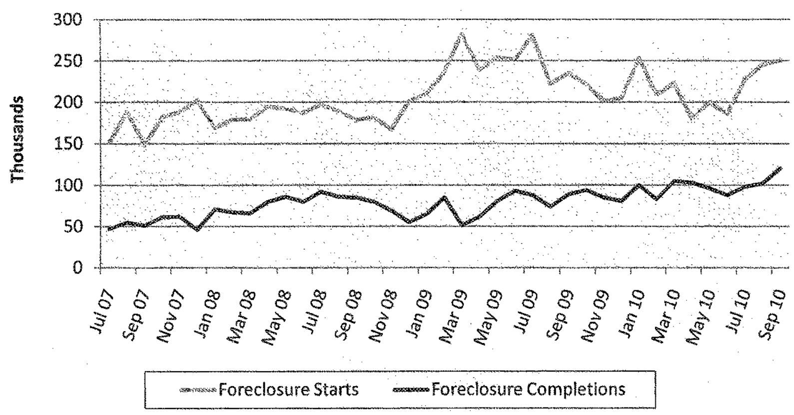
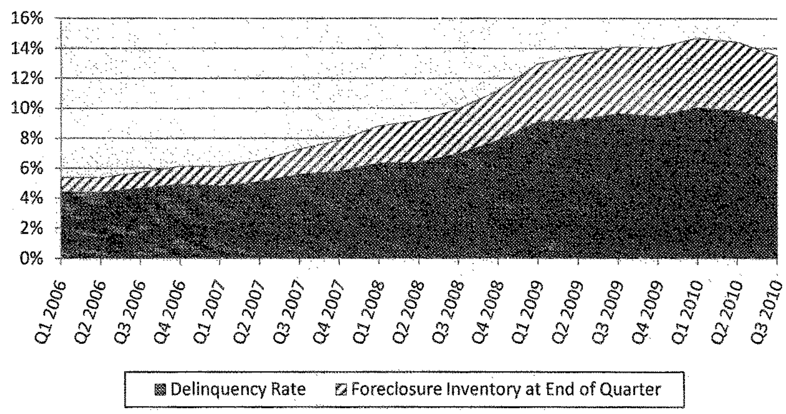


Figure 2 below shows the percentage of all mortgages that are in delinquency and the percentage of all mortgages that are counted as foreclosure inventory, meaning they are somewhere in the foreclosure process. Please note that the foreclosure inventory is stacked on top of delinquency, that is, delinquency is currently around 10 percent, and foreclosure inventory is roughly 4 percent, not 14 percent. Although both factors are at historically high levels, they have been relatively steady for the past two years.

[3] For an analysis of the programs' structures, see April 2010 Oversight Report, *supra* note 1, at 8–29.

[4] HOPE NOW Alliance, *Appendix—Mortgage Loss Mitigation Statistics: Industry Extrapolations* (Monthly for Dec. 2008 to Nov. 2009) (online at www.hopenow.com/industry-data/HOPE%20NOW%20National%20Data%20July07%20to%20Nov09%20v2%20(2).pdf); HOPE NOW Alliance, *Industry Extrapolations and Metrics* (May 2010) (online at www.hopenow.com/industry-data/HOPE%20NOW%20Data%20Report%20(May)%2006-21-2010.pdf); HOPE NOW Alliance, *Industry Extrapolations and Metrics* (Sept. 2010) (online at www.hopenow.com/industry-data/HOPE%20NOW%20Data%20 Report%20(September)%20101010%20v2.pdf) (hereinafter "HOPE NOW Alliance Industry Extrapolations and Metrics").

FIGURE 2: DELINQUENCY AND FORECLOSURE RATES (Q1 2006–Q3 2010) [5]



The Federal Reserve has recently estimated foreclosures over the next two years: "All told, we expect about two and one-quarter million foreclosure filings [in 2010] and again next year, and about two million more in 2012." [6] The Center for Responsible Lending has also released a foreclosure forecast of 9 million foreclosures between 2009 and 2012.[7] Since approximately 5 million foreclosures have been completed since the beginning of 2009, this seems to be generally in line with the Federal Reserve's prediction.

B. Pre-HAMP Foreclosure Mitigation Efforts

In the wake of the financial crisis of late 2008, Treasury developed HAMP as the latest in a series of federal government initiatives to stem the growing foreclosure problem. At the time, foreclosures had been rising for several years already, leading to an increase in the number of empty homes owned by banks and weakening the banking system at a time when policymakers felt that restoring economic and bank stability was crucial. The history of prior efforts, which met with limited success, provides a useful context for examining HAMP and its performance to date.

As the housing boom peaked and began its long downward slide in 2006, policymakers appeared to take for granted that foreclosures would not require government intervention. In previous housing recessions of the post-WWII era, foreclosures and mortgage modifications had been left to the discretion of private lenders and

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[5] Mortgage Bankers Association, *National Delinquency Survey Q3 2010* (Nov. 18, 2010).

[6] Sarah Bloom Raskin, member, Board of Governors of the Federal Reserve System, Remarks at the National Consumer Law Center's Consumer Rights Litigation Conference, Boston, Massachusetts, *Problems in the Mortgage Servicing Industry,* at 2 (Nov. 12, 2010) (online at www.federalreserve.gov/newsevents/speech/bloomraskin20101112a.pdf). *See also* House Committee on Financial Services, Written Testimony of Elizabeth A. Duke, member, Board of Governors of the Federal Reserve System, *Robo-Signing, Chain of Title, Loss Mitigation, and Other Issues in Mortgage Servicing,* at 5 (Nov. 18, 2010) (online at financialservices.house.gov/Media/file/hearings/111/Duke111810.pdf) ("Over the first half of this year, we have seen a further 1.2 million foreclosure filings, and an additional 2.4 million homes were somewhere in the foreclosure pipeline at the end of June. All told, we expect about 2.25 million foreclosure filings this year and again next year, and about 2 million more in 2012.").

[7] Center for Responsible Lending, *Soaring Spillover* (May 2009) (online at www.responsiblelending.org/mortgage-lending/research-analysis/soaring-spillover-3 9.pdf).

loan servicers.[8] After all, modifications generally maximize value for the lender or investor as compared to foreclosure, so it was logical to assume that such modifications would occur. Yet, by mid-2007, it appeared that many foreclosures were proceeding even in instances where loan modifications would appear to be economically preferable to the lender or mortgage investors.

Policymakers continued to look to the private sector for a more aggressive response to the situation, but began to nudge them toward a more organized response in hopes of achieving greater results. As a result, in October 2007, the HOPE NOW Alliance was formed as a voluntary coalition of mortgage companies and industry organizations designed to centralize and coordinate foreclosure mitigation efforts. Although both Treasury and the Department of Housing and Urban Development (HUD) were consulted and strongly promoted the effort, the federal government is not an official sponsor.[9] Initially, HOPE NOW met with limited success. For instance, a 2009 study found that only 49 percent of HOPE NOW workouts had reduced the borrower's monthly payment, and 34 percent had actually resulted in a higher monthly payment.[10] However, HOPE NOW recently reported that 91 percent of the nearly 150,000 modifications completed in August 2010 involved payment reductions.[11] As of August 2010, HOPE NOW participants report a total of 10.7 million mortgage "solutions" since the inception of the alliance, including 3.2 million proprietary modifications. However, the Mortgage Metrics Report compiled by the Office of Comptroller of the Currency and the Office of Thrift Supervision reports only 1.3 million such modifications.[12] Proprietary modifications are discussed further in Section E below.

The first official federal government foreclosure mitigation program was FHA Secure, announced in August 2007, which refinanced adjustable-rate mortgages into fixed-rate mortgages insured by the Federal Housing Administration (FHA). FHA Secure permitted the refinancing of delinquent and underwater borrowers, which was rare in the private sector. However, delinquencies had to be attributable to the loan resetting, and borrowers could not generally show any delinquencies in the six-month period prior to the rate reset. Borrowers participating in this program were therefore able to refinance their existing underwater mortgages into

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[8] The Home Owners' Loan Corporation, a depression-era federal government mortgage modification program, is discussed in Annex I.

[9] *See* U.S. Department of the Treasury, *Statement by Secretary Henry M. Paulson, Jr. on Announcement of New Private Sector Alliance—HOPE NOW* (Oct. 10, 2007) (online at 205.168.45.71/press/releases/hp599.htm).

[10] Congressional Oversight Panel, *March Oversight Report: Foreclosure Crisis: Working Toward a Solution,* at 31 (Mar. 6, 2009) (online at cop.senate.gov/documents/cop-030609-report.pdf) (hereinafter "March 2009 Oversight Report"). *See also* Sonia Garrison et al., *Continued Decay and Shaky Repairs: The State of Subprime Loans Today,* Center for Responsible Lending Study, at 7 (Jan. 2009) (online at www.responsiblelending.org/mortgage-lending/research-analysis/continued_decay_and_shaky_repairs.pdf). This study reported only 20 percent of modifications resulted in lower payments.

[11] HOPE NOW Alliance, *HOPE NOW: Nine out of Ten Proprietary Loan Mods in August Included Principal & Interest Payment Reduction* (Oct. 7, 2010) (online at www.hopenow.com/press_release/files/August%202010%20Data%20Release_FINAL.pdf).

[12] *See* Congressional Oversight Panel, Written Testimony of Joseph H. Evers, deputy comptroller for large bank supervision, Office of the Comptroller of the Currency, *COP Hearing on TARP Foreclosure Mitigation Programs,* at 4, 7–8 (Oct. 27, 2010) (online at cop.senate.gov/documents/testimony-102710-evers.pdf) (stating that loan servicers modified 1,239,896 loans between the start of 2008 and the end of the first quarter of 2010, including 121,731 HAMP modifications, and that an additional 164,473 non-HAMP modifications were done in the second quarter of 2010).

safer loans at a time when lenders were tightening underwriting standards and underwater borrowers were unable to refinance in the private market. As the Panel has noted previously, however, this was accomplished at the cost of having the taxpayer insure a large number of negative equity mortgages. FHA Secure was closed down at the end of 2008. Although the program refinanced nearly half a million loans, only 4,128 of these were delinquent at the time of refinancing. The Panel has previously attributed FHA Secures failure to its restrictive borrower criteria.[13]

Following the lackluster results stemming from the private sector initiatives, policymakers determined that a new government program was the next appropriate step. Accordingly, HOPE for Homeowners was established by Congress in July 2008 to permit FHA insurance of refinanced distressed mortgages. While less restrictive in some areas than FHA Secure, the program did not guarantee negative equity loans. Since the goal of the program was specifically to encourage principal reduction modifications of negative equity loans, guaranteeing them as is would have defeated the purpose, as well as likely been impossible under FHA‘s 97 percent LTV statutory limit. Nonetheless, although HOPE for Homeowners was predicted to help 400,000 homeowners, it managed to refinance only a handful of loans. This was likely due to the program‘s poor initial design, lack of flexibility, and its reliance on voluntary principal write-downs, which lenders were very reluctant to do, a pattern also seen in HAMP.[14]

In the same month HOPE for Homeowners was created, the Federal Deposit Insurance Corporation (FDIC) took over IndyMac, one of the largest subprime lenders. Soon afterwards, the FDIC announced a loan modification program to assist the 65,000 delinquent borrowers with loans in IndyMac‘s non-securitized portfolio. Although no FDIC funds were allocated specifically for these modifications, loss-sharing agreements were signed with the purchasers of IndyMac‘s assets. A number of other, similar efforts were instituted with smaller failed lenders taken over by the FDIC. The IndyMac program and other FDIC foreclosure mitigation efforts had limited reach, but may have influenced the structure of HAMP.[15] This and other aspects of the FDIC IndyMac program are discussed in more detail in Section I.2.

Even with increasing government intervention throughout this timeframe, foreclosures continued to surge. It became clear that the private sector was either unable or unwilling to conduct mortgage modifications on its own of a scope and scale necessary to stem the tide. Most likely, this was due to rational behavior on the part of

[13] March 2009 Oversight Report, *supra* note 10, at 35. *See also* Kate Berry, *HUD Mulling How to Widen FHA Refi Net,* American Banker (Feb. 15, 2008) (online at www.americanbanker.com/issues/173_33/-344173-1.html); Michael Corkery, *Mortgage 'Cram-Downs' Loom as Foreclosures Mount,* Wall Street Journal (Dec. 31, 2008) (online at online.wsj.com/article/SB123068005350543971.html).

[14] *See* March 2009 Oversight Report, *supra* note 10, at 36. *See also* Dina ElBoghdady, *HUD Chief Calls Aid on Mortgages A Failure,* Washington Post (Dec. 17, 2008) (online at www.washingtonpost.com/wp-dyn/content/article/2008/12/16/AR2008121603177.html).

[15] *See* March 2009 Oversight Report, *supra* note 10, at 32–33; Congressional Oversight Panel, *October Oversight Report: An Assessment of Foreclosure Mitigation Efforts After Six Months,* at 83–84 (Oct. 9, 2009) (online at cop.senate.gov/documents/cop-100909-report.pdf) (hereinafter "October 2009 Oversight Report"). *See also* Charles Duhigg, *Fighting Foreclosures, F.D.I.C. Chief Draws Fire,* New York Times (Dec. 11, 2008) (online at www.nytimes.com/2008/12/11/business/11bair.html).

servicers. As discussed below, there are incentives built into the mortgage servicing system that encourage servicers to prefer foreclosure in many cases, and discourage certain types of modifications. HAMP, and specifically its servicer incentive payments, were created to overcome the additional costs that servicers incur in modifying loans, and to compensate them in part for the income they may forgo by choosing modification over foreclosure.

C. HAMP's Structure

HAMP is designed to provide a path to modification in those cases in which modification is the economically preferable outcome, from the perspective of the lender or investor who owns the loan, to foreclosure. Because such modifications are in the interest of both the borrower and the lender, it would seem to follow that mortgage servicers should be providing modifications in those cases without any payments from the government. As observed by David Stevens, commissioner of the Federal Housing Administration, "To be frank, too often during this crisis, that private sector engagement hasn't happened. In some instances, we've seen market actors refuse to participate. In others, we've seen them participate half-heartedly." [16] The failure of the private sector to reduce debt service payments on a substantial number of mortgages in part led to Treasury's decision to create HAMP.

HAMP provides financial incentives to mortgage servicers to modify mortgages for homeowners at risk of default, and incentives for the beneficiaries of these modifications to stay current on their mortgage payments going forward.[17] Participation in the program by servicers is voluntary, but once a servicer elects to participate, adherence to the program standards is mandatory for all the servicer's loans. If a participating servicer has a borrower who qualifies for HAMP, the lender must first reduce monthly payments until they are no more than 38 percent of the borrower's gross monthly income. Treasury will then match, dollar for dollar, further reductions required to bring the monthly payments down to 31 percent of the borrower's income.

Only borrowers whose mortgage servicers have opted into the program may apply for assistance. Pooling and servicing agreements (PSAs) for securitized mortgages may also limit the latitude that servicers have to modify loans.[18] Furthermore, borrowers must meet the following criteria to be eligible:

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[16] David H. Stevens, commissioner, Federal Housing Administration, Remarks at the Mortgage Bankers Association Annual Convention, at 7 (Oct. 26, 2010).

[17] Servicers of government-sponsored enterprise (GSE) mortgages are required to participate in HAMP for their GSE portfolio. Servicers of non-GSE mortgages may elect to sign a servicer participation agreement (SPA) in order to participate in the program. Once an agreement has been signed, the participating servicer must evaluate all mortgages under HAMP unless the participation contract is terminated.

[18] The decision to modify securitized mortgages rests with the servicer, and servicers are instructed to manage loans as if for their own account and maximize the net present value of the loan. Nevertheless, some PSAs contain additional restrictions that can hamper servicers' ability to modify mortgages. Sometimes the modification is forbidden outright, sometimes only interest rates can be adjusted, not principal, and sometimes there are limitations on the amount by which interest rates can be adjusted. Other times the total number of loans that can be modified is capped (typically at 5 percent of the pool), the number of times a loan may be modified will be capped, or the number of modifications in a year will be capped. Generally, the term of a loan cannot typically be extended beyond the last maturity date of any loan in the securitized pool. Additionally, servicers are sometimes required to purchase any loans they modify at the

Continued

- The home must be owner-occupied, not vacant, and not condemned;
- The remaining balance on a single unit home must be no more than $729,750, with higher limits for properties containing up to four units;
- The borrower must be delinquent, or default must be reasonably foreseeable, and the borrower must demonstrate financial hardship, including the fact that he or she has insufficient liquid assets to make the required monthly payments; and
- The borrower must have a monthly "front-end" debt-to-income (DTI) ratio of more than 31 percent, meaning that the monthly mortgage payment must be greater than 31 percent of the borrower's gross monthly income.[19]

If a borrower meets these criteria, the servicer must then use Treasury's Net Present Value (NPV) model to determine whether or not a HAMP modification makes economic sense from the lender's perspective. The NPV model calculates net present values for the expected income from the mortgage under a HAMP modification, and the expected income with no modification (generally a foreclosure and home sale scenario). The two figures are then compared. If the mortgage has a greater value under the HAMP modification, it is said to be "NPV positive," in which case a participating servicer *must* offer the borrower a HAMP modification.

HAMP prescribes a "waterfall" to determine what type of modification should be offered. First, the servicer should consider whether lowering the loan's interest rate, to as low as 2 percent, would result in a monthly front-end DTI ratio of less than 31 percent. If the ratio would still be too high, the next step should be extending the loan period out to as long as 40 years. If the DTI ratio would still be greater than 31 percent, the final step is principal forbearance.[20]

Once approved for assistance through HAMP, a borrower must successfully complete a trial period, typically three months, during which the borrower makes payments on the modified mortgage. A borrower who remains current through the trial period becomes eligible for a permanent modification, under which the terms of the trial modification remain in effect for a period of five years.[21] For each year that the borrower remains current under the modified mortgage, he or she receives a $1,000 incentive payment from HAMP, for up to five years. After the five year term is up, the interest rate on the loan can increase by a maximum of 1 percent per

face value outstanding (or even with a premium). This functions as an antimodification provision. *See* March 2009 Oversight Report, *supra* note 10, at 42–44.

[19] U.S. Department of the Treasury, *Introduction of the Home Affordable Modification Program,* Supplemental Directive 09–01, at 6 (Apr. 6, 2009) (online at www.hmpadmin.com/portal/programs/docs/hamp_servicer/sd0901.pdf) (hereinafter "Introduction of the Home Affordable Modification Program,"). "Monthly payment" means monthly mortgage payment before modification, including both principal and interest, plus applicable taxes, hazard insurance, flood insurance, condominium association fees and homeowners' association fees, as applicable. "Front-end" DTI refers to a ratio of the borrower's monthly mortgage payment to their monthly income, as opposed to a "back-end" DTI which compares all of a borrowers debt service payments (including credit cards, car payments, etc.) to their income.

[20] As described in Section F, an alternate waterfall moves the principal reduction option to earlier in the process.

[21] "Current" means that no payment is more than 30 days overdue. *See* Introduction of the Home Affordable Modification Program, *supra* note 19, at 17–18.

year until it reaches the prevailing Freddie Mac average interest rate at the time the HAMP modification was made. As of December 2, 2010, Freddie Mac's average interest rate on a 30-year fixed rate conforming mortgage is 4.46 percent. Incentive payments also flow to the mortgage servicer and investor.[22] For mortgages that are not backed by government-sponsored entities Fannie Mae or Freddie Mac (the GSEs), the funding comes from $29.9 billion currently set aside from the TARP for foreclosure mitigation.[23] For GSE mortgage modifications, $25 billion has been set aside from the Housing and Economic Relief Act of 2008.

Under HAMP's Principal Reduction Alternative (PRA) initiative, which became effective on October 1, 2010, servicers must conduct an additional evaluation of borrowers who meet the HAMP criteria and whose mortgages are significantly underwater, resulting in a loan-to-value (LTV) ratio, at current market prices, of more than 115 percent. If the mortgage meets these criteria, the servicer must evaluate it to determine, as with the original HAMP NPV test, whether the NPV of a principal reduction under the program is greater than the NPV under no modification. If so, the servicer has the option to offer a principal reduction under the PRA. These principal reductions are voluntary for servicers, unlike interest payment reductions which are a mandatory part of HAMP. A servicer who elects to offer a principal reduction first reduces the principal until the LTV is 115 percent or the DTI is no more than 31 percent, whichever happens first. Then the servicer follows the HAMP guidelines for completing the modification. The amount of principal reduced is treated initially only as forbearance. Each year for three years, however, a third of that amount is forgiven if the borrower remains current on the modified loan.[24]

The NPV test is key to HAMP's strategy. The program is not intended to prevent all foreclosures, but rather to encourage modification in those cases in which the value of a modification is greater than the value of a foreclosure. One might very reasonably ask why a government program involving servicer payments is necessary when servicers should already be modifying these loans out of self-interest. However, there are other factors at work that may

[22] The incentive payments for investors and borrowers are included when calculating the net present value of a loan modification under Treasury's NPV analysis. *See* Introduction of the Home Affordable Modification Program, *supra* note 19, at 22–25.

[23] The original funding amount allotted for HAMP was $50 billion. In May 2009, the $1.2 billion reduction in TARP due to the passage of the Helping Families Save Their Homes Act was officially allocated to HAMP. *See Helping Families Save Their Homes Act of 2009,* Pub. L. No. 111–22 § 402(f) (2009) (online at financialservices.house.gov/FinancialSvcsDemMedia/file/public%20laws/111–22.pdf). The $50 billion HAMP funding was later reduced to a ceiling of $30.6 billion by the Dodd-Frank Wall Street Reform and Consumer Protection Act. To date Treasury has expended less than $800 million on HAMP.

[24] Principal forbearance is not the same as principal reduction. In the first case, the borrower's unpaid principal balance remains unchanged but is restructured to reduce monthly payments. In the latter case, a certain amount of the principal is forgiven by the lender. Principal forbearance means that the loan's unpaid principal balance is not fully amortized over the remaining life of the loan. The balance, less the amount subject to forbearance, is then amortized or "spread out" over the remaining period of the loan, lowering the amount due each month. The amount by which the principal was reduced is then due as a balloon payment at the end of the loan, or when the property is sold. In the case of principal reduction, a certain amount of the principal is forgiven and is no longer owed by the borrower. *See* U.S. Department of the Treasury, *Making Home Affordable: Borrower Frequently Asked Questions* (Oct. 12, 2010) (online at makinghomeaffordable.gov/borrower-faqs.html).

affect a servicer's decision, particularly the many incentives in securitized mortgages for servicers to prefer foreclosure.[25]

During the period that the mortgage is in default, the servicer typically must continue to make payments to the investor out of its own pocket. It may also incur other expenses related to holding the troubled mortgage in its portfolio. If the mortgage goes into foreclosure, the servicer is reimbursed for these expenses before any of the money passes to the investors. Moreover, if a mortgage goes into foreclosure, the servicer holding the loan at that time typically handles the foreclosure, earning various fees for this service. Additionally, servicers earn income from float on the payments they collect—interest earned from the short-term investment of mortgage payments made between the time the servicer receives it from the borrower and the time it must be remitted to the investors.[26]

Therefore, it is in the servicer's interest to keep a mortgage for as long as it is producing an income stream and, once it goes into default, to ensure that the mortgage goes through foreclosure. HAMP's servicer incentive payments are designed, at least in part, to overcome these incentives that distort servicer decision making and lead to unnecessary foreclosures.

HAMP also offers incentive payments to borrowers over the course of the modification. These payments are designed to encourage borrowers to remain in the program and continue to pay their mortgages as well as to encourage participation in the first place. While it would seem unnecessary to pay borrowers to do what should already be in their interest, Treasury obviously felt otherwise, probably due to the poor track record of prior programs at obtaining and keeping borrower participation. Additionally, the added income from these borrower incentives is considered in the NPV model and may help some marginal HAMP applicants to achieve an NPV positive result, thus obtaining a HAMP modification.[27]

D. HAMP's Performance

After an influx of new trial modifications in 2009 and early 2010, the pace of entry into the program has fallen off considerably, according to the most recent data on the program's performance. Moreover, although some headway has been made in reducing the enormous number of borrowers in trial modifications awaiting conversion to permanent status, a sizeable backlog remains. Finally, while nearly 1.4 million trial modifications have been initiated since the start of the program, the number of borrowers who have dropped out of the program remains high. To date, HAMP has processed 519,648 permanent modifications.[28]

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[25] For a detailed explanation of these factors, *see* March 2009 Oversight Report, *supra* note 10. *See also* Office of the Special Inspector General for the Troubled Asset Relief Program, *Quarterly Report to Congress,* at 163–176 (Oct. 26, 2010) (online at sigtarp.gov/reports/congress/2010/October2010_Quarterly_Report_to_Congress.pdf) (hereinafter "SIGTARP Quarterly Report to Congress").

[26] Privately modified loans generally follow a similar pattern of reimbursement of the servicer for costs incurred, such as advancing coupon payments to investors while loans in the pool are in default. Individual PSAs can differ in their terms, however.

[27] U.S. Department of the Treasury, *Home Affordable Modification Program: Base Net Present Value (NPV) Model v4.0: Model Documentation,* at 33 (Oct. 1, 2010) (online at www.hmpadmin.com//portal/programs/docs/hamp_servicer/npvmodeldocumentationv4.pdf) (hereinafter "HAMP Base NPV Model v4.0: Model Documentation").

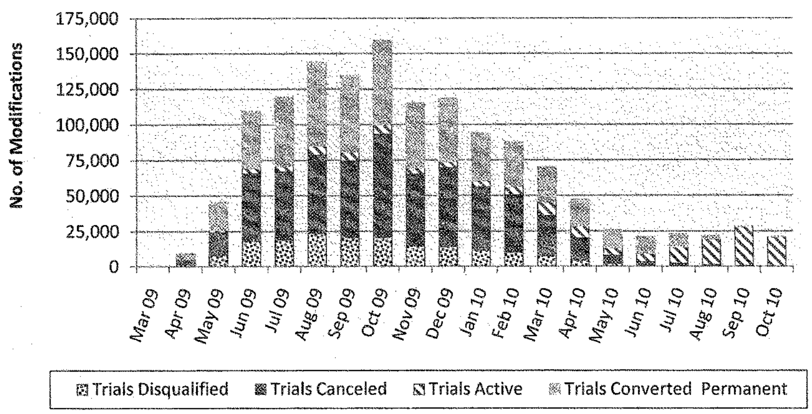
[28] Data provided by Treasury.

1. Trial Modifications

As of October 31, 2010, approximately 1.4 million trial modifications had been initiated under HAMP. Of these, 20,998 were initiated in October 2010. Between May and October 2010, each month posted, on average, approximately 23,000 new trial modifications, down from a high of almost 160,000 in October 2009.[29]

Figure 3 below shows the total number of trial modifications granted by month (e.g. October 2010: approximately 21,000 modifications) as well as the disposition of loans in each monthly cohort of HAMP modifications. Note that some trial modifications from the earliest months of the program remain active as trials.

FIGURE 3: DISPOSITION OF HAMP TRIAL MODIFICATIONS BY VINTAGE (MARCH 2009–SEPTEMBER 2010) [30]



Home mortgages have been traditionally divided into three categories of borrower credit quality, although these categories are not clearly defined. In the traditional usage, prime mortgages are loans to borrowers with good credit (typically above FICO 620) and adequate income. Alt-A mortgages are also loans to borrowers with prime (A) credit. However, Alt-As usually do not require income documentation (they are "stated income" loans), which is useful for small business owners and independent contractors who have variable income, but making the loans susceptible to fraud. Subprime mortgages refer to loans to borrowers with poor credit (below 620). Although in the past the Prime, Alt-A, and Subprime categories formerly did not indicate anything about mortgage type (e.g., fixed or floating rate, interest only or fully amortizing), the terms have come to be associated with specific loan types without regard to credit score in recent usage. For example, "subprime" is often used to refer to more exotic and risky mortgage types such as option ARMs.

Despite the fact that much of the analysis of the housing crisis has focused on subprime loans, the majority of loans past due as

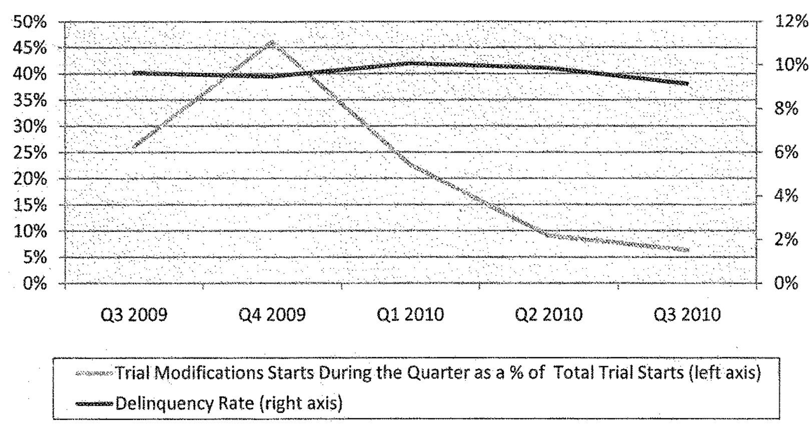
[29] Data provided by Treasury. These figures represent new trial modification first payments reported in October 2010.

[30] Data provided by Treasury.

of June 2010 were prime mortgages.[31] Prime mortgages received more than half of all HAMP modifications in the second quarter of 2010, while subprime and alt-A mortgages each received less than a quarter.[32]

Treasury has attributed the dramatic decrease in new trial modifications to several factors. According to officials, most of the decline is likely due to the institution of a verified income requirement in June 2010. Information provided by borrowers (including income), now must be documented before a trial modification can be initiated. "Stated income" (i.e. non-verified) was previously allowed for trial modifications. Additionally, Treasury has said that servicers increasingly shifted their attention from initiating new trial modifications to converting the existing backlog to permanent modifications. Finally, Treasury has indicated that the declining overall mortgage delinquency rate may play a role as well. There is reason to doubt that this latter factor has been a major cause of the decline, however. Figure 4 below shows new trial modifications and mortgage delinquency from the third quarter of 2009 to the third quarter of 2010. Clearly, the decline in delinquency has been relatively slight, while the decline in new trials has been much more severe.

FIGURE 4: TRIAL MODIFICATIONS VS. MORTGAGE DELINQUENCY (Q3 2009–Q3 2010) [33]



The change to verified income cannot completely explain the decrease either, since the number of new trial modifications began dropping off long before the up-front verified documentation standard was implemented in July 2010. It is possible that the program has already reached the majority of borrowers who can be helped. In the early months of the program, there was a large pool of borrowers awaiting help. Once many of these homeowners entered

[31] Office of the Comptroller of the Currency and Office of Thrift Supervision, *Mortgage Metrics Report, Second Quarter 2010,* at 22 (Sept. 2010) (online at www.ots.treas.gov/_files/490019.pdf) (hereinafter "OCC/OTS Mortgage Metrics Report, Second Quarter 2010").

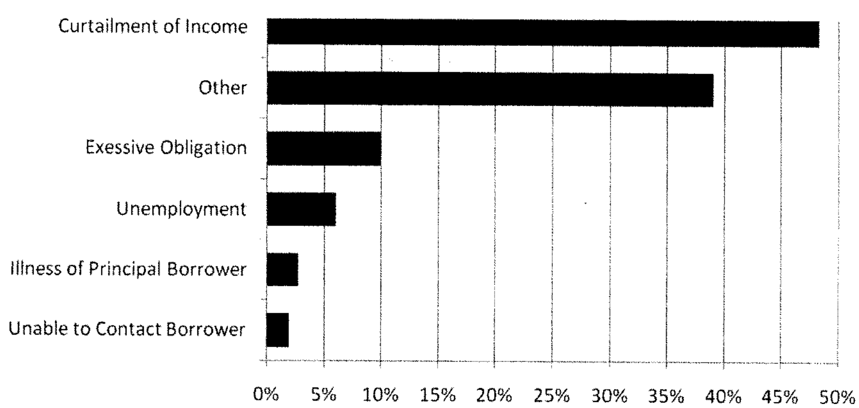
[32] *Id.* at 22.

[33] Mortgage Bankers Association, *National Delinquency Survey Q3 2010* (Nov. 18, 2010); Data provided by Treasury.

HAMP or other programs, there were simply fewer potential applicants who met HAMP criteria.[34]

Among borrowers starting trial modifications, "curtailment of income" remains the most common reason provided to explain the borrowers' economic hardship: around 47 percent of borrowers gave this reason for their hardship, reflecting in part the effect of underemployment. Unemployment accounts for only around 6 percent.[35] This is not surprising since the program originally was structured in such a way that made it almost impossible for an unemployed borrower to receive help under HAMP without another source of income. Furthermore, an applicant from a household in which one spouse has lost a job, while the other remains employed may select "curtailment of income" instead of "unemployment." In July 2010, Treasury rolled out an add-on program, the HAMP Unemployment Program, which offers forbearance for those who are unemployed and are receiving unemployment benefits. Additionally, several states, through the Hardest Hit Fund (HHF), have taken steps to address the effects of unemployment on homeowners' ability to keep their homes. For further discussion of these programs, see Section F. Figure 5 below details the top economic hardship reasons for trial modification starts.

FIGURE 5: ECONOMIC HARDSHIP REASONS FOR TRIAL MODIFICATION STARTS [36]



2. Conversion to Permanent Modification

In its previous reports, the Panel expressed concern regarding the rate at which trial modifications were converting to permanent modifications. As noted in the October 2009 report, only 1.26 percent of modifications had converted to permanent modifications, or approximately 2,000 borrowers. The April 2010 report found that the conversion rate had improved to 23.1 percent, or around 4,000 borrowers, although only 9.7 percent converted within the standard

[34] OCC/OTS Mortgage Metrics Report, Second Quarter 2010, *supra* note 31, at 22. *See also* Fitch Ratings, *U.S. RMBS: Still Under a Shadow,* at 5 (Nov. 1, 2010) (noting that "the number of remaining borrowers eligible for a loan modification appears to be declining, as new loan modification activity has declined from its peak in 2009.").

[35] Data provided by Treasury.

[36] Data provided by Treasury.

three months. Through September 2010, 38.4 percent of HAMP conversions happened within three months.[37] While, as noted in the Panel's prior reports, the earlier conversion rates were based on a fairly small loan pool, HAMP is demonstrating improvement in conversion of modifications from trial to permanent. As mentioned above, however, the number of new trial modifications has declined substantially in recent months.

In this area, some servicers have performed markedly better than others. Among the top servicers, for example, Wachovia Mortgage and HomeEq Servicing have conversion rates of 89 percent and 95 percent respectively. In contrast, Bank of America's rate is closer to 30 percent.[38] Conversations with Treasury officials indicate that much of the difference in conversion rates between servicers is due to the recent switch from stated income trials to verified income, and because stated income was used primarily by larger servicers, such as Bank of America. As a result, these servicers still have large pools of difficult to convert, stated income modifications.

During the early days of HAMP, Treasury focused on providing payment relief to as many borrowers as possible. Servicers were able to grant trial modifications to borrowers with no documentation required. However, the documentation required to convert the trial to a permanent modification proved to be a challenge as demonstrated by the earlier anemic conversion rate. Accordingly, mortgage servicers utilizing stated income began to develop a backlog of trial modifications awaiting a decision. In its last report on foreclosure mitigation, the Panel noted steps that Treasury had taken to ensure that servicers would clear these cases in a timely manner. As of October 31, 2010, the backlog of modifications that had been in a trial period for six months or longer had fallen to 69,400. Three servicers—Bank of America, JPMorgan Chase, and CitiMortgage—comprise more than two-thirds of the backlog, and not surprisingly, all three utilized stated income trials prior to the new standard. Bank of America alone services approximately half of the backlog of aged trials.[39]

While it is good that the servicers appear to be clearing out the backlog of trial modifications eligible for conversion, much of the increase in the conversion rate is linked to the decline in number of people entering new trial modifications, and therefore a decline in the total number of borrowers in trial modifications, and not from an actual increase in the number of borrowers moving to permanent modifications. That is, while the conversion rate is improving, it is primarily a result of the smaller pool of borrowers eligible for conversion. Treasury expects the HAMP conversion rate to increase significantly going forward as trial modifications are now started only after the borrower has provided all documentation, previously a major stumbling block, and servicers shift their focus more to processing the existing backlog of trial modifications.[40] As

[37] Data provided by Treasury.

[38] U.S. Department of the Treasury, *Making Home Affordable Program: Servicer Performance Report Through October 2010,* at 4 (Nov. 19, 2010) (online at www.financialstability.gov/docs/Oct%202010%20MHA%20Public%20Final.pdf) (hereinafter "MHA Servicer Performance Report").

[39] *Id.* at 4.

[40] Treasury conversations with Panel staff (Nov. 16, 2010).

the Panel has noted before, different pieces of the HAMP modification process, such as initiating trial modifications and converting trials to permanent modifications are linked, and a narrow focus by servicers on one aspect to the exclusion of others may lead to tradeoffs that diminish overall modification success.[41] Currently, as Treasury has acknowledged, a focus by servicers on converting the backlog has caused the number of new trials to decline.[42]

3. Permanent Modifications

Through October 2010, 519,648 homeowners have been able to obtain a conversion to a permanent modification through HAMP. Of these, 483,342 are currently active modifications. The remaining 36,306 represent 491 loans that have been paid off and 35,815 that have been cancelled due to redefault.[43]

There were a total of 23,750 new permanent modifications in October 2010. The number of new permanent modifications peaked in April 2010 at 68,291 and has declined steadily since then. The number of new permanent conversions is now averaging less than half the number of new monthly permanent modifications at the peak.[44] This trend is closely tied to the significant decrease in trial modifications coming into the pipeline rather than a failure to convert modifications once they enter the pipeline. This development raises the question of whether HAMP has already surpassed its maximum effectiveness and will continue the trend of diminishing results.

All HAMP permanent modifications have used interest rate reductions in order to reach the program's affordability target. In addition, more than 57 percent of the modifications include a term extension, and 30 percent feature principal forbearance.[45] Principal reduction remains relatively rare, with only around 3 percent of the permanent modifications offering a principal write-down as of early October 2010.[46] Prior to modification, the median interest rate of HAMP participants is 6.63 percent. This drops to 2 percent after the permanent modification. Similarly, monthly payments decline from a median value of $1,434 before modification to $838 after modification, a difference of $596.[47]

Figure 6 below shows the number of all active permanent modifications and redefaults by month.

[41] April 2010 Oversight Report, *supra* note 1, at 69–70.
[42] Treasury conversations with Panel staff (Nov. 16, 2010).
[43] Data provided by Treasury; MHA Servicer Performance Report, *supra* note 38, at 4.
[44] Data provided by Treasury; MHA Servicer Performance Report, *supra* note 38, at 2.
[45] MHA Servicer Performance Report, *supra* note 38, at 3.
[46] Data provided by Treasury; MHA Servicer Performance Report, *supra* note 38, at 3.
[47] Data provided by Treasury.

FIGURE 6: MONTHLY HAMP PERMANENT MODIFICATIONS AND REDEFAULTS (FEBRUARY 2010–SEPTEMBER 2010) [48]

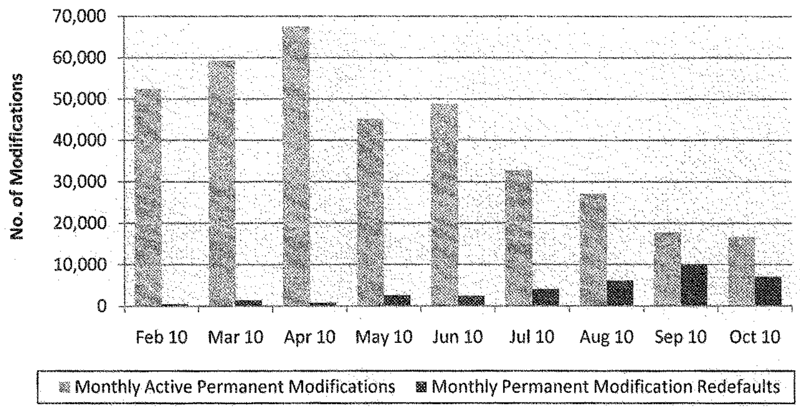
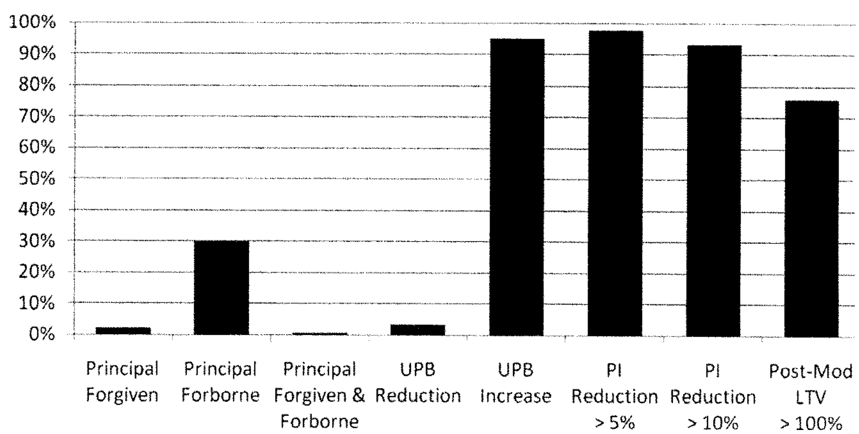


Figure 7 below summarizes the characteristics of all permanent modifications granted under HAMP. Forgiveness and forebearance are explained in footnote 24 above. UPB refers to the unpaid principal balance. PI refers to debt service payments—principal and interest.

FIGURE 7: SUMMARY DATA ABOUT PERMANENT MODIFICATIONS [49]



a. Borrower Debt

Permanent HAMP modifications offer much more affordable mortgage payments over unmodified mortgages, but they nonethe-

[48] "Monthly Active Permanent Modifications" and "Monthly Permanent Modification Redefaults" are derived from cumulative "Active Permanent Modifications" and "Permanent Modifications Canceled" (excluding loans paid off) levels from March 2010 to October 2010 recorded in the Making Home Affordable Program's monthly Servicer Performance Reports. For these monthly reports, *see* U.S. Department of the Treasury, *Reports and Documents* (online at financialstability.gov/latest/reportsanddocs.html) (accessed Dec. 10, 2010) (hereinafter "Treasury Reports and Documents").

[49] Data provided by Treasury.

less leave borrowers with very high overall debt levels. Prior to modification, the median borrower receiving a HAMP modification was paying 45 percent of his or her pre-tax income towards the mortgage (front-end DTI), and nearly 80 percent of pre-tax income toward all debts (back-end DTI). After receiving a HAMP permanent modification, the median borrower's front-end DTI had been reduced to 31 percent, and their back-end DTI fell to 63 percent.[50]

However, even these post-modification DTIs are higher than those allowed by most mortgage underwriting standards. To qualify for a new FHA loan, for example, a borrower typically needs to show a back-end DTI ratio of no more than 41 percent of gross income, while a borrower receiving a mortgage through Freddie Mac must not have a back-end DTI ratio of more than 45 percent.[51] The situation worsens once state and federal taxes are subtracted from income. Pre-modification borrowers appear to be spending nearly all of their after-tax income on debt service, with other expenses presumably paid for with credit. Even at the improved 63 percent back-end DTI of borrowers following a HAMP modification, debt service payments will still consume approximately 80 percent of after-tax income, which is of course the income borrowers actually have to spend.[52] Furthermore, the Panel is particularly concerned that the post-modification back-end DTI ratio appears to be rising—up 4 percent since the Panel's April 2010 foreclosure report, where post-modification back-end median DTI was 59 percent.[53] These high and rising DTIs do not bode well for the long term success of the program.

Figure 8 below shows the distribution of (pre-tax) back-end DTIs for borrowers receiving permanent modifications from HAMP. Since these borrowers have already been in trials for at least three months, these DTIs are post-modification. The bulk of borrowers receiving permanent modifications are clearly either in the more moderate 31 percent–40 percent DTI category or the very high over 80 percent DTI. In fact, nearly one-third of post-modification borrowers have back-end DTI in excess of 80 percent. This is troubling, as it indicates that the overall 63 percent post-modification

[50] Since the purpose of HAMP is to lower high-DTI borrowers to 31 percent or below, and since servicers have no incentive to lower payments below this, the average borrower DTI is the same as the 31 percent limit. Data provided by Treasury.

[51] Federal Housing Administration, *FHA Requirements: Debt Ratios* (online at www.fha.com/fha_requirements_debt.cfm) (accessed Dec. 10, 2010); Federal Home Loan Mortgage Corporation, *Underwriting Reminders for Loan Prospector Caution Risk Class Mortgages,* at 4 (Oct. 2010) (online at www.freddiemac.com/learn/pdfs/uw/caution_remind.pdf).

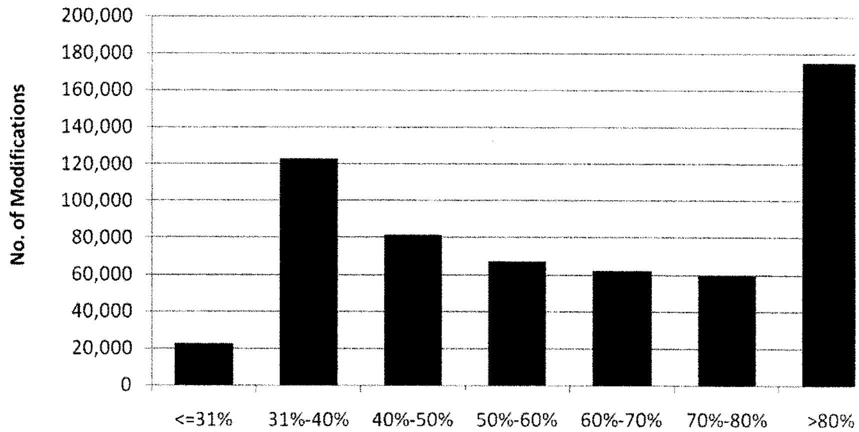
[52] A rough calculation of after-tax income can give a more realistic picture of the financial situation of HAMP participants. The median HAMP participant earning $32,000 a year, filing as the head of household, and taking the standard deduction, would pay approximately $2,954 in federal income taxes, $2,448 in Social Security and Medicare taxes and, in this example, $1,000 in state taxes, although this latter figure will vary greatly depending on the state. The borrower in this case would then have an after-tax income of $25,598.

The median HAMP participant's pre-tax, pre-mod, back-end DTI of 80 percent equates to $25,555 in total debt service owed annually, divided into $14,422 in mortgage payments and $11,133 of service on other debts. If accurate, total debt service is nearly as much as the after-tax income above (a 100 percent after-tax back-end DTI). After a HAMP permanent modification, the borrower would still be paying $20,272 annually on all debts, including $9,930 in mortgage payments (a savings of $4,493 annually). Interestingly, service on other debts apparently falls as well after modification, down $790 to $10,342. After taxes and debt service, the median HAMP participant has just $5,326 per year, or $444 per month, for all other expenses, including food, clothing, health care, education, etc.

[53] *See* April 2010 Oversight Report, *supra* note 1, at 43; Data provided by Treasury. Sustainability of HAMP modifications is discussed further in Section G.2.g, *infra.*

DTI statistic contains a very large sub-segment of heavily indebted borrowers.

FIGURE 8: NUMBER OF PERMANENT MODIFICATIONS BY BACK-END DTI (AS OF SEPTEMBER 30, 2010) [54]



The question of what DTI level is sustainable remains open, and complicated by HAMP's focus on front-end DTIs. Other debts such as second liens, credit card debt, and car debt are not factored into the front-end DTI used to determine HAMP eligibility, despite the fact that most HAMP applicants have substantial amounts of such debt. It would appear that back-end DTI may be the more important metric for gauging a homeowner's overall financial picture and their ultimate ability to remain current on a mortgage. Indeed some borrowers, although heavily indebted overall, do not meet HAMP's front-end DTI eligibility threshold. Faith Schwartz, senior adviser for the HOPE NOW Alliance, testified that HAMP's 31 percent minimum front-end DTI for eligibility was considered "aggressive" when HAMP was first rolled out, but that even this level is too high for many homeowners who wind up in foreclosure because their front-end DTI is too low to make them HAMP-eligible.[55] Any additional assistance necessary to bring down the back-end DTI ratio could theoretically come from a number of sources, including federal, state, or local agencies, or from private sources.[56] Obviously, however, in any effort of this sort to reduce back-end DTIs, policymakers will have to weigh the costs and benefits of any additional assistance, as well as how the burden of these costs would be distributed between servicers, investors, and taxpayers.[57]

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[54] Data provided by Treasury.

[55] Congressional Oversight Panel, Written Testimony of Faith Schwartz, senior advisor, HOPE NOW Alliance, *COP Hearing on TARP Foreclosure Mitigation Programs,* at 7 (Oct. 27, 2010) (online at cop.senate.gov/documents/testimony-102710-schwartz.pdf).

[56] For instance, Treasury's 2MP program is designed to decrease second lien payments which would reduce back-end DTI. See Section F, *infra.*

[57] Continuing with the median HAMP participant example discussed in footnote 52, *supra,* an additional subsidy sufficient to put the borrower at a 50 percent pre-tax back-end DTI would raise the borrower's after-tax, after debt service, disposable income by $4,272 ($356 per month) from $5,326 ($444 per month) to $9,598 ($800 per month). Although an extra $356 a month could greatly help many distressed borrowers living at the edge of their means, it is difficult to determine how much such a policy would actually reduce foreclosures in the long run. The

b. Negative Equity

Permanent modifications have not, however, made much of an impact on the depth of borrowers' negative equity. Of all active permanent modifications, nearly 95 percent have an unpaid principal balance that is *higher* than it was before modification.[58] Negative equity remains high, with more than 76 percent of mortgages in permanent modification still carrying a negative LTV ratio. In fact, LTV ratios have increased, on average, after modifications. The median LTV ratio is approximately 120 percent before a modification and about 125 percent after the modification.[59] Although HAMP may provide a more affordable monthly payment for homeowners, it does not address the problems caused by mortgages that are deeply underwater. Negative equity can restrict the ability of homeowners to move, whether for family reasons or to pursue greater job opportunities, since home sale proceeds will not be sufficient to repay their loan. It also provides an incentive for borrowers who can afford to pay their mortgages to stop paying intentionally and walk away from their homes if they believe that they will remain deeply underwater for a long time, a decision known as a "strategic default."

The value of futures contracts based on the Case-Shiller Housing Price Index can be a useful indicator of market expectations for future home prices. A chart showing the current prices for these contracts for the 10 largest Metropolitan Statistical Areas (MSAs) and the composite of these MSAs is shown as Figure 45 in the Metrics section. The futures market expects that over the next five years housing prices will remain relatively flat in all MSAs as well as the 10–MSA composite. Although the predictive accuracy of these prices is limited, especially for the more illiquid contracts, and as they go further out in time, the prices seem to indicate that few of the educated observers of the housing market who trade these contracts expect a rapid rise in home prices. It would therefore appear that borrowers at 120 percent LTV or higher, such as the average HAMP participant, have a slim chance of returning to positive equity in the foreseeable future.[60]

4. Borrowers Dropped from the Program

As servicers began to work through the significant backlog in the program, many borrowers in trial modifications were denied permanent modifications and dropped from the program. In total, servicers have cancelled 541,907 trial modifications through October 2010.[61] According to Treasury, the most common reasons for trial modification cancellations are insufficient documentation, trial

cost of such a program is also difficult to estimate, as it would depend on how the subsidy was structured (direct payment of debt service vs. principal reduction) and which debts are affected (the low-interest first mortgage or higher interest debts such as credit cards).

[58] The increase does not represent a true increase in the obligations of the borrower because it represents mostly capitalization of arrearages and escrow requirements. Data provided by Treasury.

[59] Data provided by Treasury. Much of this increase in LTV is due to adding missed mortgage payments to the principal balance.

[60] Further discussion of Case-Shiller futures can be found below in Section Three: TARP Updates Since Last Report (see Section D.3 on housing prices).

[61] In addition to these canceled modifications that failed to convert from trial to permanent status, an additional 177,580 trial modifications were disqualified through October 2010. Data provided by Treasury.

plan payment default, and ineligibility because the first mortgage payment is already at or below the program DTI standard of 31 percent. Specifically, among the HAMP servicers, just under 30 percent of trial modifications have been cancelled because of incomplete requests. Surprisingly, the percentage did not change significantly between the period preceding June 1, 2010—the date the verified income requirement was implemented—and the period following that date. Trial plan defaults, however, have crept up slightly. Prior to June 1, 2010, approximately 21 percent of cancellations were due to a default during the trial period, and 24 percent for the period following June 1. Among those with the first payment due on or before June 1, 2010, nearly 8 percent did not go forward because of a negative NPV test result, meaning that foreclosure was found to be more cost effective than modification. Among those with a first payment due after June 1, 2010, only 4 percent were cancelled for this reason. Figure 9 below shows reasons for permanent conversion denials for the period prior to June 1, 2010, and post June 1, 2010, respectively.[62]

[62] Data provided by Treasury.

FIGURE 9: CONVERSION DENIAL REASONS[63]

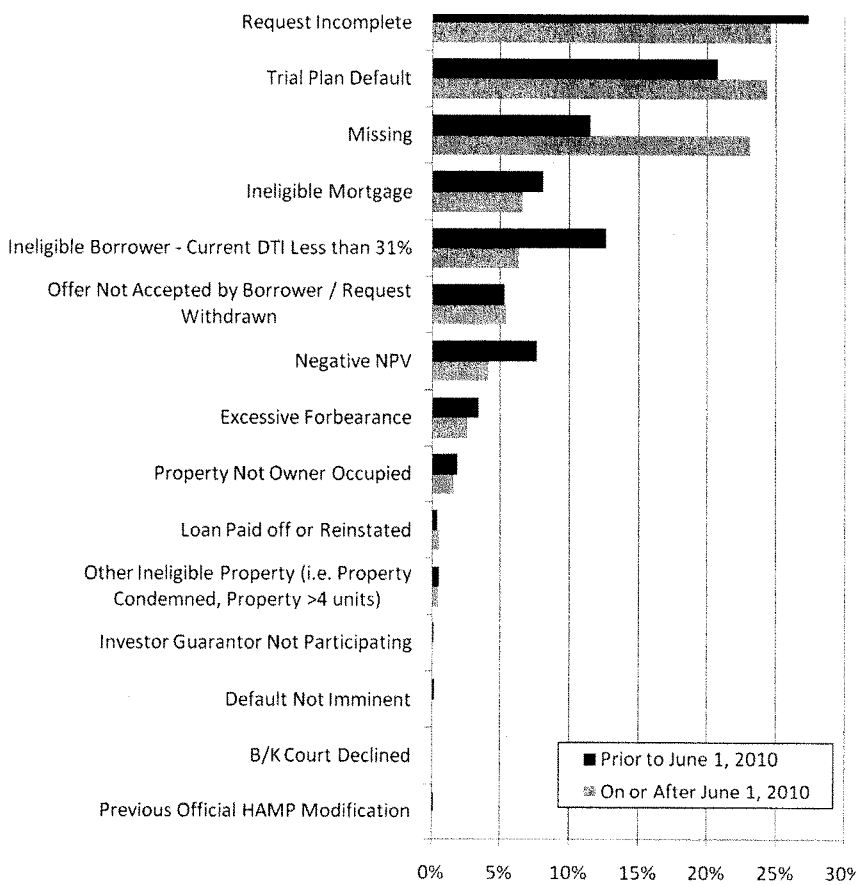
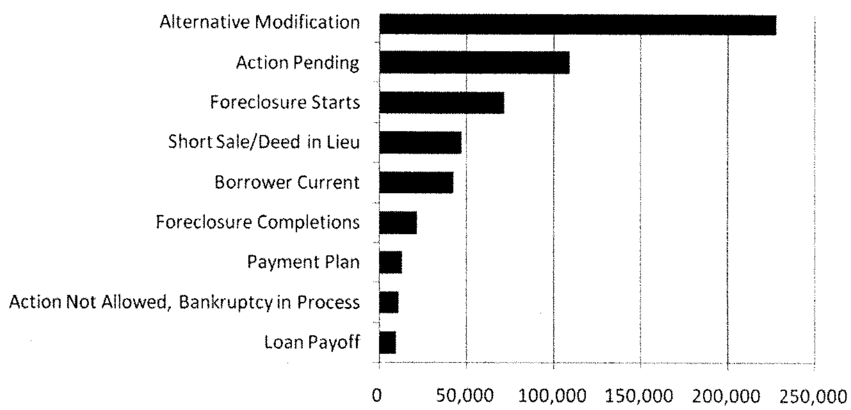


Figure 10 below shows the status of cancelled trial modifications for the eight largest servicers. Only 3.9 percent experienced a foreclosure sale, while 13 percent are in the foreclosure process. Another 41.3 percent of the borrowers received an alternative modification, although the alternative modification terms are not necessarily comparable to a HAMP modification.[64] See Section E for a discussion of alternative modifications.

[63] Data provided by Treasury.
[64] MHA Servicer Performance Report, *supra* note 38, at 5. These eight are the servicers with the largest allocated HAMP cap amounts.

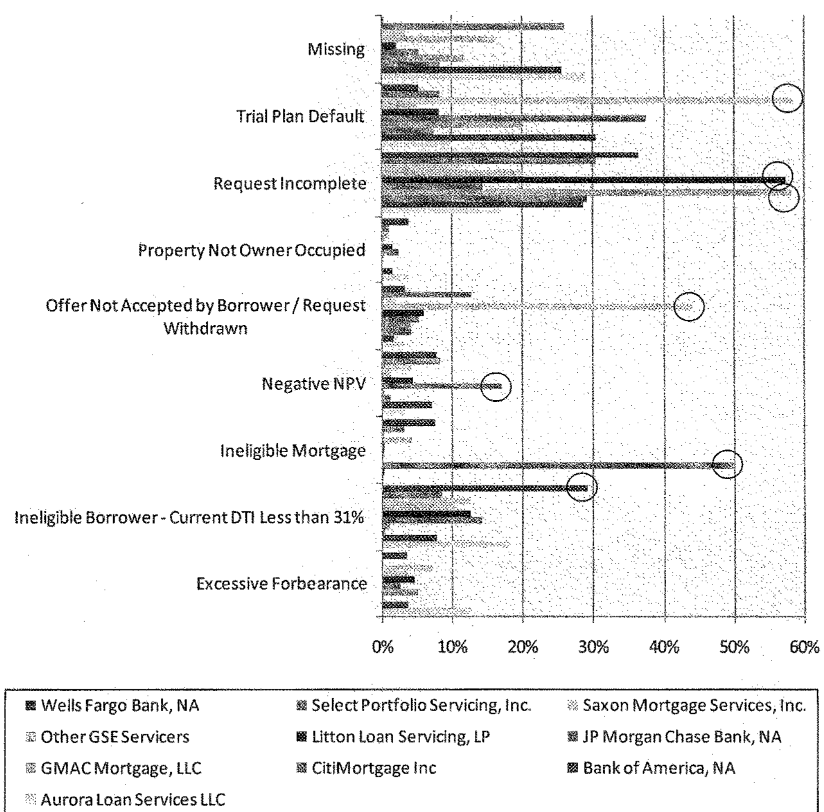
FIGURE 10: STATUS OF CANCELLED TRIAL MODIFICATIONS (AS OF SEPTEMBER 2010)[65]



There is a tremendous variation in the reasons given by different servicers for trial plan failures. Some notable outliers are identified with circles in Figure 11 below. For example, a significantly greater percentage of Wells Fargo's trial modifications failed because of low front-end DTI (<31 percent) than was the case for other servicers. Of the trial modifications terminated by Citibank, nearly half were due to "ineligible mortgages." JPMorgan Chase's borrowers had NPV negative modifications at a much higher rate than other servicers. This might be a function of other servicers ruling out more modifications before even getting to NPV, or it could be a function of the particular inputs JPMorgan Chase uses for its NPV test.[66] Of the trial modifications terminated by GMAC and Litton Loan Servicing, over half were caused by a failure to receive complete paperwork. Nearly 60 percent of failed trials at Saxon Mortgage Services, Inc., were due to trial plan default. At present, the Panel is unsure why these wide discrepancies exist. It might be explained by heterogeneity in the loan pools or by servicer choices in coding denials, but it could also be explained by particular servicer behavior or decisions. Treasury should be closely monitoring this issue and provide an explanation for these wide discrepancies.

[65] MHA Servicer Performance Report, *supra* note 38, at 5.
[66] Treasury permits larger servicers such as JPMorgan Chase to adjust certain inputs to the NPV model to suit their particular circumstances. This is discussed further in Section G.2.f, *infra*.

FIGURE 11: REASONS FOR TRIAL PLAN FAILURE FOR LARGE HAMP SERVICERS (>20,000 TRIAL MODIFICATIONS), MARCH 2009–JUNE 2010 [67]



5. Redefault

There are also a number of borrowers who are unable to remain current even after receiving a permanent modification through HAMP and ultimately redefault on their mortgages. As of October 2010, 35,815 borrowers with permanent modifications had redefaulted. Although the trend has been toward lower rates of redefault, October posted an increase. Actual redefaults to date have been lower than the redefault rate assumed in the NPV model. However, the NPV model considers the likelihood of redefault over the entire 5-year term of a modification, while the current redefault rate only looks at the experience of the program since its inception. Many of these loans are only a few months into their modifications, so it is too soon to tell if the current redefault rates will continue.

It is important to note that Treasury does not have complete data on HAMP permanent modification performance. Treasury lacks complete or valid performance information for 63,169 permanent HAMP modifications or 13 percent of all permanent modifica-

[67] Data provided by Treasury.

tions. The inclusion of full information for these permanent modifications could potentially raise or lower redefault rates. The Panel urges Treasury to ensure that going forward it has complete, valid performance data on all HAMP permanent modifications. For further discussion of HAMP redefaults, see Section D.5.

E. Performance of Non-HAMP Modifications

Taken as a whole, 54 percent of the nearly 1.4 million temporary modifications that have been initiated under HAMP have ultimately failed.[68] What became of the borrowers who are no longer in the program? According to Treasury, the majority of the borrowers go on to receive modifications through the servicers' own proprietary modification programs. Under program guidelines, participating servicers must consider borrowers who were unable to receive a HAMP modification for a proprietary modification, but there are no specific eligibility or modifications standards, only the requirement that borrowers not receiving a HAMP modification must be considered for a proprietary modification according to the servicers' own standards. Thus, whereas HAMP modifications are standardized and the terms are publicly transparent, non-HAMP modifications are not, creating concern about their sustainability.

In addition, proprietary modifications serve borrowers who are not eligible for HAMP. Of the 5.1 million first lien mortgages that were more than 60 days delinquent as of October 31, 2010, Treasury estimates that only around 1.5 million are HAMP-eligible. The most common reasons for ineligibility, are: (1) having a servicer that is not participating in HAMP; (2) having an ineligible loan, such as a loan backed by FHA or Department of Veterans Affairs (VA); (3) having a front-end DTI ratio of less than 31 percent, and (4) having a loan for a home reported as non-owner occupied at the time of origination.[69]

Banks report that they are increasing their number of non-HAMP modifications to help those who are not eligible or do not qualify for a HAMP modification. Statistics gathered by HOPE NOW, an alliance of mortgage servicers, show that the number of loan modifications implemented through private channels is outpacing the number of HAMP modifications.[70] Year-to-date, there have been more than twice as many modifications performed outside of Treasury programs as HAMP modifications,[71] and in October 2010 alone, 81 percent of all completed modifications were done outside of HAMP.[72] In addition to various types of modifications, HAMP and proprietary, some homeowners have sought assistance through other payment plans. More than 18 percent of the home

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[68] Data provided by Treasury. These failed modifications include disqualified and cancelled trials as well as disqualified permanent modifications.

[69] Data provided by Treasury. Having a non-participating servicer excludes 600,000 borrowers, while the other most common reasons for ineligibility affect approximately 700,000 borrowers each. HAMP applicants are evaluated via a waterfall method. Therefore, a borrower who is disqualified because his or her servicer is not participating may also be ineligible for other reasons, but is only counted among those disqualified at the top of waterfall.

[70] HOPE NOW Alliance, *Industry Extrapolations and Metrics (October 2010),* at 3–4 (Dec. 6, 2010) (online at www.hopenow.com/industry-data/HOPE%20NOW%20Data%20Report%20(October)%2012-05-2010%20v2.pdf) (hereinafter "HOPE NOW Industry Extrapolations and Metrics").

[71] HOPE NOW Industry Extrapolations and Metrics, *supra* note 70, at 3.

[72] Year-to-date, nearly 87 percent of all completed modifications have been performed outside of HAMP. HOPE NOW Industry Extrapolations and Metrics, *supra* note 70, at 4.

retention actions initiated in the second quarter of 2010 were payment plans.[73]

While the number of proprietary modifications currently outpaces HAMP modifications, HAMP still produces, on average, a modification offering more relief to the borrower and having a lower likelihood of redefault. For those modifications made during the second quarter of 2010, non-HAMP modifications reduced monthly payments, on average, half as much as HAMP payment reductions, and of the nearly 10 percent of loan modifications that result in unchanged or increased monthly payments, nearly all are non-HAMP modifications.[74] The lower average payment reductions for non-HAMP modifications seems to impact directly their potential to redefault, as non-HAMP modifications have a redefault rate six months after modification of 22.4 percent, compared to only 10.8 percent for HAMP modifications.[75] While the redefault rate six months after modification is a more preliminary data point that does not encompass the full scope of likely redefaults, it is the longest time span currently available for rates that break out HAMP and non-HAMP modifications. HAMP modifications have a redefault rate of 21 percent twelve months after modification for loans 90 or more days past due,[76] while the same rates for all modifications (HAMP and non-HAMP combined) are 48.6 percent and 36.6 percent for loans modified in the first quarter and second quarter of 2009, respectively.[77]

Beyond these data points, HAMP continues to provide a roadmap (i.e., the "waterfall") for servicers to use when considering various tools to use in mortgage modifications. As Ms. Schwartz noted at the Panel's October foreclosure mitigation hearing, "The first most important contribution of HAMP is that all servicers who signed up for HAMP must review all homeowners for eligibility. The HAMP process offers homeowners a first line of defense to avoid foreclosure. Second is the importance of the HAMP waterfall. Investors, servicers, lenders, and nonprofits, and homeowners have a uniform map of activity that is necessary to ensure delinquent homeowners who seek help are being considered for a solution prior to foreclosure."[78] HAMP has created a uniform approach to mortgage modifications: participating servicers must evaluate borrowers for and (assuming criteria are met) provide them with a HAMP modification first, ensuring a set affordability standard, and only consider a proprietary modification, the terms of which are determined completely by the servicer, after it has been determined that HAMP is not an option.

Unfortunately, while some limited data do exist on non-HAMP programs, the data collection efforts have not been sufficiently robust. The lack of comprehensive, reliable data makes it difficult to

[73] OCC/OTS Mortgage Metrics Report, Second Quarter 2010, *supra* note 31, at 21.
[74] OCC/OTS Mortgage Metrics Report, Second Quarter 2010, *supra* note 31, at 30–32.
[75] The redefault rate is for fourth quarter 2009 loan modifications that have aged six months and are 60 or more days delinquent. OCC/OTS Mortgage Metrics Report, Second Quarter 2010, *supra* note 31, at 35.
[76] Data provided by Treasury.
[77] OCC/OTS Mortgage Metrics Report, Second Quarter 2010, *supra* note 31, at 37.
[78] Congressional Oversight Panel, Testimony of Faith Schwartz, senior advisor, HOPE NOW Alliance, *Transcript: COP Hearing on TARP Foreclosure Mitigation Programs* (Oct. 27, 2010) (publication forthcoming) (online at cop.senate.gov/hearings/library/hearing-102710-foreclosure.cfm) (hereinafter "Testimony of Faith Schwartz").

make an apples-to-apples comparison of HAMP and non-HAMP programs. While the average monthly payment reduction and redefault rates are available, the specifics of the structure of the modifications are unknown. Since its initial report on foreclosure in March 2009, the Panel has stressed the importance of collecting data on loan performance, loss mitigation efforts, and foreclosure. While data collection has improved, including the data collected through HAMP, non-HAMP modifications do not have the same level of transparency. The Panel questions why a system of record was not established to track non-HAMP modifications at the outset and why one still does not exist. The HOPE NOW Alliance has increased its collection of data on this type of modification but, as of publication, the data are not available. Mortgage servicers representing the bulk of the mortgage servicing industry are owned or controlled by federally regulated entities.[79] Regulators of those entities, typically the Federal Reserve System and the Office of the Comptroller of the Currency, could and should be collecting and reporting this information from the mortgage servicers under their jurisdiction. Given the need for specific and robust data on non-HAMP modifications to analyze properly their effectiveness and viability and further inform the continued analysis of HAMP, the Panel reiterates its call for Treasury to increase or aid in data collection.

F. Treasury's Other Foreclosure Mitigation Programs

Establishing HAMP was part of Treasury's initial response to the housing crisis, and it has remained Treasury's largest foreclosure mitigation program, both in terms of funding and borrowers. However, as the crisis evolved and HAMP's reach began to prove too limited, Treasury announced and rolled out the following additional programs: Home Price Decline Protection (HPDP), PRA, Home Affordable Unemployment Program (UP), Home Affordable Foreclosure Alternatives (HAFA), Second Lien Modification Program (2MP), HHF, FHA Refinance Program, and various agency-specific programs to encourage modifications. Although many of these programs have been in existence for many months to over a year, at this time there are either no data available or such a limited data pool that meaningful analysis of these programs is not possible. Therefore, this report will confine its primary analysis to HAMP. However, it is important to understand that HAMP currently operates in conjunction with these other programs.

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[79] For instance the top four servicers, Bank of America, Wells Fargo, JPMorgan and Citigroup, who service over 50 percent of all mortgages (by outstanding principal balance), are all bank holding companies. Congressional Oversight Panel, *November Oversight Report: Examining the Consequences of Mortgage Irregularities for Financial Stability and Foreclosure Mitigation*, at 59 (Nov. 16, 2010) (online at cop.senate.gov/documents/cop-111610-report.pdf) (hereinafter "November 2010 Oversight Report"); Federal Financial Institutions Examination Council, *Top 50 BHCs* (Sept. 30, 2010) (online at www.ffiec.gov/nicpubweb/nicweb/top50form.aspx); House Financial Services, Subcommittee on Housing and Community Opportunity, Written Testimony of John Walsh, acting comptroller of the currency, Office of the Comptroller of the Currency, *Robo-Signing, Chain of Title, Loss Mitigation, and Other Issues in Mortgage Servicing,* at 2 (Nov. 18, 2010) (online at financialservices.house.gov/Media/file/hearings/111/Walsh111810.pdf) ("The OCC supervises all national banks and their operating subsidiaries, including their mortgage servicing operations. The servicing portfolios of the eight largest national bank mortgage servicers account for approximately 63 percent of all mortgages outstanding in the United States—nearly $33.3 million loans totaling almost $5.8 trillion in principal balances as of June 30, 2010.").

Home Price Decline Protection (HPDP)

The HPDP, announced on July 31, 2009, and effective the following day,[80] was designed to address the issue of investor objections to modifications due to fear of a potential future decline in home values. For an investor who anticipates a future decline in home values, it is preferable to foreclose today rather than consent to a modification that might fail and end in a future foreclosure. Under this program, investors receive incentive payments that accrue over a 24-month period to mitigate potential losses and encourage their consent to proposed modifications.

Principal Reduction Alternative (PRA)

Treasury's PRA program was announced on June 3, 2010, and went into effect on October 1, 2010. This program was a response to the large number of underwater mortgages, as principal reductions can be a significant means of preventing foreclosures and redefaults. It operates much like HAMP, except that instead of postponing payments on a portion of the mortgage, the PRA program forgives that portion altogether.[81] Servicers are required to evaluate a loan that is HAMP eligible and has a mark-to-market loan-to-value ratio greater than 115 percent with both the standard HAMP waterfall and an alternative waterfall that includes principal reduction as the required second step, and then must use the NPV model to evaluate the modifications proposed by both waterfalls. If the NPV result generated by the standard waterfall is positive, servicers must modify the loan; if the NPV result generated by the alternative waterfall is positive, servicers are encouraged but not required to perform a HAMP modification including principal forgiveness; if the NPV result for both waterfalls is negative, loan modification is not required.[82] Thus, the final decision on whether to grant a principal reduction is ultimately up to the servicer. Investors receive standard incentive payments as well as a percentage of each dollar forgiven.

Home Affordable Unemployment Program (UP)

Treasury's unemployment program, announced on March 26, 2010,[83] and effective July 1, 2010,[84] was designed to assist unemployed homeowners by granting a temporary forbearance of a portion of their monthly mortgage payment for, at a minimum, the lesser of three months or until employment is regained.[85] During the forbearance period, payments are reduced to no more than 31 percent of the borrower's gross monthly income, including unem-

[80] U.S. Department of the Treasury, *Treasury Announces Home Price Decline Protection Incentives* (July 31, 2009) (online at www.financialstability.gov/latest/tg__07312009.html).

[81] U.S. Department of the Treasury, *Modification of Loans with Principal Reduction Alternative, Supplemental Directive 10–05* (June 3, 2010) (online at www.hmpadmin.com/portal/programs/docs/hamp_servicer/sd1005.pdf).

[82] *Id.* The alternative waterfall inserts principal reduction in between the standard waterfall's step one (capitalization) and step two (interest rate reduction).

[83] U.S. Department of the Treasury, *Housing Program Enhancements Offer Additional Options for Struggling Homeowners* (Mar. 26, 2010) (online at www.financialstability.gov/latest/pr_03262010.html).

[84] U.S. Department of the Treasury, *Home Affordable Unemployment Program,* Supplemental Directive 10–04 (May 11, 2010) (online at www.hmpadmin.com//portal/programs/docs/hamp_servicer/sd1004.pdf) (hereinafter "Supplemental Directive 10–04").

[85] Servicers have the discretion to extend the minimum forbearance period in increments in accordance with investor and regulatory guidelines.

ployment benefits.[86] In order to be eligible, a borrower must hold a mortgage that: is secured by the borrower's principal residence, is first-lien and originated on or before January 1, 2009, has an unpaid principal amount equal to or less than $729,750, is delinquent or default is reasonably foreseeable, has not yet been modified under the HAMP, and has not yet received UP forbearance. Additionally, the borrower must: be eligible for HAMP, make the request before becoming seriously delinquent (three months overdue on monthly payments), and be unemployed. An unemployed borrower who requests HAMP assistance must be evaluated for and receive UP forbearance before being considered for a HAMP modification, if all criteria are met. Servicers may require as a pre-condition to approval that borrowers be in receipt of unemployment benefits for up to three months before the forbearance period begins. Once in the program, if a borrower regains employment, the forbearance ends. If the borrower still meets HAMP eligibility, the servicer must consider him for a permanent HAMP modification, and any arrearages are capitalized as part of the standard HAMP process. If the borrower is still unemployed at the end of the forbearance period, the borrower will be considered for a HAMP foreclosure alternative, like HAFA or PRA.[87] A unique feature of this program is that no TARP funds are obligated to it.

Recent research has suggested that the loss of a job is a significant factor in a homeowner's determination of whether or not to default on a loan and that foreclosure prevention policy that addresses this finding would be more effective than traditional modifications. Researchers at the Federal Reserve Banks of Boston and Atlanta conclude that unaffordable loans, defined as those with high monthly payments relative to income at the time of origination, are unlikely to be the main reason borrowers default. Their analysis concludes a better served policy would be one that cushions the immediate effects of job loss or other adverse life events instead of conducting mortgage modifications aimed at long-term affordability.[88] As nearly 60 percent of borrowers report loss of income through reduction in hours or lost jobs as the primary reason for permanent modification, Treasury's unemployment program has the potential to reduce significantly foreclosures prompted by job loss.[89]

Home Affordable Foreclosure Alternatives (HAFA)

Announced on November 30, 2009,[90] but not effective until April 5, 2010,[91] Treasury's HAFA program was created to encourage the use of short sales and deeds-in-lieu of foreclosure for HAMP-eligible borrowers unable to qualify for modifications of currently under-

[86] *See* Supplemental Directive 10–04, *supra* note 84.
[87] *See* Supplemental Directive 10–04, *supra* note 84.
[88] Christopher Foote et al., *Reducing Foreclosures: No Easy Answers,* Federal Reserve Bank of Atlanta Working Paper No. 2009–15 (May 2009) (online at www.frbatlanta.org/filelegacydocs/wp0915.pdf) (hereinafter "Federal Reserve Bank of Atlanta Working Paper").
[89] Data provided by Treasury.
[90] U.S. Department of the Treasury, *Making Home Affordable: HAMP Update—New Program Offers Borrowers Foreclosure Alternatives* (Nov. 30, 2009) (online at www.hmpadmin.com/portal/news/docs/2009/hampupdate113009.pdf).
[91] U.S. Department of the Treasury, *Making Home Affordable: HAMP Updates—New Supplemental Directives Issued* (Mar. 26, 2010) (online at www.hmpadmin.com/portal/news/docs/2010/hampupdate032610.pdf).

water mortgages. Servicers agree to forfeit the ability to seek a deficiency judgment in exchange for borrowers engaging in short sales or issuing a deed-in-lieu of foreclosure. Essentially, a servicer agrees to accept the property itself in satisfaction of a borrower's mortgage obligation. All parties receive financial incentives in the form of relocation assistance, one-time completion, and reimbursement to release subordinate liens.

Second Lien Modification Program (2MP)

The 2MP was announced on April 28, 2009, and went into effect on August 14, 2009.[92] This program was created to address the issue of homeowners remaining distressed even after their first liens were modified because there was also a second lien on the property. Borrowers are eligible to apply for the 2MP after their corresponding first liens have been modified under HAMP. Although servicer participation is voluntary, once on board, servicers must modify or extinguish the second liens of all eligible borrowers.[93] All 2MP modifications must consist of: an interest rate reduction, an extension of term years matching that of the first lien modification, and principal forbearance or principal reduction matching the percentage of any principal forbearance or reduction of the first lien.[94] All parties receive incentive payments for their participation.

Hardest Hit Fund (HHF)

The HHF provides TARP money to state-run foreclosure mitigation programs in specific states hit hardest by home value decreases and high unemployment rates. In a series of announcements, Treasury has stated that 18 states and the District of Columbia are eligible for HHF funding. Before receiving the funds, eligible states must submit and receive approval for their plans to use the money. To date, there have been four rounds of funds approved and expended under the HHF. The first round of HHF funding was announced on February 19, 2010, and the plan to distribute the first round of funds was approved on June 23, 2010. The first-round money went to qualifying states where the average home price declined by more than 20 percent from its peak: Arizona, California, Florida, Michigan, and Nevada.[95] The second-round funding went to the top five states (excluding those included in the first round) with the highest shares of their state populations living in counties in which the unemployment rate exceeded 12 percent, on average, over the twelve calendar months in 2009. The states receiving the second round of funding are North Carolina, Ohio, Oregon, Rhode Island, and South Carolina.[96] The third-

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[92] U.S. Department of the Treasury, *Making Home Affordable: Second Lien Modification Program Details Announced* (Aug. 14, 2009) (online at www.hmpadmin.com/portal/news/docs/2009/hampupdate081409.pdf).

[93] U.S. Department of the Treasury, *Making Home Affordable Program, Policy Update,* Supplemental Directive 10–16 (Nov. 23, 2010) (online at www.hmpadmin.com/portal/programs/docs/hamp_servicer/sd1016.pdf).

[94] *Id.*

[95] U.S. Department of the Treasury, *Update on HFA Hardest-Hit Fund* (Mar. 5, 2010) (online at www.makinghomeaffordable.gov/pr_03052010.html).

[96] U.S. Department of the Treasury, *Update to the HFA Hardest Hit Fund Frequently Asked Questions,* at 4 (Mar. 29, 2010) (online at financialstability.gov/docs/Hardest%20Hit%20public%20QA%200%2029%2010.pdf).

round funding went to qualifying states, including those that received funding in prior rounds, with an unemployment rate at or above the national average during the previous 12 months: Alabama, California, Florida, Georgia, Illinois, Indiana, Kentucky, Michigan, Mississippi, Nevada, New Jersey, North Carolina, Ohio, Oregon, Rhode Island, South Carolina, Tennessee, and the District of Columbia.[97] The fourth-round dollars were provided to existing HHF participants to be used in approved programs.[98] A total of $7.6 billion in TARP funds has been allocated for the HHF.

All state recipients of HHF funds are using at least a portion of those funds to aid unemployed homeowners. California, for example, has developed a program targeting unemployed homeowners. Under that program, homeowners could receive a mortgage subsidy for up to 6 months, with monthly benefit of up to $1,500 or 50 percent of existing total monthly mortgage payment. Other states, such as Arizona, have developed programs intended to help any struggling homeowner with a demonstrated hardship and who meets certain qualifications. Among the recognized hardships are unemployment as well as medical condition, divorce, and death. Many of the proposed HHF programs are aimed at low- to moderate-income families, requiring those eligible to have a household income of no more than 120 or 140 percent of median household income. These programs are all in the early stages of implementation, and there are not yet data available on the programs' results.

In August 2010, HUD announced the $1 billion Emergency Homeowners Loan Program (EHLP) to complement Treasury's Hardest Hit Fund and continue to target unemployed borrowers at risk of foreclosure. The program will provide assistance to homeowners in Puerto Rico and 32 states not funded by Treasury's Innovation Fund for Hardest Hit Housing Markets program through a declining balance, deferred payment bridge loan for up to $50,000 to assist borrowers with arrearages and mortgage payments for up to 24 months. HUD intends to start taking applications by the end of this year.[99]

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[97] U.S. Department of the Treasury, *Troubled Asset Relief Program Section 105(a) Report—August 2010* (Sept. 10, 2010) (online at www.financialstability.gov/docs/105CongressionalReports/August%202010%20105(a)%20Report__final__9%2010%2010.pdf).

[98] U.S. Department of the Treasury, *Troubled Asset Relief Program—Two Year Retrospective* (Oct. 2010) (online at www.financialstability.gov/docs/TARP%20Two%20Year%20Retrospective__10%2005%2010__transmittal%20letter.pdf) (hereinafter "TARP Two Year Retrospective").

[99] The HUD EHLP loans will be non-recourse, zero-interest, subordinate loans. U.S. Department of Housing and Urban Development, *Emergency Homeowner Loan Program—Summary* (Oct. 8, 2010) (online at www.hud.gov/offices/hsg/sfh/hcc/msgs/EHLP100810.pdf). The Pennsylvania Housing Finance Agency implemented a similar program, the Homeowners' Emergency Mortgage Assistance Loan Program (HEMAP), which targets borrowers facing foreclosure who are dealing with financial hardship due to circumstances beyond their control (i.e., unemployment, wage loss, illness). HEMAP provides a loan of up to $60,000 that cannot exceed a period of 24 months (or 36 months in the case of unemployment) to cover mortgage payments. The loan is considered a mortgage lien against the homeowner's property. Non-continuing loan recipients must begin repayment immediately following loan closing at a monthly amount based on income but not less than $25 per month. Payment increases are based on 40 percent of a homeowner's net monthly income less total monthly housing expense. Continuing loan recipients begin repayment immediately following termination of continuing loan disbursements. Pennsylvania Housing Finance Agency, *Frequently Asked Questions (FAQ)* (online at www.phfa.org/hsgresources/faq.aspx) (accessed Dec. 1, 2010).

FHA Short Refinance Program

The FHA Short Refinance Program was announced on March 26, 2010,[100] and went into effect on September 7, 2010.[101] This program was created to refinance non-FHA-insured underwater mortgages into above-water, FHA-insured mortgages. Eligible borrowers are not guaranteed a refinance, and program participation is voluntary for servicers on a case-by-case basis. Under the terms of the refinance, the existing lien holder is given a cash payment equal to 97.75 percent of the current home value and issued a subordinate second lien for up to 17.25 percent of the current home value, if applicable. Thus, the existing lien holder can retain an interest in up to 115 percent of the current home value, but any interest above 115 percent of the current home value is deemed forgiven. The new FHA-insured mortgage payments can be no more than 31 percent of the borrower's gross monthly income.

Other Agency Programs

Lastly, Treasury has coordinated with the FHA, the United States Department of Agriculture, and the VA to encourage modification of the mortgages they insure. These agencies have each developed their own versions of HAMP, in support of which Treasury provides incentive payments to servicers and borrowers. No incentive payments are made to investors, because they already have the benefit and protection of a government loan guarantee.

As stated earlier, there is not yet sufficient data available to analyze whether these programs are achieving their goals or operating effectively. While the Panel appreciates the length of time involved in moving a program from inception to data validation, the timely availability of data is a key component of transparency and oversight, and the Panel urges Treasury to continue working towards this goal. For an analysis of the structural aspects of these programs, and the Panel's recommendations as to addressing new issues surrounding foreclosure mitigation programs overall, see the Panel's April 2010 report.

G. Barriers to Success

1. What Are HAMP's Goals?

In considering whether a program has been a success, the goals and metrics outlined for that program offer an important yardstick. When the stated objectives are limited or not meaningful, the scope of oversight and analysis is narrowed. Treasury's only explicitly stated goal for HAMP is to offer three to four million homeowners lower mortgage payments through a modification.[102] As noted in the Panel's April report, the meaning of even that one goal has shifted over time. Treasury and the administration initially stated

[100] U.S. Department of Housing and Urban Development, *Housing Program Enhancements Offer Additional Options for Struggling Homeowners* (Mar. 26, 2010) (online at portal.hud.gov/portal/page/portal/HUD/press/press_releases_media_advisories/2010/HUDNo.10-058).

[101] U.S. Department of Housing and Urban Development, *FHA Launches Short Refi Opportunity for Underwater Homeowners* (Aug. 6, 2010) (online at portal.hud.gov/portal/page/portal/HUD/press/press_releases_media_advisories/2010/HUDNo.10-173).

[102] U.S. Department of the Treasury, *Making Home Affordable Program: Servicer Performance Report Through January 2010,* at 2 (Feb. 18, 2010) (online at www.financialstability.gov/docs/press/January%20Report%20FINAL%2002%2016%2010.pdf).

a goal of ensuring that three to four million homeowners avoid foreclosure and remain in their homes.[103] This nebulous target gave rise to uncertainty about Treasury's goal: did Treasury intend HAMP's three to four million target to refer to permanent modifications, as was widely assumed? Or did the goal refer to trial modifications started, or merely trial modifications offered?

A year into the program's life, Treasury clarified its goal by stating its intended objective is to offer three to four million modifications, with one Treasury official estimating that the number of permanent modifications would be only between 1.5 and 2 million.[104] This not only cut what was assumed to be the initial modification goal in half but also established a relatively meaningless measurement, trial modification offers, as the touchstone for program success.

Recently, Treasury has claimed that the existence of a government foreclosure program—HAMP—accelerated the number of proprietary modifications.[105] While counting these non-HAMP modifications as successful "HAMP" modifications would allow Treasury to come closer to its three to four million target, the lack of public data by servicers on the terms of proprietary modifications hinders the ability to assess properly whether these modifications are actually helping homeowners. While Treasury believes that HAMP accelerated the pace of proprietary modifications, when pressed, Treasury acknowledges that there is no clear causal link between HAMP and proprietary modifications.[106]

Treasury has not explicitly stated its own definition of program success, noting only that it plans to evaluate success in the context of the state of the economy over time,[107] and remains elusive on this issue when questioned by the Panel and others.[108] Using its singular goal, however, one can reasonably infer that success, from Treasury's point of view, is measured by reaching three to four million trial modification offers. Under this definition, the program has not been "successful" to date, as nearly 1.65 million trial plan offers have been extended through October 2010. As noted in Section D above, trial modification offers have significantly declined

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[103] April 2010 Oversight Report, *supra* note 1, at 63; Office of the Special Inspector General for the Troubled Asset Relief Program, *Factors Affecting Implementation of the Home Affordable Modification Program* (Mar. 25, 2010) (online at sigtarp.gov/reports/audit/2010/Factors_Affecting_Implementation_of_the_Home_Affordable_Modification_Program.pdf) (hereinafter "SIGTARP Report—Factors Affecting Implementation of HAMP").

[104] SIGTARP Report—Factors Affecting Implementation of HAMP, *supra* note 103, at 10.

[105] Treasury conversations with Panel staff (Oct. 21, 2010). *See* TARP Two Year Retrospective, *supra* note 98, at 67 ("A cancelled trial modification does not mean that the program has completely failed a homeowner or that the borrower will inevitably face foreclosure: HAMP explicitly requires servicers to consider these borrowers for other foreclosure prevention options including proprietary modifications or other options like a short sale or deed-in-lieu of foreclosure that also prevent a foreclosure sale. The broader HAMP program provides borrowers with a range of assistance; success can only be measured on an aggregate basis, taking account of homeowners' individual situations and outcomes.").

[106] Treasury conversations with Panel staff (Oct. 21, 2010).

[107] Treasury conversations with Panel staff (Oct. 21, 2010).

[108] *See* Congressional Oversight Panel, Testimony of Phyllis Caldwell, chief of the Homeownership Preservation Office, U.S. Department of the Treasury, *Transcript: COP Hearing on TARP Foreclosure Mitigation Programs* (Oct. 27, 2010) (publication forthcoming) (online at cop.senate.gov/hearings/library/hearing-102710-foreclosure.cfm) (hereinafter "Transcript Testimony of Phyllis Caldwell"). *See also* Congressional Oversight Panel, Written Responses of Timothy F. Geithner, secretary, U.S. Department of the Treasury, *COP Hearing with Treasury Secretary Timothy Geithner* (June 22, 2010) (online at cop.senate.gov/documents/testimony-062210-geithner-qfr.pdf); This Week with Jake Tapper, *Interview with Treasury Secretary Timothy Geithner,* ABC News Television Broadcast (Feb. 7, 2010) (online at abcnews.go.com/ThisWeek/week-transcript-treasury-secretary-timothy-geithner/story?id=9758951).

since September 2009 and seem to have leveled off recently. Although Treasury is halfway to its goal with two years remaining in the program's life, and the long-term trend is uncertain, at the current rate of trial offers, HAMP is not on target to meet its one goal.[109] Assuming a continued pace of 20,000 to 30,000 offers per month going forward,[110] HAMP will provide a cumulative total of only 2.17 to 2.43 million trial modification offers.[111] And if the current pace of new permanent modifications continues, the program will result in only about 1.26 million permanent modifications, many of which will likely end in redefaults.[112]

The Congressional Budget Office (CBO) last month projected that Treasury will spend only $12 billion on all TARP housing programs, including HAMP and the Hardest Hit Fund, out of the $45.6 billion in TARP funds allocated for those programs.[113] While the CBO did not publish a breakdown of how it expects the projected $12 billion to be divided between the various TARP housing programs, if one assumes that the Hardest Hit Fund-recipient states will spend the $7.6 billion allocated to them in grants, that would leave only $4.4 billion to be spent on HAMP and the other TARP housing programs.[114]

Treasury has declined to state publicly any metrics or benchmarks by which HAMP should be judged, a fact that has frustrated Congress and TARP oversight bodies, and has made clear to the Panel that it has no other unarticulated goals for HAMP.[115] As stated earlier, the absence of additional, more meaningful goals hinders the Panel's ability to perform oversight and adequately assess HAMP's level of success or failure. The Panel has expressed concerns about Treasury's lack of transparency and accountability in regards to its goals for HAMP, noting in its April report that ". . . Treasury needs to take care to communicate its goals, its strategies, and its measures of success for its programs. Its stated goal of modifying three to four million mortgages has proven too vague. . . ."[116] Further, the Panel has continued to urge Treasury to develop specific objectives for other program measures.[117] In its most recent Quarterly Report to Congress, the Special Inspector General for the Troubled Asset Relief Program (SIGTARP) clearly

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[109] MHA Servicer Performance Report, *supra* note 38, at 2.

[110] The Panel previously noted in its October 2009 report that Treasury officials stated a goal of modifying 25,000 to 30,000 loans per week; however, the actual pace is currently only 20,000 to 30,000 trial modifications per month. October 2009 Oversight Report, *supra* note 15, at 4; Data provided by Treasury.

[111] Panel staff calculation using assumed range of 20,000 to 30,000 trial modification offers per month over the remaining 26 months of the program's life, added to the actual cumulative total of 1.65 million offers through October 2010.

[112] Panel staff calculation that assumes 28,311 new permanent modification each month through December 2012, based on the average number of new permanent modifications between August–October 2010.

[113] Congressional Budget Office, *Report on the Troubled Asset Relief Program—November 2010,* at 7 (Nov. 29, 2010) (online at www.cbo.gov/ftpdocs/119xx/doc11980/11-29-TARP.pdf) (hereinafter "CBO Report on the TARP—November 2010").

[114] Through November 2010, Treasury has spent $652.4 million on the first-lien portion of HAMP, $71.3 million on HPDP, $4.3 million on HAFA, $959,1335 on 2MP, and $8,990 on FHA–HAMP. Data provided by Treasury.

[115] Treasury conversations with Panel staff (Oct. 21, 2010).

[116] April 2010 Oversight Report, *supra* note 1, at 95.

[117] Congressional Oversight Panel, *Transcript: COP Hearing on TARP Foreclosure Mitigation Programs* (Oct. 27, 2010) (publication forthcoming) (online at cop.senate.gov/hearings/library/hearing-102710-foreclosure.cfm).

pointed out Treasury's lack of meaningful program benchmarks or measures of success:

> SIGTARP, along with the other TARP oversight bodies (GAO and the Congressional Oversight Panel), has long argued that Treasury should adopt meaningful benchmarks and goals for HAMP, including setting forth its expectations and goals for the most meaningful aspect of HAMP—permanent modifications that offer secure, sustainable relief to the program's intended beneficiaries. Remarkably, Treasury has steadfastly rejected these recommendations, and now finds itself defending a program that is failing to meet TARP's goal of "preserv[ing] homeownership." . . . and it has steadfastly and explicitly declined to articulate well-considered, consistent, and meaningful success standards for HAMP. . . . Instead it continues to cite the number of HAMP trial modifications, as opposed to permanent modifications, as an indication of success. . . . While it may be true that many homeowners may benefit from temporarily reduced payments even though the modification ultimately fails, Treasury's claim that "every single person" who participates in HAMP gets "a significant benefit" is either hopelessly out of touch with the real harm that has been inflicted on many families or a cynical attempt to define failure as success. Worse, Treasury's apparent belief that all failed trial modifications are successes may preclude it from seeking to make the meaningful changes necessary to provide the "sustainable" mortgage relief for struggling families it first promised.[118]

During a July Senate Finance Committee hearing with TARP oversight bodies, Senator Charles Grassley (R–Iowa) similarly noted, "Moreover, Treasury still has not established performance goals or benchmarks for HAMP, meaning that there is no effective way for us to know whether this 50 billion dollar program is accomplishing its intended purpose. That's not accountability, that's not transparency—that's just more taxpayer money flying out the window."[119] Richard Hillman, managing director of financial markets and community investment team at the Government Accountability Office (GAO), emphasized that even as Treasury created new programs and modified existing programs under the MHA initiative, it failed to redefine the program's reach and goals, undercutting program transparency.[120] Despite Treasury's frequent changes to the program, despite HAMP's inadequate performance compared to

[118] Senate Committee on Finance, Written Testimony of Neil Barofsky, Special Inspector General for the Troubled Asset Relief Program, *An Update on the TARP Program,* at 3 (July 21, 2010) (online at finance.senate.gov/imo/media/doc/072110nbtest.pdf).

[119] Senate Committee on Finance, Opening Statement of Senator Chuck Grassley, *An Update on the TARP Program,* at 2 (July 21, 2010) (online at finance.senate.gov/imo/media/doc/072110CG.pdf).

[120] Senate Committee on Finance, Written Testimony of Richard Hillman, managing director, Financial Markets and Community Investment Team, U.S. Government Accountability Office, *An Update on the TARP Program,* at 11 (July 21, 2010) (online at finance.senate.gov/imo/media/doc/072110rhtest.pdf) ("Treasury announced several potentially substantial new HAMP-funded efforts in March 2010, but did not say how many borrowers these programs were intended to reach. . . .We noted that Treasury needed to ensure that future public reporting on this program [principal reduction initiative] provided program transparency and address the potential question of whether borrowers were being treated fairly.").

Treasury's initially stated goal, and despite the urgings of Congress and oversight bodies to articulate a meaningful benchmark for success beyond the initial, opaque goal of "reaching" three to four million homeowners, Treasury has failed to do so.

As SIGTARP noted in its March 2010 report on HAMP, "the anticipated benefits of a program . . . and how a program's success or failure is defined are important to provide a reference point for discussions about whether a program is worth the resources devoted to it and whether the program is functioning as it should." [121] While Treasury has clarified its target goal of trial modification offers, it has not provided a clear definition of program success. Meeting a goal that has no basis in whether borrowers have actually received help does not make a program successful, and, as noted in Section D.2, intense focus on one goal over another can limit broader success. In order to demonstrate the legitimacy and effectiveness of its chief foreclosure mitigation program, the Panel believes Treasury should clearly articulate its definition of success for HAMP, allowing the defined benchmarks to be the true measure of HAMP's worth.

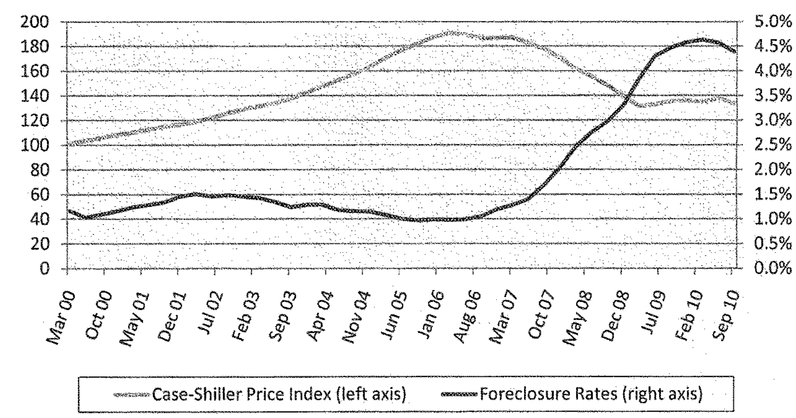
The Panel stated in its April 2010 report that Treasury's success with HAMP will be measured by the number of homeowners who avoid foreclosure, not the number of mortgages modified.[122] It is difficult to track precisely the number of homeowners who have avoided foreclosure because of HAMP, as there are no public data for foreclosure avoidance due to trial modification only, so the most recent modification results are the closest proxy. As of October 31, 2010, HAMP has 156,408 active trial modifications and 483,342 active permanent modifications.[123] Thus, 639,750 homeowners are currently avoiding foreclosure, on either a temporary basis or for five years, through HAMP.[124] Foreclosure starts since HAMP's inception, on the other hand, reached a total of approximately 4.4 million in October 2010.[125] These results mean that since HAMP was unveiled, there have been just over nine foreclosure starts for every one permanent, or five-year, HAMP modification.[126]

While the number of foreclosure starts that were HAMP eligible is unknown, as of October 31, 2010, only 29 percent of loans 60 or more days delinquent were estimated to be eligible for HAMP modification, as noted in Section D.[127] As the Panel noted in its April 2010 report, certain HAMP exclusions prevent aid from flowing to speculators, wealthy borrowers, those covered by other modification programs, or those unlikely to benefit from HAMP. Other HAMP exclusions, however, such as borrowers with nonpartici-

[121] SIGTARP Report—Factors Affecting Implementation of HAMP, *supra* note 103, at 8.
[122] April 2010 Oversight Report, *supra* note 1, at 95.
[123] Data provided by Treasury.
[124] Data provided by Treasury. (The trial period typically lasts for three months to provide immediate relief and ensure that the new payment plan will work for the borrower.)
[125] The total of 4.4 million starts includes foreclosure starts from March 2009, the time of HAMP's inception, through October 2010. The number of foreclosure starts is an imperfect data point, as it is incomplete, potentially redundant, and is extrapolated out to determine national totals; however, it is helpful in providing the ability to track trends in foreclosures. These flaws emphasize the need for the government to collect data on foreclosure starts and completions on a nationwide basis. Over this same time period, the number of foreclosure completions, or actual foreclosure sales, reached nearly 1.8 million. HOPE NOW Alliance Foreclosure Data.
[126] Panel staff calculation using total foreclosure starts through October 2010 of 4.4 million and total permanent HAMP modifications that are active or paid off (excluding those that were disqualified or cancelled) of 483,833 as of October 31, 2010. Data provided by Treasury.
[127] Data provided by Treasury.

pating servicers and those with DTI less than 31 percent, may be preventing a significant number of modifications and more positive program results. Foreclosure rates remain at historically very elevated levels, and housing prices have not recovered significantly compared to the highs reached in the middle of the decade, as indicated in Figure 12 below. Therefore, it is unclear whether HAMP has made appreciable improvement in the unstated but implicit goals of reducing foreclosures and stabilizing the housing markets.

FIGURE 12: FORECLOSURE RATE AND HOME VALUES [128]



Despite HAMP's lack of clearly articulated goals and metrics, the program has had a positive impact in another way, even if inadvertently so. It has provided standardization of the mortgage modification process, an issue noted as a significant industry problem in the past,[129] by encouraging the use of a common model, reporting platform, and affordability measurement.[130] Phyllis Caldwell, chief of Treasury's Homeownership Preservation Office, noted at the Panel's most recent hearing on foreclosure mitigation, ". . . it [HAMP] has helped transform the way the entire mortgage servicing industry operates. HAMP established a universal affordability standard, a 31 percent debt to income ratio." [131] Ms. Schwartz reiterated these sentiments, stating, ". . . it's very integral and important that the government stepped forward to put a protocol in place for modifications and that this protocol would have been very difficult to get into place otherwise . . . . And HAMP offers uniformity of approach, which is fair and systematic in its approach for all homeowners at risk." [132] While Treasury was not the first entity to propose or employ a 31 percent standard, through the parameters of HAMP and substantial servicer participation, Treasury

[128] Bloomberg data (graph created from FORLTOTL and SPCSUSS indices) (accessed Dec. 9, 2010). Data for the Case-Shiller Price Index are normalized to 100 at March 2000.
[129] *See* Joseph R. Mason, *Mortgage Loan Modification: Promises and Pitfalls,* at 17 (Oct. 3, 2007) (online at www.lebow.drexel.edu/PDF/Docs/20071003LoanModificationPaper.pdf).
[130] Transcript Testimony of Phyllis Caldwell, *supra* note 108.
[131] Transcript Testimony of Phyllis Caldwell, *supra* note 108.
[132] Testimony of Faith Schwartz, *supra* note 78.

solidified the wide acceptance of 31 percent as an industry affordability standard.[133]

Nonetheless, when viewed in light of the millions of foreclosure completions since 2007 and the large number waiting in the pipeline due to continued hardships from high unemployment rates and lower home values, HAMP has failed to make a significant dent in the number of foreclosures and does not appear likely to do so in the future.

2. Factors Affecting HAMP Success

In many cases, mortgage modifications are economically rational; the investor loses less money on a modification than the losses that it would incur under a foreclosure. In a well-functioning market, modifications, principal forgiveness, and refinancings will occur as long as they are in the best interests of all parties. If a mortgage modification allows a lender or investor to sustain a smaller loss than a foreclosure and allows a borrower to remain in his home at a sustainably affordable monthly payment, then incentives to modify the loan should be unnecessary. However, as discussed in Section B, the housing market has been in a state of disequilibrium, and the private sector failed to conduct modifications on its own, which triggered government intervention in the form of HAMP and the use of incentives to enhance the likelihood that the decision scale tipped in favor of modification.

HAMP is premised upon the idea of economically rational mortgage modifications—beneficial to both borrower and investor—as embodied in its NPV model. The model is explicitly designed to determine whether a modification or a foreclosure makes more sense economically for the mortgage holder. If the NPV model shows that it is economically better to modify the mortgage, participating servicers are compelled to make the modification. HAMP also added financial incentive payments for investors, servicers, and borrowers, some of which are included in the NPV model calculations, to promote participation further. These incentives were designed to encourage mortgage modifications by lessening the financial burden on all parties, especially given the dearth of private-

[133] In testimony before the Senate Banking, Housing, and Urban Affairs Committee in November 2008, Martin D. Eakes, CEO of Self-Help and Center for Responsible Lending, noted the industry standard of 38 percent DTI but urged Congress to push Treasury to utilize TARP to create a modification program that required 31 percent DTI, referencing the FDIC proposal at the time to use TARP funds for a modification program with a 31 percent HTI (housing-to-income). Eakes noted that the standard had moved over time from a lending standard of 25 percent DTI to the current 38 percent. *See* Senate Committee on Banking, Housing, and Urban Affairs, Written Testimony of Martin D. Eakes, chief executive officer, Self-Help Credit Union and the Center for Responsible Lending, *Oversight of the Emergency Economic Stabilization Act: Examining Financial Institution Use of Funding Under the Capital Purchase Program,* at 8 (Nov. 13, 2008) (online at banking.senate.gov/ public/ index.cfm? FuseAction=Files. View&FileStore_id=26c73c7a-bafc-4ff1–88f9-e984d672c9f6). Gregory Palm, Executive Vice President and General Counsel of The Goldman Sachs Group, also testified at the hearing that Litton Loan Servicing, Goldman Sachs' affiliate, was already employing a 31 percent DTI standard. *See* Senate Committee on Banking, Housing, and Urban Affairs, Testimony of Gregory K. Palm, executive vice president and general counsel, The Goldman Sachs Group, Inc., *Transcript: Oversight of the Emergency Economic Stabilization Act: Examining Financial Institution Use of Funding Under the Capital Purchase Program,* at 8 (Nov. 13, 2008) (publication forthcoming) (online at banking.senate.gov/public/ index.cfm? FuseAction= Hearings. Hearing& Hearing_ ID=1d38de7d- 67db- 4614–965b-edf5749f1fa3). The IndyMac Federal program implemented by the FDIC utilized a DTI standard of 38 percent. Federal Deposit Insurance Corporation, *FDIC Implements Loan Modification for Distressed IndyMac Mortgage Loans* (Aug. 20, 2008) (online at www.fdic.gov/news/news/press/2008/pr08067.html).

sector modifications at the outset of HAMP and to offset any disincentives.[134]

As of the October 3, 2010 deadline for enrolling in HAMP, 105 servicers,[135] covering nearly 90 percent of all non-GSE mortgage loans, had signed Servicer Participation Agreements.[136] Servicers of GSE mortgages are required to evaluate mortgages for HAMP. Thus, the program clearly has broad coverage of the mortgage market.

Yet, despite this broad commitment by servicers to participate in a program that offers additional payments on top of an often economically rational decision, HAMP's results remain underwhelming. Why has HAMP failed to deliver? It is unclear what the additional cost would be to provide sufficient incentives to induce greater numbers of modifications, and there does not appear to be one single answer as to why HAMP has not resulted in more modifications. Rather, it appears that multiple factors have inhibited otherwise sensible mortgage modifications.

a. Voluntary Nature of the Program

A key characteristic that has limited Treasury's influence over servicers is the voluntary nature of the program for servicers of non-GSE loans.

Although Treasury has been able to pressure servicers to sign participation agreements, Treasury has little ability to pressure servicers when it comes to actually making modifications. This structure has created an imbalance of power between Treasury and the servicers, and has hindered Treasury's ability to influence, oversee, and compel servicers into more aggressive action. According to Treasury officials, "Because it is a voluntary program, our abilities to enforce specific performance are extremely limited,"[137] and it "makes aggressive enforcement difficult."[138] The California Reinvestment Coalition has noted that the voluntary nature of the program is a hindrance to success. Its recent survey of mortgage counselors indicated a growing frustration with servicers not following HAMP requirements and Treasury not enforcing servicer compliance.[139] Treasury has focused on establishing a tone of program compliance, directing servicers to fix issues instead of doling out penalties.[140] Although Treasury oversees servicers and encourages compliance, there is little real accountability for servicers that fail to adhere to program standards, lose borrower submitted paperwork, unnecessarily delay the process, or otherwise don't make modifications. In describing this system of incentives with no real sticks, Professor Katherine Porter, a professor of law who testified at the Panel's October hearing, said, ". . . [servicers] have gorged

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[134] Transcript Testimony of Phyllis Caldwell, *supra* note 108 ("No, I think it's that when you look back at the beginning of the program—again, HAMP was a—is a voluntary program—getting the servicers, the investors and the homeowners to the table and to change their business model to—to do that required some incentives.").

[135] Treasury conversations with Panel staff (Oct. 21, 2010).

[136] TARP Two Year Retrospective, *supra* note 98, at 65.

[137] Treasury conversations with Panel staff (Sept. 10, 2010).

[138] Treasury conversations with Panel staff (Oct. 21, 2010).

[139] California Reinvestment Coalition, *Chasm Between Words and Deeds IV: HAMP Is Not Working,* at 2, 9–11 (July 2010) (online at www.calreinvest.org/system/assets/234.pdf) (hereinafter "Chasm Between Words and Deeds IV: HAMP Is Not Working").

[140] Treasury conversations with Panel staff (Oct. 21, 2010).

themselves at a buffet of carrots, and they're still not doing what we want them to do." [141]

The Panel has previously noted that servicers need to face "meaningful monetary penalties" for noncompliance with SPAs and denial of modification for an unexplained reason, a breach of their contractual obligations under HAMP SPAs.[142] However, Treasury has seemed reluctant to do more than vaguely threaten the potential for clawbacks of HAMP payments.[143] Despite rampant anecdotal stories of servicer errors, to date, no servicer has experienced a clawback or other financial repercussion. The steepest penalty Treasury has levied to date has been withholding payments to servicers due to data issues. But after remedying the problem, these servicers will receive any missed incentive payments, despite a prolonged remediation process.[144] By signing HAMP participation agreements, servicers indicated that they agreed with the NPV model and would provide modifications based on the model's results. They knew they were legally obligated to do so when they signed.

An additional challenge of voluntary participation is the issue of potential servicer withdrawal. Despite a formal contract for those who voluntarily participate, the contract does not explicitly address servicer withdrawal. It is unclear whether or not servicers can withdraw without Treasury's consent, creating uncertainty regarding the ramifications should a servicer decide unilaterally to exit the program. The Servicer Participation Agreements (SPAs) require participating servicers to offer HAMP modifications to all eligible borrowers, but the contracts do not explicitly compel servicers to remain in the program. Some servicers have exited HAMP for various reasons,[145] and Treasury has indicated that in those instances it worked with the servicer to ensure that the HAMP-modified loans remained in the program or were transferred to another HAMP servicer. Further, Treasury noted that its concern with servicer exit is most applicable to the larger servicers. Should a servicer choose to exit the program without Treasury's consent, Treasury has indicated to the Panel that it could potentially sue the servicer for specific performance.[146] Treasury encouraged servicer participation by adding incentives to the program and by

[141] Congressional Oversight Panel, Testimony of Katherine Porter, professor of law, University of Iowa College of Law, *Transcript: COP Hearing on TARP Foreclosure Mitigation Programs* (Oct. 27, 2010) (publication forthcoming) (online at cop.senate.gov/ hearings/ library/ hearing-102710-foreclosure.cfm).

[142] April 2010 Oversight Report, *supra* note 1, at 55.

[143] *See* House Committee on Financial Services, Written Testimony of Herbert M. Allison, Jr., assistant secretary for financial stability, U.S. Department of the Treasury, *The Private Sector and Government Response to the Mortgage Foreclosure Crisis,* at 3 (Dec. 8, 2009) (online at financial services. house. gov/ media/ file/ hearings/ 111/ herb_allison.pdf); Rob Chrisman, *Cinco de Mayo: HAMP Incentives Denied to NonCompliant Servicers? High Balance Loans; PennyMac Earnings; Flood Zone Alert,* Mortgage News Alert (May 5, 2010) (online at www.mortgagenewsdaily.com/ channels/ pipelinepress/ 05052010-hamp-greece.aspx).

[144] Treasury noted that it is currently considering no longer accruing missed incentive payments to the five servicers that have failed to remedy their data issues. Treasury conversations with Panel staff (Oct. 21, 2010).

[145] Treasury conversations with Panel staff (Oct. 21, 2010). Treasury noted that servicers might exit due to having better proprietary modification options or because of the costs of participating in HAMP (e.g., labor and time needed to complete additional paperwork). Treasury indicated that the latter has occurred.

[146] Treasury conversations with Panel staff (Oct. 21, 2010).

sharing some of the financial burden of modifying a loan.[147] Servicers that do not participate also face the public stigma of being seen as unwilling to help homeowners avoid foreclosure.

A program structure in which participation is voluntary and the repercussions of exit are uncertain has presented a key problem within HAMP: namely a lack of accountability for performance. Without more useful, publicly available performance data, transparency is compromised, and without stringent enforcement of contractual obligations, servicer underperformance is unpunished. Of course, such an inability to enforce standards would be an Achilles heel in virtually any voluntary foreclosure mitigation program design.

b. Accounting Issues

Because of the latitude participating servicers have in ultimately granting a modification with little accountability for performance, many external incentives or disincentives will remain crucial in shaping the decision to modify a loan. As discussed in the Panel's April 2010 Report, the current accounting rules provide investors a disincentive to modify loans under HAMP.[148] Since HAMP loans are contractually modified, under the current accounting rules there is immediate loss recognition for financial institutions.[149] For other loans that are not modified, the current accounting rules provide a financial institution more discretion to determine when a loss should be recognized.[150] In addition, write-downs on loans would require financial institutions to boost their regulatory capital ratios. As a result, financial institutions are reluctant to write down mortgages since their capital structures have already been weakened by a variety of factors, including write-downs already taken on residential and commercial real estate loans, losses taken on other loans due to the recession, and recent actions by Fannie

[147] Servicers that make modifications to get a homeowner down to a 38 percent mortgage DTI ratio receive aid from Treasury in the form of half of the remaining cost of getting the borrower down to a final 31 percent DTI ratio. This amount is not paid by Treasury, though, until the modification moves to permanent status. Servicers also receive an up-front payment for each eligible modification meeting program guidelines and yearly Pay for Success payments for up to three years as long as the borrower remains in the program. Initially, these payments were $1,000, but Treasury increased them to $1,500 to encourage servicers to increase their use of foreclosure alternatives and engage in additional outreach to homeowners unable to complete a modification. U.S. Department of the Treasury, *Making Home Affordable Program Enhancements to Offer More Help for Homeowners* (Mar. 25, 2010) (online at making home affordable.gov/ docs/ HAMP%20 Improvements_Fact_% 20Sheet_ 032510%20FINAL2.pdf) (hereinafter "MHA Program Enhancements to Offer More Help for Homeowners").

[148] *See* April 2010 Oversight Report, *supra* note 1, at 74. Under generally accepted accounting principles (GAAP), once the terms of a loan are contractually modified, the modified loan is accounted for as a "troubled debt restructuring." A troubled debt restructuring occurs when the terms of a loan have been modified due to the borrower's financial difficulties, and a long-term concession has been granted to the borrower. Examples of such concessions include interest rate reductions, principal forbearance, principal forgiveness, and term extensions, all of which may be used to modify loans in HAMP.

[149] For all restructured loans, GAAP requires that a loss be recognized if the difference in cash flows to be received under the modified loan is less than the cash flows of the original loan. By nature of the modified terms of the loan under HAMP (i.e., reduction of interest to be received and/or principal forbearance or forgiveness) the entity's future cash flows to be received will be less than the current loan payoff amount. *See* April 2010 Oversight Report, *supra* note 1, at 74 n. 243.

[150] Current accounting rules require that a loss contingency is required to be recognized only if it is probable that an asset has been impaired *and* the amount of the loss can be reasonably estimated. *See* April 2010 Oversight Report, *supra* note 1, at 74 n. 244.

Mae and Freddie Mac to require banks to buy back mortgages that the banks had previously sold to them.[151]

There continues to be tension between Treasury's goal of mitigating foreclosures and its goal of maintaining adequate capital levels at large banks. A new proposed accounting rule that would eliminate the disincentives to modify loans under HAMP is currently under consideration. This rule, which is to be adopted at the earliest in 2013, would require a financial institution to account for all loans similar to the accounting for HAMP loans.[152] Unfortunately, the rule will come too late to make a difference for HAMP, which will stop offering modifications in 2012.

c. Second Liens

Since the Panel's March 2009 oversight report, the Panel has been highlighting the significant financial and legal barriers that second liens impose on the successful implementation of HAMP.[153] Because more than 40 percent of homes and approximately 50 percent of HAMP participants have second liens,[154] it is important to reemphasize the importance of several of those impediments.[155] Though Treasury has recently implemented several initiatives designed to address the problems caused by second liens, these programs have not yet produced data sufficient to evaluate their success.[156]

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[151] Financial institutions are faced with write-downs on both first and second lien mortgages. *See* April 2010 Oversight Report, *supra* note 1, at 75.

[152] On May 26, 2010, the Financial Accounting Standards Board (FASB) issued proposed Accounting Standard Update (ASU), *Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities—Financial Instruments (Topic 825) and Derivatives and Hedging (Topic 815)*. The rule applies to all entities and there is a phase in period for non-public entities that have less than $1 billion in total assets. The rule would eliminate an entity's discretion to determine when a loan impairment loss should be recognized and would also require that loans and other financial instruments be classified on the balance sheet at fair value. Changes in fair value would be reported at each reporting period and would either flow through an entity's equity or net income. An adjustment to equity (other comprehensive income) would be made if the entity does not plan to sell the loan. Otherwise, the fair value adjustment would be required to flow through the income statement. *See* Financial Accounting Standards Board, *Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities—Financial Instruments (Topic 825) and Derivatives and Hedging (Topic 815)*, Financial Accounting Series FASB Exposure Draft, at paragraph 38 at 40 (May 26, 2010) (online at www. fasb. org/cs/ BlobServer? blobcol=urldata&blob table= Mungo Blobs&blobkey= id&blobwhere= 1175820761372&blobheader= application%2Fpdf).

[153] April 2010 Oversight Report, *supra* note 1, at 15.

[154] Amherst Securities Group LP, *Amherst Mortgage Insight: 2nd Liens—How Important,* at 3 (Jan. 29, 2010) (hereinafter "Amherst Mortgage Insight: Second Liens"); House Committee on Financial Services, Testimony of Phyllis Caldwell, chief of the Homeownership Preservation Office, U.S. Department of the Treasury, *Transcript: Robo-Signing, Chain of Title, Loss Mitigation, and Other Issues in Mortgage Servicing* (Nov. 18, 2010) (publication forthcoming) (online at financialservices.house.gov/Hearings/hearingDetails.aspx?NewsID=1376.)

[155] Based on data representing approximately a third of all second liens outstanding and over 75 percent of all first liens outstanding, as of September 2010, the average second lien is approximately $55,000, while the average first lien is roughly $170,000. In general, second liens that are home equity loans tend to be larger in dollar value than close-end second liens, with approximate average sizes of $57,000 and $46,000, respectively. Data provided to Panel staff by CoreLogic (Dec. 8, 2010).

[156] The second lien program was announced in April 2009, four months later, in August 2009, Treasury released the first guidance regarding the program. SIGTARP Report—Factors Affecting Implementation of HAMP, *supra* note 103, at 20. During the summer, banks commented on the interim rule and requested that second liens modified in tandem with first liens be given the same favorable treatment as the first liens, meaning that as long as certain criteria are met, loans modified under the program will retain the risk weight assigned to that loan prior to the modification. Letter from Gregory A. Baer, deputy general counsel for corporate law, Bank of America, to Jennifer J. Johnson, secretary, Board of Governors of the Federal Reserve System, et al. (July 30, 2009) (online at www.federalreserve.gov/SECRS/2009/August/20090810/R–1361/R–1361_073009_21279_428725101156_1.pdf); Letter from David Pommerehn, counsel, Legislative and Regulatory Affairs, Consumer Bankers Association, to Office of the Comptroller of the

Continued

Second liens are loans where the collateral interest for that loan is second in ranking to the primary or first lien.[157] In general terms this means that in the foreclosure process, the first lien would need to be compensated in full before the second lien would be paid from the proceeds of the sale. In other words, the first liens have lien priority. Therefore, in cases where the first lien is underwater and the home is in foreclosure, the second lien holder is generally not entitled to any of the proceeds from the sale.

Loan modifications, including some of those performed under HAMP, could affect lien priority.[158] The law in this area, however, is not always clear.[159] In general, in the absence of a clause in the first lien reserving the right to modify, a modification performed between the first lien holder and the borrower could jeopardize the lien priority of the first lien holder.[160] The usual standard to determine whether lien priority remains intact is if a modification materially prejudices the second lien holder.[161] For instance, modifications that lower the interest rate or reduce principal are generally considered favorable to the second lien holder and should not affect

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Currency, et al. (July 30, 2009) (online at 192.147.69.84/regulations/laws/federal/2009/09c04AD42.PDF). In December 2009, the rule on risk based capital guidelines for liens modified under the program became effective not reflecting the banks' request on the treatment of second liens. U.S. Department of the Treasury, *Risk-Based Capital Guidelines; Capital Adequacy Guidelines; Capital Maintenance; Capital—Residential Mortgage Loans Modified Pursuant to the Home Affordable Mortgage Program,* 74 Fed. Reg. 60138–60140 (Nov. 20, 2009) (online at www.occ.gov/news-issuances/federal-register/74fr60137.pdf) ("the agencies have determined that allowing a banking organization to risk weight junior-lien mortgage loans at less than 100 percent is not appropriate other than in those circumstances already permitted by the agencies general risk-based capital rules"). The first servicer signed up for the program in January 2010. April 2010 Oversight Report, *supra* note 1, at 14–15. In March 2010, Treasury issued new guidelines for the second lien program. U.S. Department of the Treasury, *Making Home Affordable Program—Update to the Second Lien Modification Program (2MP),* Supplemental Directive 09–05 Revised (Mar. 26, 2010) (online at www.hmpadmin.com/portal/programs/docs/second_lien/sd0905r.pdf). To date, there is limited data to report for the second lien programs as Ms. Caldwell indicated, "we don't have data to report yet, as the program really got started at the beginning of October [2010]." Transcript Testimony of Phyllis Caldwell, *supra* note 108. Treasury expects to have more complete data and the programs in early March 2011. Treasury conversations with Panel staff (Nov. 23, 2010). As of September 30, 2010, 19 first lien servicers representing 60 percent of the second liens are participating in the program, and information supplied to SIGTARP on October 15, 2010 indicates that only 21 permanent modifications have been performed under the program. SIGTARP Quarterly Report to Congress, *supra* note 25, at 67, 69.

[157] It is possible that a home could have more than two liens; however, as most homes only have two liens, in this section second liens are often used as a proxy for all subordinated liens and the analysis with respect to second liens holders can often by extrapolated to apply to other subsequent lien holders.

[158] "HAMP does not require extinguishment of subordinate lien instruments as a condition of modification. However, servicers must follow investor guidance to ensure first lien priority." U.S. Department of the Treasury, *Making Home Affordable Program: Handbook for Servicers of Non-GSE Mortgages–Version 3.0,* at 42 (Dec. 2, 2010) (online at www.hmpadmin.com/portal/programs/docs/hamp_servicer/mhahandbook_30.pdf) (hereinafter "MHA Handbook for Servicers of Non-GSE Mortgages"); House Oversight and Government Reform, Subcommittee on Domestic Policy, Written Testimony of David Berenbaum, chief program officer, National Community Reinvestment Coalition, *Foreclosures Continue: What Needs to Change in the Administration's Response?,* at 21 (Feb. 25, 2010) (online at oversight.house.gov/images/stories/Hearings/Domestic_Policy/2010/022510_Foreclosure/022310_DP_David_Berenbaum_022510.pdf).

[159] Furthermore, real estate law is state specific and states differ in their approaches to determinations of lien priority.

[160] In general, the first lien holder retains the priority to any subsequent modification if the modification is not materially prejudicial to the second lien holder or there is a clause in the contract that allows for a modification. However, there is a limited case law and scholarship is mixed on the enforceability of this clause. An example of such a provision would read, "This mortgage shall also secure all extensions, amendments, modifications, or alterations of the secured obligation including amendments, modifications, or alterations that increase the amount of the secured obligation or the interest rate on the secured obligation." Restatement (Third) of Prop. (Mortgages) § 7.3 (1997).

[161] The determination of what is considered materially prejudicial is generally a question of fact to be determined by the court and court decisions in this area vary. Restatement (Third) of Prop. (Mortgages) § 7.3 (1997).

lien priority, while modifications that increase principal can prejudice the second lien holder and might affect lien priority.[162] Furthermore, it is possible that a court would only subordinate (rank lower in lien priority) the additional amounts due to the modification.[163] However, though a more drastic remedy, courts have on occasion elevated the second lien before the entire first lien in priority.[164]

While the HAMP modifications are geared to making the first liens more affordable and do utilize tools such as interest and principal reductions (which can be viewed as favorable to the second lien holder), the vast majority of active HAMP modifications have a higher principal balance after the modification than before the modification.[165] Though this increase in principal balance is mostly due to capitalization of arrearages and escrow requirements, it is unclear how courts would treat this principal increase.[166] Even if courts were to decide that HAMP modifications do not change or even partially affect the lien priority, this legal murkiness could complicate or at least extend the foreclosure process. Therefore, in order to assure the first lien holder their position of seniority, it is more prudent to have that lien holder reach an agreement with the subsequent lien holders.[167]

In addition, there are reasons of equity why having an agreement with the second lien holder, especially an agreement that also modifies or extinguishes the second lien, is important to the modification process. Unless the second lien is modified or extinguished, many of the concessions the first lien holder makes to help the borrower could disproportionately accrue to the benefit of the second

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[162] There is mixed case law on modifications that extend the length of the first lien. In general, this type of modification aids in affordability and can be considered favorable to the second lien holder; however, there is legal precedent where loan priority is shifted due to this type of modification. Restatement (Third) of Prop. (Mortgages) § 7.3 (1997) ("Absent an increase in the interest rate or principal amount of the mortgage obligation, courts routinely hold that such modifications do not defeat the mortgagee's priority as against intervening lienors. The assumption is that such transactions reduce the likelihood of foreclosure of the senior mortgage and that they are therefore beneficial to the interests of junior lienors. *See, e.g., Crutchfield v. Johnson & Latimer,* 8 So.2d 412 (Ala. 1942); *Lennar Northeast Partners v. Buice,* 57 Cal.Rptr.2d 435 (Cal.Ct. App.1996); *Eurovest Ltd. v. 13290 Biscayne Island Terrace Corp.,* 559 So.2d 1198 (Fla.Dist.Ct.App.1990); *State Life Insurance Co. v. Freeman,* 31 N.E.2d 375 (Ill.Ct.App.1941); *Guleserian v. Fields,* 218 N.E.2d 397 (Mass.1966); *Shultis v. Woodstock Land Dev. Assoc.,* 594 N.Y.S.2d 890 (N.Y.App.Div.1993); *Skaneateles Savings Bank v. Herold,* 376 N.Y.S.2d 286 (N.Y.App.Div.1975), aff'd, 359 N.E.2d 701 (N.Y. 1976); *Resolution Trust Corp. v. BVS Development, Inc.,* 42 F.3d 1206 (9th Cir.1994); *In re Fowler,* 83 B.R. 39 (Bankr.Mont. 1987); *In re Earl,* 147 B.R. 60 (Bankr. N.D.N.Y.1992); Kratovil & Werner, *Mortgage Extensions and Modification,* 8 Creighton L. Rev. 595, 607 (1975); 1 G. Nelson & D. Whitman, *Real Estate Finance Law,* § 9.4 (3d ed. 1993). *Contra Citizens and Southern National Bank v. Smith,* 284 S.E.2d 770 (S.C.1981) (extension of senior mortgage results in loss of its priority as against intervening lienor).

[163] For instance, a homeowner borrows $100,000 from Lender A to buy a property, Blackacre, and uses Blackacre as collateral against the note. Then the homeowner borrows $20,000 from Lender B, again using Blackacre as collateral. Both liens are properly recorded in a timely fashion and in accordance with local laws and there is no clause reserving the right to modify in the agreement with Lender A. Subsequently, the homeowner and Lender A modify their agreement in a way which has the effect of increasing the total principal outstanding to $110,000. If a court decides on an equitable solution, it might decide that from the proceeds of a foreclosure sale the ranking would be such that Lender A is entitled to $100,000, then Lender B $20,000 and thirdly, Lender A would be entitled to the additional amount due to the modification, $10,000. Restatement (Third) of Prop. (Mortgages) § 7.3 (1997).

[164] Using the example describe above in footnote 163, if a court decides to elevate the second lien over the first lien, then Lender B would be entitled to his entire $20,000 before Lender A would get paid back any of the $110,000 that homeowner still owes him. Restatement (Third) of Prop. (Mortgages) § 7.3 (1997).

[165] See Section D.3.b, *supra,* for a discussion on the increase of principal balance.

[166] Restatement (Third) of Prop. (Mortgages) § 7.3 (1997).

[167] April 2010 Oversight Report, *supra* note 1, at 13–16; Restatement (Third) of Prop. (Mortgages) § 7.3 (1997).

lien holder.[168] Therefore, for these legal and financial reasons, second lien holders can act as a hold out and make modification more difficult.

Similar to first liens, losses on modified second liens generally need to be recognized sooner than losses on loans that have not been modified. In general, if a second lien is modified, the loss requires immediate recognition.[169] However, despite the fact that many such liens may not have any recoverable value at current home prices, many second lien holders currently carry these liens at improbably high accounting values for various reasons, including that they are optimistic that home prices will recover shortly, they believe they can extract some value from the first lien holder, many of the second liens are actually current, or because not doing so would damage their capital position.[170] Therefore, recognizing these losses could have significant economic costs, including that it might require the second lien holder to raise additional capital or increase other reserves.[171] Treasury has indicated that it does not require second lien write-downs and is "indifferent to it in the [. . .] first lien program." [172]

As the vast majority of second liens are not securitized and are held directly by banks and other financial institutions, a write-down of second lien portfolios under a modification program could cause substantial accounting losses and thereby impact the solvency of some banks. In fact, the largest four banks—JPMorgan Chase, Bank of America, Citigroup, and Wells Fargo—hold 43 percent or $420.0 billion of all U.S. revolving and second liens ($975.3 billion).[173] To give a sense of the magnitude, the value of the second liens held by these banks is roughly comparable to just under 80 percent of the amount of their Tier 1 capital, the principal measure used by regulators to determine the adequate capitalization of a bank. Specifically, at the end of the third quarter 2010, the four largest banks reported $420.0 billion in second lien mortgages while having total Tier 1 capital of $535.2 billion.[174] In the

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[168] April 2010 Oversight Report, *supra* note 1, at 13–14.

[169] See Section G.2.b, *supra,* for a more in-depth discussion of accounting issues.

[170] Second liens are current in many cases where first liens are in default. This could be for a variety of reasons, including that second liens tend to have lower payments, and that since many of them are home equity lines of credit, the borrowers want to keep those lines of credit open for future needs. In addition, second liens tend not to be securitized. Therefore, the servicing bank is also the investor and might be more aggressive in collecting payments. Furthermore, many of the second liens are home equity lines of credit and could be technically current even if the lien holder is not being paid, as the unpaid interest can simply be rolled into the balance due. April 2010 Oversight Report, *supra* note 1, at 119–120; Amherst Mortgage Insight: Second Liens, *supra* note 154, at 11–12. *See also* Section G.2.b, *supra.*

[171] April 2010 Oversight Report, *supra* note 1, at 15–16.

[172] Transcript Testimony of Phyllis Caldwell, *supra* note 108. According to Treasury, borrower qualification for HAMP is based on first lien affordability. Treasury conversations with Panel staff (Oct. 21, 2010).

[173] In terms of market size, the first lien market is roughly 10 times the size of the second lien market. However, since almost all second liens are not securitized, the exposure that banks have with respect to second liens tends to be disproportionately larger than their exposure from first liens. For instance, at the end of the third quarter, the largest four banks hold $420.0 billion in second liens, while holding $793.1 billion in first liens. Board of Governors of the Federal Reserve System, *Flow of Funds Accounts of the United States,* at 96 (Sept. 30, 2010) (online at www.federalreserve.gov/RELEASES/z1/Current/z1.pdf) (hereinafter "Federal Reserve—Flow of Funds Accounts of the United States"); Data provided by Federal Reserve staff (Dec. 1, 2010); Data on first and second lien holdings of the four largest banks accessed through SNL Financial data service (Dec. 9, 2010).

[174] The Tier 1 Capital amount is based on reporting by the banks, not their holding companies, and therefore may not include all second liens held by affiliates. Data accessed through SNL Financial data service (Dec. 9, 2010).

case of Wells Fargo, their second lien exposure actually exceeds the amount of their Tier 1 capital.

Figure 13 shows that these banks are some of the largest investors in second lien mortgages, and Figure 14 details their second lien exposure as compared to their Tier 1 capital.

FIGURE 13: OWNERSHIP OF SECOND-LIEN MORTGAGES BY INSTITUTION TYPE, AS OF Q3 2010[175]

[Dollars in billions]

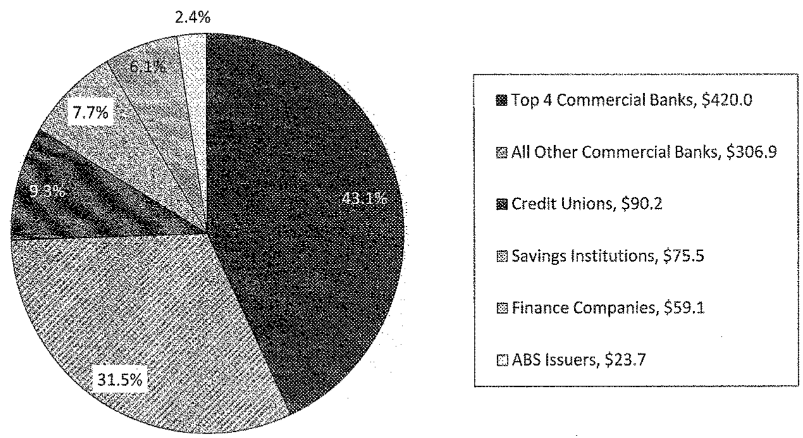

FIGURE 14: SECOND LIENS COMPARED TO TIER 1 CAPITAL AS OF THE THIRD QUARTER OF 2010[176]

[Dollars in billions]

Company	Second Liens	Tier 1 Capital	Second Liens as a Percent of Tier 1 Capital
Bank of America Corporation	$137.4	$164.8	83
JPMorgan Chase & Co	108.6	139.4	78
Citigroup Inc	52.0	125.4	41
Wells Fargo & Company	122.0	105.6	116
Total Top 4	**$420.0**	**$535.2**	**78**

[176] Data accessed through SNL Financial data service (Dec. 9, 2010).

In addition, the four largest commercial banks, Bank of America, Citigroup, JPMorgan Chase, and Wells Fargo, are both servicers of first and second liens as well as owners of large second lien portfolios. Therefore, this potential for a significant write-down of second lien mortgages creates a profound conflict of interest for these entities, putting their financial well-being at odds with their duties as first lien servicers.[177]

[175] Federal Reserve—Flow of Funds Accounts of the United States, *supra* note 173 at 96; Data on second lien holdings of the four largest banks accessed through SNL Financial data service (Dec. 9, 2010).

[177] For instance, Bank of America and Chase have indicated that for first liens that they service, they own 15 percent and 10 percent, respectively, of the related second liens. House Committee on Financial Services, Written Testimony of Barbara Desoer, president, Bank of America Home Loans, *Second Liens and Other Barriers to Principal Reduction as an Effective Foreclosure*

Continued

Finally, the salient objective of HAMP is to make homes more affordable. Statistically, having a second lien decreases the likelihood that the property is affordable.[178] If a homeowner has two liens, even if that homeowner is granted a modification on the first lien, the homeowner might still not have the funds to make his or her mortgage payments, as the modified first lien payment combined with the cost of the second lien might still be beyond the homeowner's reach.[179] The existence of multiple liens also increases the likelihood that there is negative equity in the home and makes it more likely that the homeowner will default.[180]

Though the administration's two announced second lien programs—2MP and the second-lien portion of the FHA Short Refinance Program—are structured to better align the interests of the first and second lien holders in order to increase the likelihood that a borrower's modification will be successful, it is unclear that all of the impediments caused by second liens have been adequately addressed.

d. Misaligned Incentives

Mortgage servicers, often divisions of large banks, are responsible for collecting payments from borrowers on behalf of the investors who own the loans. These servicers play a key decision-making role on HAMP modifications—they are the firms that have entered into contracts with Treasury to make modifications under HAMP—but they have different financial incentives than the investors who own the loans. Hence, as the Panel described in its April 2010 report, HAMP may be faltering because of a principal-agent problem. The servicers are interested in maximizing their revenue from each loan while minimizing their expenses.[181] Servicers typically incur most of their costs on the front-end when "boarding" the loans into their systems. Since they make money from servicing on an ongoing basis it is in their interest to keep servicing loans that are current. However, once a loan is on the verge of becoming delinquent or defaults, servicers' incentives change: because the costs associated with servicing a delinquent loan often exceed the revenues that a servicer can generate from the same loan, it may be in the servicer's interest to move to foreclosure as soon as possible.[182] Consequently, the servicer's financial interests may be at

Mitigation Program, at 6 (Apr. 13, 2010) (online at financialservices.house.gov/media/file/hearings/111/desoer.pdf); House Committee on Financial Services, Written Testimony of David Lowman, chief executive officer, JPMorgan Chase Home Lending, *Second Liens and Other Barriers to Principal Reduction as an Effective Foreclosure Mitigation Program,* at 5 (Apr. 13, 2010) (online at financialservices.house.gov/media/file/hearings/111/jpmc_lowman_4.13.10.pdf).

[178] The likelihood that properties financed through multiple liens have aggregate mortgage payments greater than 30 percent of income is nearly 22 percent, as compared to an only 2.2 percent likelihood for properties with only one lien against the property. David Bernstein, *A Presentation: Seconds First: The Role of Second Liens in the Mortgage Crisis and Rescue,* at 7 (Nov. 10, 2008) (online at ssrn.com/abstract=1299144).

[179] Second liens, as additional borrower debt, contribute to back-end DTI. See Section D.3.a., discussing how borrower debt affects the affordability and sustainability of a modification.

[180] Amherst Mortgage Insight: Second Liens, *supra* note 154, at 5.

[181] April 2010 Oversight Report, *supra* note 1, at 71–74.

[182] *See* October 2009 Oversight Report, *supra* note 15, at 71–74. *See also* SIGTARP Quarterly Report to Congress, *supra* note 25, at 162 ("Typically, if a borrower's payments are not made promptly and in full, servicers must advance to the investor the required amount of the monthly payment owed by the borrower, although in some circumstances servicers are required to advance only the unpaid interest. . . . As more loans in a servicer's portfolio become delinquent, these advance payments can strain servicers' cash supplies or their lines of credit. Servicers thus have incentives to pursue aggressive collection techniques to "cure" a loan and return it to a performing status or to place the property into foreclosure, which may enable them to re-

odds with the interests of the loan investors, who will generally receive far less from a foreclosure than they will from a modification. The picture is even more complicated when the mortgages have been securitized, because the holders of the senior tranches of mortgage-backed securities tend to benefit from more rapid foreclosures, while the holders of the junior tranches benefit from a more drawn-out foreclosure process.[183] This misalignment of incentives and the disputes that can result from it are sometimes called "tranche warfare."[184] The complexity and opacity of the situation combined with the lack of accountability—where it is not clear whose interests the servicers are serving—appear to be undermining HAMP's effectiveness.

e. Pooling and Servicing Agreements

The contracts between the investors in a mortgage and the mortgage's servicers are known as PSAs. In some cases, as the Panel has noted in its previous reports, these agreements may be serving as contractual barriers to HAMP modifications.[185] While PSAs generally do not bar loan modifications, they typically restrict the ability of servicers to extend the term of the loan by more than one year, and they often make it difficult for servicers to reduce the loan principal as part of a modification.[186] These contractual restrictions may be hindering the ability of servicers to qualify borrowers for HAMP, since term extensions are a key tool for reducing monthly payments to the level that the program requires.

f. Treasury's Base NPV Model

Treasury's base NPV model is in many ways the linchpin for HAMP. Treasury requires that participating servicers use the NPV test for all HAMP eligible loans that are in imminent default or are at least 60 days delinquent.[187] The NPV test is run before a home-

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cover their advances more quickly. . . . Servicers often borrow to fund these advances, and they incur interest expenses on that borrowing.").

[183] *See* Amherst Securities Group LP, *Amherst Mortgage Insight: The Affidavit Fiasco—Implications for Investors in Private Label Securities* (Oct. 12, 2010) ("In general, when liquidations are postponed, servicers generally continue to advance (*"as long as it is deemed recoverable"*). These advances are repaid to a servicer at liquidation, which increases the loss severity at liquidation. That helps the more junior bonds, which continue to receive interest payments for a longer period (they never expected to receive principal, anyway). But postponement hurts the more senior bonds, as (1) they experience higher losses due to the higher severities and (2) the average life lengthens for their bonds, a negative for bonds purchased/carried at a discount.").

[184] Larry Cordell et al., *The Incentives of Mortgage Servicers and Designing Loan Modifications to Address the Mortgage Crisis,* at 233–234, in LESSONS FROM THE FINANCIAL CRISIS: CAUSES, CONSEQUENCES, AND OUR ECONOMIC FUTURE (Robert W. Kolb ed., 2010).

[185] March 2009 Oversight Report, *supra* note 10, at 42–44; October 2009 Oversight Report, *supra* note 15, at 28–29; April 2010 Oversight Report, *supra* note 1, at 72. *But see* John P. Hunt, *What Do Subprime Securitization Contracts Actually Say About Loan Modification? Preliminary Results and Implications,* at 8 (Mar. 25, 2009) (online at www.law.berkeley.edu/files/Subprime_Securitization_Contracts_3.25.09.pdf) ("The most common rules are that the servicer must follow generally applicable servicing standards, service the loans in the interest of the certificateholders and/or the trust, and service the loans as it would service loans held for its own portfolio. Notably, these conditions taken together can be read as attempting to cause the loan to be serviced as they would have been if they had not been securitized.").

[186] April 2010 Oversight Report, *supra* note 1, at 72.

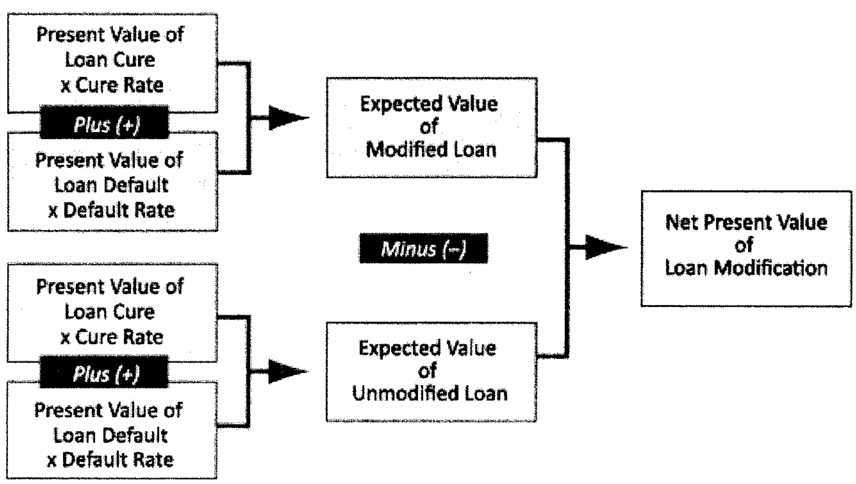
[187] The determination of delinquency is based on the Mortgage Bankers Association delinquency calculation; however, the determination for imminent default for non-GSE mortgages is left to the servicer with very little guidance from Treasury. MHA Handbook for Servicers of Non-GSE Mortgages, *supra* note 158, at 58, 73 ("All loans that meet HAMP eligibility criteria and are either deemed to be in imminent default or delinquent as to two or more payments must be evaluated using a standardized NPV test."); U.S. Department of the Treasury, *Home Affordable Modification Program: Base Net Present Value (NPV) Model Specifications,* at 3 (June 11,

Continued

owner is offered a trial modification.[188] The base NPV model computes the difference between the expected values of those loans under unmodified and modified scenarios. This is the gateway into HAMP. As long as agreed to by the investor,[189] a servicer must offer a HAMP modification when an NPV evaluation yields a positive value, meaning the total discounted value of expected cash flows is greater for the modified loan than the non-modified loan.[190] A loan modification is not required when the NPV is negative.[191]

To best conceptualize the NPV model, Treasury describes it as three discrete calculations, which are combined in the final stage.[192] The inputs of the program are used to generate (1) default rates (for both the modified and unmodified scenarios), (2) cure rates (for both the modified and unmodified scenarios), as well as (3) a cash flow equation.[193] All three results are then combined in the cash flow equation where the default and cure rates are used to predict the likelihood for various cash streams.[194] The following figure represents a simplified form of that equation.

FIGURE 15: NPV MODEL DIAGRAM [195]



2009) (online at www.hmpadmin.com/portal/programs/docs/hamp_servicer/npvoverview.pdf) (hereinafter "HAMP Base NPV Model Specifications"). Large servicers with at least $40 billion on their servicing books have the option of using the base NPV model or creating their own proprietary model. To date, no servicer has elected to customize the model and Treasury indicated that it would remove the new model as an option, if no servicer makes such an election by December. HAMP Base NPV Model v4.0: Model Documentation, *supra* note 27, at 41; Treasury conversations with Panel staff (Oct. 20, 2010).

[188] HAMP Base NPV Model v4.0: Model Documentation, *supra* note 27, at 3; MHA Handbook for Servicers of Non-GSE Mortgages, *supra* note 158, at 73.

[189] See Section G.2.e, *supra*.

[190] MHA Handbook for Servicers of Non-GSE Mortgages, *supra* note 158, at 73–74; HAMP Base NPV Model Specifications, *supra* note 187.

[191] MHA Handbook for Servicers of Non-GSE Mortgages, *supra* note 158, at 73–74.

[192] Treasury conversations with Panel staff (Oct. 20, 2010).

[193] The cure rate represents the likelihood that a borrower who was previously behind in his payments, makes up those missing payments.

[194] A more complete description of the base NPV model equations can be found online on the administrative web site for servicers for HAMP. HAMP Base NPV Model v4.0: Model Documentation, *supra* note 27, at 31–40 .

[195] HAMP Base NPV Model v4.0: Model Documentation, *supra* note 27, at 6.

In order to calculate the NPV, the model has several inputs and variables, including the government incentives.[196] Therefore, both borrowers with a positive NPV in the absence of the government incentives, as well as those who only have a positive NPV due to the addition of government incentives, can participate in HAMP.[197] Other variables in the NPV model are as follows:[198]

- Modification costs and incentives, including lower monthly mortgage payments, likelihood of a redefault, and likelihood that a loan will be paid off before its term expires;
- Property value relative to mortgage value;
- Likelihood of foreclosure; and
- Foreclosure costs, including legal expenses, property maintenance costs, and expenses involved in reselling property, and lost interest.[199]

The NPV model also has a significant amount of inputs. Post-modification principal and interest payments, loan terms, and principal amounts are included among the many inputs. Since many of the PSAs with investors limit the type of modification that can be offered on a loan, the NPV model needed to be flexible enough to account for the investor restrictions.[200] Furthermore, not all the inputs are used in the calculation as some are strictly for data collection purposes.[201]

Servicers are limited in their flexibility to tweak these inputs and variables; however, they can adjust the discount rate, the rate at which future cash flows are brought back to the present time, by adding a risk premium. For non-GSE loans, all servicers may add a risk premium of up to 250 basis points to the minimum discount rate set at Freddie Mac's Primary Mortgage Market Survey rate for 30-year fixed rate conforming loans.[202] The number of loans that will qualify for a HAMP modification will vary depending on the risk premium a servicer uses in its NPV calculations.[203] Higher risk premiums decrease the likelihood of a loan modifica-

[196] HAMP Base NPV Model v4.0: Model Documentation, *supra* note 27.

[197] HAMP Base NPV Model v4.0: Model Documentation, *supra* note 27, at 7–8.

[198] Some of these variables are fixed and others are updated in regular intervals depending on the availability of data. For instance, Treasury indicated that it updates some parameters such as home price projections and real estate owned (REO) discount rate on a quarterly basis. However, the redefault rates and cure rates are based on GSE analytics, and program portfolio data are updated on an as needed basis. Treasury conversations with Panel staff (Oct. 20, 2010).

[199] HAMP Base NPV Model Specifications, *supra* note 187, at 3; HAMP Base NPV Model v4.0: Model Documentation, *supra* note 27, at 36–37; Treasury conversations with Panel staff (Oct. 20, 2010). See Section G.2.c, *supra,* for a discussion of second liens, which are not captured in Treasury's base NPV model.

[200] See Section G.2.e, *supra,* for a further discussion on the limits on modifications placed by these agreements.

[201] This includes the Borrower's Total Monthly Obligation, an NPV input closely correlated to back-end debt. Treasury conversations with Panel staff (Oct. 20, 2010).

[202] For GSE loans, servicers are not permitted to add a premium. Servicers only have the flexibility to choose two risk premium rates, one which they must use for all loans in portfolio (loans owned by the servicers) and one that they need to apply to all private label loans (generally, loans that are owned by private label securitization trusts and not sponsored by any GSE). In addition, the specific risk premiums are considered to be proprietary and confidential by servicers and are not publicly disclosed. October 2009 Oversight Report, *supra* note 15, at 130; Treasury conversations with Panel staff (Oct. 20, 2010); Treasury conversations with Panel staff (Dec. 9, 2010).

[203] U.S. Government Accountability Office, *Troubled Asset Relief Program: Further Actions Needed to Fully and Equitably Implement Foreclosure Mitigation Programs,* at 19 (June 2010) (GAO–10–634) (online at www.gao.gov/new.items/d10634.pdf) (hereinafter "GAO Report on Foreclosure Mitigation Programs").

tion.[204] In the October 2009 Report, the Panel noted that for a baseline scenario "only a one basis point change in the risk premium is necessary to change the outcome of the test for the baseline loan from NPV positive to NPV negative."[205] This demonstrates how sensitive the NPV model is to changes in the risk premium.

Since the NPV model is complex, there are several factors that could affect the success of the model, including the design of the model, the implementation of the model, and the accuracy of the data input by the servicers into the model.[206]

The correct design of the model is critical. If the NPV model is calibrated correctly, it will get the correct homeowners into HAMP to prevent avoidable foreclosures. However, an incorrect calibration could either act as a means to delay inevitable foreclosures or grant subsidies to those who would otherwise cure and therefore do not need the extra help.[207] In response to servicer feedback as well as changes to HAMP, Treasury has recently released a new version of the NPV model. This new model, which is effective as of October 1, 2010, reflects the PRA initiative as well as updates to the default and prepayment models.[208]

The NPV model, similar to any financial model, can only be as accurate as its assumptions and inputs.[209] In creating the model, Treasury had to make decisions about what to incorporate, balancing better results with limitations on data. In the NPV model, among the items that Treasury did not incorporate were the impact of accounting rules and back-end debt (including second liens).[210] Furthermore, the economics captured in the NPV model are primarily those of the borrower and the investor, therefore the NPV model does not directly take into account servicer costs and incentives.[211] Therefore, it is likely that one reason for these incentives is to compensate the servicers for some of their costs in implementing the program.

The Panel previously examined Treasury's base NPV model in its October 2009 report. Among its recommendations was the need to increase transparency regarding the methodology of the model. Treasury has since released documents detailing model inputs, as-

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[204] Since the loan modifications push the cash stream further into the future, discount rates decrease the expected value of the modified loans more than the unmodified loans, thereby decreasing the possibility that the NPV will be a positive number. Treasury conversations with Panel staff (Oct. 20, 2010).

[205] October 2009 Oversight Report, *supra* note 15, at 130.

[206] SIGTARP is in the process of auditing the NPV model, including the implementation by servicers of the NPV model, Treasury efforts to ensure quality control, and the procedures that servicers follow to communicate the reasons for NPV test failure to the borrowers. SIGTARP Quarterly Report to Congress, *supra* note 25, at 31.

[207] These risks, the risk of delaying inevitable foreclosure (or redefault risk) and the cure risk, can significantly increase costs during renegotiation. In evaluating a modification, "[o]ne must take into account both the redefault *and* the self-cure risks." Manuel Adeline, Kristopher Gerardo, and Paul S. Willen, *Why Don't Lenders Renegotiate More Home Mortgages? Redefaults, Self-Cures, and Securitization,* Federal Reserve Bank of Boston Working Paper 09–4, at 7 (July 6, 2009) (online at www.bos.frb.org/economic/ppdp/2009/ppdp0904.pdf).

[208] HAMP Base NPV Model v4.0: Model Documentation, *supra* note 27, at 4–5.

[209] Many assumptions in the model, including the default, prepayment and cure rates, are based off of historic data. Treasury updates these assumptions when it is warranted with the data and when there is sufficient new information to create reliable models. Treasury conversations with Panel staff (Oct. 20, 2010); Treasury conversations with Panel staff (Nov. 15, 2010).

[210] HAMP Base NPV Model v4.0: Model Documentation, *supra* note 27, at 13–20; Treasury conversations with Panel staff (Oct. 20, 2010); Treasury conversations with Panel staff (Nov. 15, 2010).

[211] Treasury conversations with Panel staff (Dec. 3, 2010).

sumptions, and underlying equations for the expected cash flows and default probabilities. These documents have been updated to reflect the new version of the NPV model.[212]

A further issue concerning the performance of the model is the granularity of its inputs. The Panel's October 2009 report called for "incorporating more localized information when determining a mortgage loan's value." For example, home price projections used in the base model are constructed from state averages rather than values within specific communities or neighborhoods. Limited granularity within the model is a possible source of inaccurate NPV calculations, and by extension, wrongful denials for loan modifications.[213]

The implementation of the model is also a source of concern. A June 2010 GAO report noted that audits conducted by MHA Compliance (MHA–C) revealed that 15 of the largest 20 HAMP servicers were not in compliance with certain guidelines for implementation of the NPV model. Further, the report discussed inconsistencies with seven servicers that coded the NPV model on their internal systems rather than running the model through the Fannie Mae web portal. Those servicers were required to fix the coding on their in-house models and until that coding was fixed, "MHA–C required the servicers to refrain from denying permanent modifications because of negative NPV results unless these results were validated by the Treasury version of the NPV model housed on the Fannie Mae Web portal."[214] Failing to code the NPV model properly has likely led to inconsistent evaluations of similarly situated borrowers.[215]

Finally, the accuracy of the inputs is vital. Servicers are responsible for collecting the financial information from the borrower and inputting the data for the NPV tests. Treasury has taken steps to improve accuracy, including changing the guidelines to require that borrowers denied based on a negative NPV receive letters containing the 33 inputs used in the NPV model.[216] Beginning February 1, 2011, these denial letters will be required and borrowers will then have 30 days from the notice to correct the NPV inputs.[217] Moreover, as required by the Dodd-Frank Wall Street Reform and Consumer Protection Act, Treasury is in the process of establishing a web portal so that borrowers can perform their own NPV analysis.[218] Treasury indicated that it intends to launch this

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[212] HAMP Base NPV Model v4.0: Model Documentation, *supra* note 27.

[213] Congressional Oversight Panel, Written Testimony of Larry Litton, president and chief executive officer, Litton Loan Servicing, *Philadelphia Field Hearing on Mortgage Foreclosures,* at 3–4 (Sept. 24, 2009) (online at cop.senate.gov/documents/testimony-092409-litton.pdf).

[214] GAO Report on Foreclosure Mitigation Programs, *supra* note 203, at 20; Congressional Oversight Panel, Written Testimony of Paul Heran, program executive, Making Home Affordable—Compliance, Freddie Mac, *COP Hearing on Treasury's Use of Private Contractors,* at 5 (Sept. 22, 2010) (online at cop.senate.gov/documents/testimony-092210-heran.pdf) (hereinafter "Written Testimony of Paul Heran") ("[I]f a recoded NPV model is determined to provide unreliable results, a servicer may be required to validate results in the Treasury approved model until the recoded model's reliability can be substantiated.").

[215] GAO Report on Foreclosure Mitigation Programs, *supra* note 203, at 20.

[216] The new directive would be effective as of February 1, 2011. U.S. Department of the Treasury, *Making Home Affordable Program—Case Escalation Process/Dodd-Frank Act NPV Notices,* Supplemental Directive 10–15, at 2, 21–24 (Nov. 3, 2010) (online at www.hmpadmin.com/portal/programs/docs/hamp_servicer/sd1015.pdf) (hereinafter "Supplemental Directive 10–15").

[217] *Id.* at 2.

[218] Though the NPV model will be available to borrowers through a portal, it will only provide an "estimated outcome." There are many factors that a borrower may not have access to that

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portal in the spring of 2011.[219] Though, Treasury is still ultimately responsible for ensuring servicer compliance, as the Panel noted in October 2009, "[m]aking the model publicly available [will] facilitate negotiations and provide an important check against wrongful modification denials."[220]

g. Sustainability of HAMP Modifications

HAMP modifications make homeownership relatively more affordable by reducing borrowers' monthly debt burdens. The Panel has raised concerns, however, as to whether these modifications make homeownership sufficiently affordable to avoid foreclosure.[221]

Treasury has stated that its estimated redefault rate for HAMP permanent modifications is 40 percent over the five-year span for a permanent modification.[222] For the first year of a modification, the redefault rate has been significantly lower, although the Panel has previously expressed concerns that the redefault rate could be higher over the long term. For a full discussion of redefault rates, see Section I.[223] Although HAMP improves affordability, many borrowers' resources are severely constrained by debt other than monthly mortgage payments. The program does not consider the homeowner's back-end DTI ratio—the ratio of total monthly debt payments to monthly income—and as a result many borrowers with permanent modifications are still spending a large percentage of their income on housing and other debt.[224] After a HAMP modification, the median borrower is left paying 63 percent of pre-tax income towards debt.[225] This in turn implies after-tax DTI levels that could make modifications unsustainable.[226] With high levels of total debt, even a small disruption of income or increase in expenses could make repayment impossible for these borrowers. HAMP adopted DTI targets that may be inappropriately high for long-term sustainability of loans. The 31 percent DTI target is higher than the GSEs' own affordability guidelines, and arguably more important, the program does not have a back-end afford-

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will affect the outcome of the NPV model including information about mortgage insurance on the loan and restrictions on a loan modification due to PSAs with investors. Congressional Oversight Panel, Written Testimony of Phyllis Caldwell, chief of the Homeownership Preservation Office, U.S. Department of the Treasury, *COP Hearing on TARP Foreclosure Mitigation Programs,* at 11 (Oct. 27, 2010) (online at cop.senate.gov/documents/testimony-102710-caldwell.pdf) (hereinafter "Written Testimony of Phyllis Caldwell") ("As required by the Dodd-Frank Wall Street Reform and Consumer Protection Act, Treasury is preparing to establish a web portal that borrowers can access to run a NPV analysis using input data regarding their own mortgages, and to provide to borrowers who are turned down for a HAMP modification the input data used in evaluating the application."); Supplemental Directive 10–15, *supra* note 216, at 1 ("However, because a borrower using the Borrower NPV Calculator may not use exactly the same data used by the servicer, the Borrower NPV Calculator will only provide an estimated outcome."); Treasury conversations with Panel staff (Nov. 15, 2010).

[219] Supplemental Directive 10–15, *supra* note 216, at 1; Treasury conversations with Panel staff (Nov. 15, 2010).

[220] October 2009 Oversight Report, *supra* note 15, at 47.

[221] *See* April 2010 Oversight Report, *supra* note 1, at 4–5.

[222] Congressional Oversight Panel, Written Responses of Herbert M. Allison, Jr., assistant secretary for financial stability, U.S. Department of the Treasury, *COP Hearing with Assistant Treasury Secretary Herbert M. Allison, Jr.,* at 3 (Oct. 22, 2009) (online at cop.senate.gov/documents/testimony-102209-allison-qfr.pdf).

[223] April 2010 Oversight Report, *supra* note 1, at 60–62.

[224] U.S. Department of the Treasury, *Making Home Affordable Program: Handbook for Servicers of Non-GSE Mortgages—Version 3.0,* at 19 (Sept. 22, 2010) (online at www.hmpadmin.com/portal/programs/docs/hamp_servicer/mhahandbook_20.pdf) (hereinafter "MHA Handbook for Servicers of Non-GSE Mortgages").

[225] Data provided by Treasury.

[226] See Section D.3.a, *supra,* for after-tax DTI calculations.

ability target and results in back-end DTIs that are also widely regarded as too high. By comparison, as discussed above in more detail, to qualify for an FHA loan, a borrower typically needs to show a back-end DTI ratio of no more than 41 percent.[227] The inclusion of a specific and more demanding back-end DTI target in the NPV model would likely have meant either larger modification of the first lien loan or concessions from junior lienholders, raising the question of the treatment of second lien mortgages. As explained above, the inputs into the NPV model were designed to exclude back-end DTI as a factor because of difficulties involved in data collection.[228]

Moreover, interest rates and payments for borrowers who successfully complete a permanent modification can increase after the five-year modification period.[229] This calls into question whether these mortgages will be sustainable after the modification period expires. Even among borrowers who complete a five-year permanent modification, absent a dramatic recovery in housing prices, some will redefault when their payments increase at the end of the modification period. The phase-out of modification terms will be particularly problematic for those families still underwater on their properties. Unless housing prices recover to a significant degree or the economy rebounds notably, redefault rates may be higher than Treasury currently estimates.

The state of the broader economy will also have a significant influence on the redefault rate. Curtailment of income is the most common reason listed for hardship by borrowers requesting HAMP modifications, and borrowers who are unable to find sufficient work will inevitably redefault. Unemployment and underemployment are particularly problematic because loan modifications under HAMP require borrowers to stay in their homes for several years, which may prevent borrowers from moving to take advantage of better job opportunities.

The deep level of negative equity for many HAMP permanent modification recipients also makes the sustainability of these mortgages questionable in the absence of principal reductions. The median borrower in a HAMP permanent modification has a 125 percent LTV ratio, meaning the family is deeply underwater.[230] Even with affordable payments, deeply underwater borrowers may choose to strategically default or may be compelled to default in response to core life events, such as illness, changes in family circumstances, job loss or job opportunities.

h. Foreclosure Processing Problems

Charges of servicers' negligence, ranging from lost paperwork to improper claims of ownership, have plagued the government's housing rescue programs from nearly the beginning.[231] As the Panel discussed in its November 2010 report, some servicers' em-

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[227] See Section B.3.a, *supra.*

[228] See Section D.3.a, *supra,* for further discussion.

[229] Explaining the rationale underlying HAMP, Ms. Caldwell testified before the Panel "[t]he borrower's modified monthly payment would remain in place for five years, which Treasury expected would provide sufficient time for the housing market and the financial system to recover." Written Testimony of Phyllis Caldwell, *supra* note 218, at 4.

[230] Data provided by Treasury.

[231] *See* April 2010 Oversight Report, *supra* note 1, at 71.

ployees have admitted to approving foreclosures without properly verifying the accompanying documents or otherwise following proper procedure.[232]

For servicers, foreclosures carry significant costs leading up to the acquisition of a property's title. Many of the delinquency costs, including lost principal and interest payments and lost servicing fee income, are time-dependent costs that the servicer continues to accrue throughout the foreclosure.[233] Servicers are required to pay many of these funds in advance and often have to borrow money to cover these costs. In shortening the foreclosure processing period, the servicer not only pays less in delinquency costs out-of-pocket compared to a longer, and more thorough, processing period, but is also able to recoup its costs quicker and repay any amounts it has borrowed. Foreclosure processing irregularities may tilt servicers to initiate more foreclosures because pursuing this option becomes artificially cheaper, although the servicer should weigh all the relevant costs, including the cost to replace its guaranteed income from a mortgage under its management.[234] Servicers may also be lowering their overhead costs by forgoing the administrative costs of hiring additional resources to conduct more robust scrutiny on mortgage documents.

This difference in cost could also skew HAMP's NPV model. In determining whether to grant a modification to a borrower, a servicer uses HAMP's NPV model to compare the net present value of a modification versus that of a foreclosure.[235] In valuing the cost of a foreclosure, the NPV model requires inputs based on observed costs, i.e. costs calculated based on actual historical data. By cutting corners in the foreclosure process, servicers may have been able to lower artificially the cost of a foreclosure, in particular by reducing the time it would take to complete a foreclosure. A shorter foreclosure process would mean decreased costs and that in turn would tilt the model in favor of foreclosures. In such instances, servicers would have an incentive to lose paperwork or otherwise deny modifications that they would be compelled to make under the program standards. According to Treasury, it is not yet clear whether the foreclosure irregularities may have altered costs and thus NPV inputs to the point that it skewed the model toward foreclosure, however, it is carefully examining the data for such evidence and will take appropriate steps should it observe a data break point.[236]

i. Failure To Focus on Root Causes of Foreclosures

The Panel first expressed concerns that HAMP was not designed to address the root causes of the housing crisis in March 2009.[237] In subsequent reports the Panel has raised serious concerns about

[232] *See* November 2010 Oversight Report, *supra* note 79, at 10–12.

[233] The national average time between the first missed payment and the foreclosure sale is approximately one year. *See* Mortgage Bankers Association, *Lenders' Cost of Foreclosure,* at 3 (May 28, 2008) (online at www.nga.org/Files/pdf/0805FORECLOSUREMORTGAGE.PDF). *See also* Congressional Budget Office, *Policy Options for the Housing and Financial Markets,* at Chapter 3 (Apr. 2008) (online at www.cbo.gov/ftpdocs/90xx/doc9078/toc.htm).

[234] For a more detailed discussion on how servicer incentives could skew the process toward foreclosures, see Section G.2.d, *supra.*

[235] For a discussion of the NPV model, see Section G.2.f, *supra.*

[236] Treasury conversations with Panel staff (Oct. 17, 2010).

[237] March 2009 Oversight Report, *supra* note 10.

Treasury's efforts to address these problems, noting that HAMP has failed to address foreclosures caused by factors such as unemployment and negative equity.[238] Unemployment can undermine many loan modifications designed to prevent foreclosure, since these modifications generally are based on the assumption that the borrower will stay in place and make payments for several years, and it is very difficult for unemployed borrowers to pass HAMP's NPV test. Negative equity similarly leaves borrowers unable to respond to life events such as changes in family circumstances, job loss or job opportunities. Homeowners responding to life events often face the choice of either walking away from their mortgages or turning down a job opportunity. Those who choose to leave their homes depress nearby property values, while those who turn down job opportunities disrupt the labor market. In either case, the economic impact is negative.

As detailed in Section F, in response to the problem of foreclosures caused by unemployment, Treasury announced changes to HAMP that will provide temporary assistance to unemployed homeowners. Treasury also announced an FHA refinance option to address negative equity, which provides incentive payments and loss-sharing to encourage voluntary refinancing of underwater mortgages into FHA mortgages. Additionally, the HHF may offer assistance to unemployed or underwater borrowers in participating states.

While the Panel applauds Treasury's efforts to address unemployment and negative equity, it is unclear that these initiatives will make significant headway against the scope and scale of the problem. Julia Gordon, senior policy advisor for the Center for Responsible Lending, testified before the Panel that "over the next several years, the toxic combination of high unemployment and underwater loans could mean a stunning total of more than 13 million foreclosures."[239] As discussed above, these estimates are in line with those of the Federal Reserve.[240] The Panel also remains concerned about the timeliness of Treasury's response. Even if Treasury's programs succeed, their impact will not be felt until almost two years after the foreclosure mitigation initiative was first launched, perhaps proving to be too little, too late.

j. Manner in Which HAMP Rollout Happened

Since HAMP was announced in February 2009, Treasury has initiated half a dozen foreclosure mitigation programs and announced numerous changes to existing programs. The initial announcement was referenced but included little specificity about plans to modify second liens, to modify loans in geographic areas where home prices have fallen precipitously, and to encourage alternatives to foreclosure in cases where modifications are not possible.[241] In the

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[238] April 2010 Oversight Report, *supra* note 1.

[239] Congressional Oversight Panel, Testimony of Julia Gordon, senior policy counsel, Center for Responsible Lending, *Transcript: COP Hearing on TARP Foreclosure Mitigation Programs* (Oct. 27, 2010) (publication forthcoming) (online at cop.senate.gov/hearings/library/hearing-102710-foreclosure.cfm).

[240] See Section A, *supra*.

[241] U.S. Department of the Treasury, *Making Home Affordable Updated Detailed Program Description* (Mar. 4, 2009) (online at treasury.tpaq.treasury.gov/press/releases/reports/housing_fact_sheet.pdf).

months that followed, Treasury announced five additional MHA programs and released numerous supplemental directives or additional MHA program guidelines.[242] Among the changes introduced was an increase in incentive payments to lenders, servicers, and borrowers.[243]

Although Treasury should be commended for trying new approaches aimed at preventing foreclosures, loan servicers and borrower advocates continue to express confusion about the constant flux of new programs, new standards, new requirements, and continued changes to HAMP, that make implementation more complex.[244] The Panel has also expressed concern with Treasury's pattern of providing ever-greater incentives to servicers and lenders. This pattern may create an incentive for servicers and lenders to delay modifications in hopes that the government will offer a better deal in the future. The Panel raised many of these problems in its April 2010 report, and SIGTARP identified many of these issues in a March 2010 report examining root causes for HAMP's disappointing results.[245]

Additionally, HAMP could have done a much better job with borrower outreach. Servicer outreach is inherently problematic, as servicers generally first contact borrowers in a debt collector role. A government-run outreach campaign might have been more effective at ensuring the maximum reach for HAMP. In its March 2010 report, SIGTARP criticized Treasury for failing to engage in an effective educational and promotional campaign on HAMP. They note that a "lack of basic understanding about the program has sown confusion" and servicers have reported that many borrowers did not even understand that not everyone is eligible for a HAMP modification.[246] In addition, SIGTARP noted that a Treasury-run outreach effort would have provided the opportunity to educate the

[242] MHA Handbook for Servicers of Non-GSE Mortgages, *supra* note 224.

[243] MHA Program Enhancements to Offer More Help for Homeowners, *supra* note 147, at 2.

[244] Senate Committee on Banking, Housing, and Urban Affairs, Written Testimony of Barbara Desoer, president, Bank of America Home Loans, *Problems in Mortgage Servicing from Modification to Foreclosure,* at 3 (Nov. 16, 2010) (online at banking.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore_id=0a4db4b3-b131–4764–8247-c665b9978e44) ("For example, Treasury, investors, and other constituencies often change the requirements of their modification programs. HAMP alone has had nearly 100 major program changes in the past 20 months. Fannie and Freddie, as investors, have layered on additional requirements, conditions and restrictions for HAMP processing. When these changes occur, we and other servicers have to change our process, train our staff, and update technology."); Congressional Oversight Panel, Written Testimony of Julia Gordon, senior policy counsel, Center for Responsible Lending, *COP Hearing on TARP Foreclosure Mitigation Programs,* at 19–20 (Oct. 27, 2010) (online at cop.senate.gov/documents/testimony-102710-gordon.pdf) ("However, given the way HAMP was created and implemented, many of these problems are no surprise. First, the program repeatedly raised public expectations that were then dashed when programs were not already operational. This pattern began at the inception of the program, when HAMP was announced to the public well before its infrastructure was in place. Servicers were quickly overwhelmed by requests when they were not yet prepared to qualify people for the program, thereby causing many homeowners to be very disappointed early on. Despite this initial bad experience with a lag between public announcement and rollout, Treasury continued to make every subsequent program change the same way. Rather than inform the servicers and wait for them to be ready before informing the public, Treasury's routine was to release the broad outline of a new initiative or guideline change and then have an implementation date months away.").

[245] SIGTARP linked HAMP's disappointing results to undeveloped program rules at the time of the initiation, confusion resulting from continued guideline changes, the decision to permit servicers to start trial modifications without supporting documentation from borrowers, and limited marketing efforts by Treasury. SIGTARP Report—Factors Affecting Implementation of HAMP, *supra* note 103.

[246] SIGTARP Report—Factors Affecting Implementation of HAMP, *supra* note 103, at 28.

public about foreclosure rescue scams and the dangers of other types of fraud.

k. Flawed Program Structure

In designing HAMP, Treasury made key choices regarding the program structure leading to fundamental problems. First, the basic decision to run HAMP through Treasury was an initial misstep in the program. Treasury's expertise is in managing the U.S. government's debt and ensuring financial institution safety-and-soundness. Treasury had no prior experience running a program like HAMP, nor did it have experience with housing issues, with consumer programs, or with mortgage servicers. Treasury is also the government agency with the closest ties to financial institutions. It would have been appropriate to consider the costs and benefits of other agencies, including HUD, which may have greater experience in the relevant areas and are less focused on financial institutions. More directly applicable experience and distance from an interested set of program participants might have ensured better program design.

A second design flaw arises because HAMP relies on mortgage servicers as the program's interface with borrowers. As detailed above, there are a variety of conflicts of interest and misaligned incentives with mortgage servicers. These make the decision to permit servicers to be the point of borrower contact for HAMP modifications questionable. Alternatives would have been either creating a central borrower interface that would have intermediated between borrowers and servicers or putting HAMP modifications up for competitive bidding. The Panel notes that while it may have been difficult to put in place an entirely new system in a short amount of time and a central, government-operated interface would have greatly increased the program's administrative burden, such a system likely would have given Treasury or another agency much greater control and information about servicer and borrower behavior.

In addition, Treasury's decision to use Fannie Mae as its agent for HAMP program administration and Freddie Mac as its agent for program compliance set up barriers to success. Because of its own lack of housing policy expertise, Treasury contracted with the GSEs to serve as its agents for HAMP under no-bid contracts. Yet, the GSEs are highly conflicted because they hold the credit risk on most mortgages in the United States, and have their own operational concerns, raising the question of why Treasury decided to saddle the GSEs with oversight of HAMP.

Finally, HAMP tries to be both streamlined and individualized in its treatment of loans. The result is that it is neither sufficiently streamlined nor sufficiently individualized, and gains the virtues of neither.

Part Two: The Future of HAMP

Although HAMP will continue to make trial modifications until the end of 2012, the October 3, 2010 expiration of the TARP had important consequences for the program. Throughout much of 2009 and 2010, Treasury made changes to the program's structure in an effort to address different aspects of the foreclosure crisis. Because the TARP has now expired, programmatic changes to HAMP are no longer possible, and no additional TARP dollars can be allocated to HAMP, although the program can continue to spend previously obligated money. This does not mean, however, that the program will now run on auto-pilot, or that Treasury is helpless to affect its eventual impact on the foreclosure crisis.

In late 2010 and beyond, there are two main ways that Treasury can affect the program's ultimate success. In order to ensure that HAMP is as successful as possible over the long term, Treasury should pursue both avenues energetically. First, it should aggressively monitor Fannie Mae, which Treasury hired to administer HAMP, and Freddie Mac, which it hired to enforce compliance with the program's rules, and require these two contractors to ensure that HAMP servicers are living up to the obligations of their contracts with Treasury in order to provide the appropriate outcomes for borrowers. Servicers must be held accountable, for example, for failing to implement the HAMP NPV model properly. By ensuring efficient administration of the program and by requiring HAMP servicers to comply with the program's rules, Treasury can maximize the number of borrowers who will eventually benefit from a HAMP modification, given the existing program structure and constraints.

Second, Treasury should focus more strongly on minimizing redefaults within HAMP. Ultimately, a HAMP modification is only a positive outcome if it allows its beneficiary to keep his or her home, rather than simply delaying a foreclosure. Preliminary redefault rates for HAMP offer some reason for hope, but it is still too early to say whether redefault rates will be lower than expectations over the five-year term of the program. Data being collected by HAMP servicers can shed light on what borrower and loan characteristics are correlated with redefaults. Treasury should make aggressive use of these data to encourage modifications that are sustainable. For example, should Treasury find that redefaults are correlated with unemployment, it can focus on the existing initiative to assist unemployed borrowers. Similarly, a correlation with negative equity could be addressed through more focused use of the existing FHA Short Refinance program.

H. Treasury's Implementation of HAMP and Possible Improvements

To implement HAMP, Treasury has chosen to work primarily through two financial agents, the GSEs Fannie Mae and Freddie Mac. To date, there have been a number of problems, both between the GSEs and the servicers, and between the GSEs and Treasury. Despite working through agents, however, Treasury remains ultimately responsible for HAMP's execution. This section examines the structure that Treasury has constructed to implement HAMP and what steps Treasury should take to improve implementation of the program.

1. Role of Fannie Mae and Freddie Mac

a. Selection of Fannie Mae and Freddie Mac as Financial Agents

Fannie Mae and Freddie Mac are GSEs chartered by Congress with the mission of providing liquidity, stability, and affordability to the U.S. housing and mortgage markets. In 2008, Fannie Mae and Freddie Mac combined lost more than $108 billion. In response, the Federal Housing Finance Agency (FHFA) placed Fannie Mae and Freddie Mac into conservatorship on September 7, 2008, in order to preserve each company's assets and to restore them to sound and solvent condition. Since then, the GSEs' legal status has been unclear. The GSEs remain responsible for normal business operations and day-to-day management.[247] They are, however, effectively owned by the government; Treasury has guaranteed their debts and FHFA has all the powers of the management, board, and shareholders of the GSEs.[248] Thus, for example, FHFA installed new boards of directors and CEOs, but could not hire or fire regular employees. Congress has not yet determined what Fannie Mae and Freddie Mac's ultimate status will be and is considering a number of potential options.[249]

Treasury has explained its decision to select Fannie Mae and Freddie Mac as the financial agents responsible for HAMP by claiming that the GSEs were the only entities with the experience, resources, and mortgage industry contacts necessary to implement and administer the program quickly.[250] The FHFA also supported the GSEs' selection.[251] According to Deputy Assistant Secretary of Treasury Gary Grippo in testimony before the Panel, "[s]imply put, we made a determination that there were no other parties with the capabilities and infrastructure to operate a national mortgage modification program."[252] The Panel's October 2010 report questions Treasury's selection of the GSEs.[253] The GSEs both had to rely heavily on subcontractors to fulfill their responsibilities, and testimony from a Panel hearing suggested that Fannie Mae and

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[247] House Committee on Financial Services, Written Testimony of Edward J. DeMarco, acting director, Federal Housing Finance Agency, *Compensation in the Financial Industry—Government Perspectives,* at 6 (Feb. 25, 2010) (online at financialservices.house.gov/media/file/hearings/111/fhfa_acting_director_demarco_testimony_for_2–25–10.pdf).

[248] House Financial Services, Subcommittee on Capital Markets, Insurance, and Government-Sponsored Enterprises, Written Testimony of Edward J. DeMarco, acting director, Federal Housing Finance Agency, *The Future of Housing Finance: A Progress Update on the GSEs,* at 2 (Sept. 15, 2010) (online at financialservices.house.gov/Media/file/hearings/111/DeMarco091510.pdf).

[249] The Dodd-Frank Wall Street Reform and Consumer Protection Act requires Treasury to conduct a study and submit recommendations on ending the conservatorship of Fannie Mae and Freddie Mac no later than January 31, 2011. *Dodd-Frank Wall Street Reform and Consumer Protection Act,* Pub. L. No. 111–203, § 1074 (2010).

[250] Treasury conversations with Panel staff (Sept. 27, 2010). *See also* Congressional Oversight Panel, *October Oversight Report: Examining Treasury's Use of Financial Crisis Contracting Authority,* at 78–82 (Oct. 14, 2010) (online at cop.senate.gov/documents/cop-101410-report.pdf) (hereinafter "October 2010 Oversight Report").

[251] Treasury conversations with Panel staff (Oct. 7, 2010) (during which Mr. Grippo indicated that FHFA "was involved from the very beginning," provided its explicit authorization for Treasury's selection, and "always had firsthand knowledge of everything."); FHFA conversations with Panel staff (Oct. 8, 2010).

[252] Congressional Oversight Panel, Testimony of Gary Grippo, deputy assistant secretary for fiscal operations and policy, U.S. Department of the Treasury, *Transcript: COP Hearing on Treasury's Use of Private Contractors* (Sept. 22, 2010) (publication forthcoming) (online at cop.senate.gov/hearings/library/hearing-092210-contracting.cfm) (hereinafter "Transcript Testimony of Gary Grippo").

[253] October 2010 Oversight Report, *supra* note 250, at 78–82.

Freddie Mac's roles as financial agents were not simply extensions of their prior work.[254]

b. Role of Fannie Mae

Fannie Mae's principal responsibilities under its $127 million agreement include implementing HAMP guidelines and policies, serving as a point of contact for participating mortgage servicers and instructing them on how to modify loans, serving as paying agent to calculate subsidies and compensation consistent with program guidelines, and coordinating with Treasury and other parties toward achievement of the program's goals.[255]

In addition, Fannie Mae serves as the sole data collector and record keeper for executed loan modifications and program administration. Fannie Mae collects its data and records in its "IR2" database, and Treasury's Homeownership Preservation Office (HPO) periodically validates the accuracy of IR2's incentive payment data with the involvement of PricewaterhouseCoopers. The review tests three elements: (1) that all incentive payments were paid correctly; (2) that all the loans for which incentive payments were made meet HAMP eligibility requirements; and (3) that all of the IR2 data used is internally consistent. If the validation process reveals discrepancies, Treasury works with Fannie Mae to resolve them. In light of recent issues regarding misleading actions by servicers in potentially tens of thousands of foreclosure cases,[256] it is reasonable to raise concerns as to how accurate Fannie Mae's reporting and recordkeeping is in the context of HAMP, particularly as Fannie Mae officials have indicated that primary responsibility for data accuracy lies with the servicers and that the embedded data checks in IR2 check for completeness but not accuracy.[257]

In addition to these recent concerns about servicer data, servicers have long had problems with losing borrower documentation.[258]

[254] *See* Treasury conversations with Panel staff (Sept. 23, 2010); Written Testimony of Paul Heran, *supra* note 214, at 2.

[255] U.S. Department of the Treasury, *Financial Agency Agreement Between U.S. Department of the Treasury and Fannie Mae,* at Exhibit A (Feb. 18, 2009) (Contract No. TOFA–09–FAA–0002) (online at www.financialstability.gov/docs/ContractsAgreements/Fannie%20Mae%20FAA%20021809%20.pdf) (hereinafter "Financial Agency Agreement Between Treasury and Fannie Mae").

[256] For example, servicers using "robo-signers" filed false affidavits in foreclosure cases across the country. For a more complete discussion of foreclosure and mortgage irregularities, *see* November 2010 Oversight Report, *supra* note 79.

[257] Treasury conversations with Panel staff (Oct. 4, 2010).

[258] *See, e.g.,* SIGTARP Report—Factors Affecting Implementation of HAMP, *supra* note 103, at 27; October 2009 Oversight Report, *supra* note 15, at 107; Congressional Oversight Panel, Written Testimony of Irwin Trauss, supervising attorney, Consumer Housing Unit, Philadelphia Legal Assistance, *Philadelphia Field Hearing on Mortgage Foreclosures* (Sept. 24, 2009) (online at cop.senate.gov/documents/testimony-092409-trauss.pdf) (hereinafter "Philadelphia Field Hearing on Mortgage Foreclosures"); Congressional Oversight Panel, Written Testimony of Deborah Goldberg, director, Hurricane Relief Project, National Fair Housing Alliance, *Philadelphia Field Hearing on Mortgage Foreclosures* (Sept. 24, 2009) (online at cop.senate.gov/documents/testimony-092409-goldberg.pdf) (hereinafter "Written Testimony of Deborah Goldberg"); Floyd Norris, *Are Banks Losing Lots of Documents?,* New York Times (Dec. 4, 2009) (online at norris.blogs.nytimes.com/2009/12/04/are-banks-losing-lots-of-documents/); Mary Kane, *White House, Loan Servicers Point Fingers as Foreclosure Plan Fails,* The Minnesota Independent (Jan. 4, 2010) (online at minnesotaindependent.com/52967/white-house-loan-servicers-point-fingers-as-foreclosure-plan-fails); Bendix Anderson, *Second Chance for Loan Modifications,* Housing Watch (Mar. 23, 2010) (online at www.housingwatch.com/2010/03/23/second-chance-for-loan-modifications/); Bendix Anderson, *HAMP Offers New Home for Borrowers,* Housing Watch (May 28, 2010) (online at www.housingwatch.com/2010/05/28/hamp-offers-new-hope-for-borrowers/); Stephanie Armour, *More Homeowners Get Help Outside of Federal Program,* USAToday (July 23, 2010) (online at www.usatoday.com/money/economy/housing/2010–07–23-mortgages23_CV_N.htm).

This persistent failing is of particular importance to Fannie Mae's administration of HAMP because incomplete documentation is a leading cause of canceled trial modifications.[259] To resolve this issue, the Panel has repeatedly recommended that Treasury and Fannie Mae develop a web portal to allow borrowers to submit and track modification applications, to deliver application documents to servicers, and to centralize information.[260] In September 2009, Treasury testified that it was working to build one,[261] but in March 2010, Treasury stated that it was still considering whether it should release a web portal at all.[262] Treasury has since decided not to develop its own web portal for three reasons:[263] (1) to the extent the portal would facilitate moving documents between the borrower and the servicers, Treasury could not guarantee that the documents would be complete; (2) the security concerns arising from storing so much personally identifiable information; and (3) the advent of an industry solution, discussed below, led Treasury to conclude that developing a Treasury web portal was not the best use of public money.

The Panel is pleased to note, however, that in November 2009, HOPE NOW, a coalition of mortgage companies, investors, counselors, and other mortgage market participants,[264] piloted the HOPE LoanPort web portal.[265] At present, the LoanPort is primarily a "counselor's portal." In order to use the LoanPort, borrowers first approach a participating housing counselor to modify a loan with a participating servicer. The counselor works with the borrower to build a loan modification application package, and then the counselor goes on the LoanPort. The LoanPort has certain required fields and mandatory documents that must be provided in order to submit the application. Once the counselor has entered all the required information,[266] the application package is delivered to the servicer. The servicer is then required to provide the counselor with updates on the status of the application every 10 days. The process from borrower approaching a housing counselor to the servicer reaching a decision on the application takes an average of 44 days (10 days for the housing counselor to complete the application package with the borrower and 34 days for the servicer to

[259] *See, e.g.,* MHA Servicer Performance Report, *supra* note 38, at 5. There were 196,835 trial modifications that did not convert to permanent modifications because of lack of documentation. Data provided by Treasury. Given the extensive anecdotal evidence noted above, in footnote 258, it is reasonable to believe that at least some of these conversions would not have been denied absent servicers losing borrower documentation.

[260] March 2009 Oversight Report, *supra* note 10, at 52; October 2009 Oversight Report, *supra* note 15, at 111; April 2010 Oversight Report, *supra* note 1, at 83.

[261] Congressional Oversight Panel, Written Testimony of Seth Wheeler, senior advisor, U.S. Department of the Treasury, *Philadelphia Field Hearing on Mortgage Foreclosures,* at 6 (Sept. 24, 2009) (online at cop.senate.gov/documents/testimony-092409-wheeler.pdf) (hereinafter "Written Testimony of Seth Wheeler").

[262] Treasury conversations with Panel staff (Mar. 24, 2010).

[263] The web portal referred to here should not be confused with the NPV web portal Treasury is required to develop by the Dodd-Frank Wall Street Reform and Consumer Protection Act. The web portal being discussed is not for NPV calculations, but to centralize borrower documentation and submit it to servicers.

[264] HOPE NOW Alliance, *About Us* (online at www.hopenow.com/hopenow-aboutus.php) (accessed Dec. 10, 2010).

[265] The HOPE LoanPort is now operated by its own non-profit group. The LoanPort completed its pilot phase in June 2010. Testimony of Faith Schwartz, *supra* note 78.

[266] Documents are date stamped as they are submitted, providing a record to minimize later documentation problems.

reach a decision).[267] There are currently 12 servicers,[268] and over 1,800 housing counselors from more than 420 organizations participating in the LoanPort.[269] As of November 19, 2010, counselors had started a total of 8,585 applications on the LoanPort. Of those, 3,320 were still being completed, and 4,784 had been finished and submitted to the servicers.[270] Though an important start, this annual volume of applications is a tiny fraction of the 672,439 HAMP trial modifications and the 929,148 proprietary modifications started last year.[271] Nor, unfortunately, is it significant in comparison to the 1,344,337 foreclosures initiated last year.[272]

HOPE LoanPort has also developed but not deployed a "borrower portal."[273] The borrower portal allows borrowers to interact directly with the LoanPort, uploading documents and information without working through housing counselors. The LoanPort would then ensure the applications were complete and verify the borrower's information. After this was finished, LoanPort would deliver the application package to the servicer. This borrower portal has not been deployed nationwide because of lack of funding. HOPE LoanPort estimates it would cost under $30 million.[274]

Going forward, HOPE LoanPort is trying to increase the number of borrowers using the system and to expand the number of participating housing counselor organizations to over 1,000 by June 2011. It is also working with state housing agencies to develop partnerships. In addition, it is seeking to attract funding to deploy the borrower portal nationwide. Further, the LoanPort is in conversations with the GSEs to engage the investor community and move them to push servicers to use the LoanPort. Though 12 servicers currently participate, they do not use the LoanPort as their primary point of entry for modification applications. Freddie Mac has expressed interest but Fannie Mae has been reluctant. Fannie Mae has also refused to allow HOPE LoanPort to adapt Fannie Mae's counselor software, Home Counselor Online, to the LoanPort system in order to avoid the need to enter application information on both systems.[275]

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[267] HOPE LoanPort conversations with Panel staff (Nov. 15, 2010).

[268] HOPE LoanPort conversations with Panel staff (Nov. 15, 2010). The servicers are: American Home Mortgage Servicing, Bank of America, Bayview Loan Servicing, Chase, Citi, GMAC, Ocwen Loan Servicing, OneWest Bank, PNC, Saxon, Sun Trust Mortgage, and Wells Fargo. HOPE NOW Alliance, *Partners* (online at www.hopenow.com/partners.php) (accessed Dec. 10, 2010). An additional three servicers, Nation Star, Met Life, and SPS Servicing, will be live on the LoanPort by the end of the year. HOPE LoanPort conversations with Panel staff (Nov. 19, 2010).

[269] HOPE LoanPort conversations with Panel staff (Nov. 15, 2010). An additional three servicers will be live on the LoanPort by the end of the year. The 1,800 housing counselors are located in 47 states. Before allowing a housing counselor access, HOPE LoanPort provides webinar trainings. HOPE LoanPort conversations with Panel staff (Nov. 15, 2010).

[270] The remaining 481 had a variety of dispositions. E-mail from Larry Gilmore, president and CEO, HOPE LoanPort to Panel staff (Nov. 19, 2010).

[271] Data provided by Treasury; MHA Servicer Performance Report, *supra* note 38, at 2 (year measured from November 2009 through October 2010); OCC/OTS Mortgage Metrics Report, Second Quarter 2010, *supra* note 31, at 2.

[272] OCC/OTS Mortgage Metrics Report, Second Quarter 2010, *supra* note 31, at 2.

[273] A variant of the borrower portal has been deployed in Arizona. In Arizona, a borrower submits information through the LoanPort. That information is then transferred to a housing counselor in the borrower's area, who will contact the borrower and work with them to complete and verify the application package. From then on, the counselor will use the standard counselor's portal. HOPE LoanPort conversations with Panel staff (Nov. 15, 2010).

[274] HOPE LoanPort conversations with Panel staff (Nov. 15, 2010).

[275] HOPE LoanPort conversations with Panel staff (Nov. 15, 2010).

Treasury is supportive of the new portal,[276] and was consulted during its development, but was not responsible for its creation.[277] It stays abreast of new developments with the LoanPort but has no input in how it is run.[278]

Though the LoanPort as it currently stands is an important step forward, only a few borrowers are currently using the system. Deploying the borrower portal is essential and should be completed as soon as possible. Allowing direct borrower access to the system will both increase the LoanPort's utilization and most effectively solve documentation problems. The Panel recommends that Treasury examine ways to facilitate the LoanPort's development in this direction, including exploring funding the LoanPort's borrower portal. Treasury should also work with HAMP servicers to encourage them to push the LoanPort as their primary point of entry for applications. In addition, Treasury should work with FHFA to determine why Fannie Mae has been reluctant to use the LoanPort and to overcome their resistance.

Fannie Mae has additional functions relating to servicer support and operates the HOPE Hotline. The hotline provides free housing assistance to borrowers and is the primary means for borrowers to escalate concerns about how a servicer handled their claim.[279] Treasury, however, has not explicitly informed borrowers that the hotline can be used to escalate complaints.[280] If borrowers assert that their modifications were wrongly denied, complaints are escalated to HUD-approved housing counselors at MHA Help. That counselor will set up a three-way call with the servicer and borrower to attempt to resolve the issue. If the counselor is unable to broker a solution, and further intervention is needed, the complaint can then be sent to the counseling agencies' management, which will consult with higher-level officials at the servicer level.[281] If the issue still cannot be resolved, the complaint will be escalated to the HAMP Solution Center at Fannie Mae.[282] Throughout this process, the housing counselors and Fannie Mae do not have independent authority to resolve a borrower's complaint. They rely on the servicer to make the ultimate decision as to whether the initial modification decision was wrong.[283] If a complaint has been escalated through to the HAMP Solution Center and alleges that the servicer did not follow HAMP guidelines, the complaint can be es-

[276] Transcript Testimony of Phyllis Caldwell, *supra* note 108.

[277] HOPE LoanPort, *About Hope LoanPort* (online at www.hopeloanportal.org/aboutloanport.php#) (accessed Dec. 10, 2010).

[278] Treasury conversations with Panel staff (Nov. 9, 2010).

[279] GAO Report on Foreclosure Mitigation Programs, *supra* note 203, at 23–26.

[280] GAO Report on Foreclosure Mitigation Programs, *supra* note 203, at 25–26. Treasury does inform borrowers through a number of channels that the hotline can be used for problems related to HAMP, but not that it can be used to escalate complaints. Treasury has explained this decision by stating that it wanted a single number for everything and that Treasury did not wish to confuse the market by identifying that number as a place to escalate complaints. Treasury conversations with Panel staff (Nov. 16, 2010).

[281] Treasury conversations with Panel staff (Nov. 16, 2010).

[282] GAO Report on Foreclosure Mitigation Programs, *supra* note 203.

[283] Treasury conversations with Panel staff (Nov. 16, 2010). On November 3, 2010, Treasury issued HAMP Supplemental Directive 10–15. The Directive requires servicers to have written procedures and sufficient personnel in place to provide timely responses to escalated complaints. The Directive further requires that, for large servicers, the personnel who review escalated cases must be independent from the servicer personnel who made the initial modification decision. It also compels improved communications between the borrower and servicer during the escalation process. The Directive will take effect on February 1, 2011. Supplemental Directive 10–15, *supra* note 216.

calated one more time, to the MHA Compliance Committee at Treasury, which *does* have authority to require the servicer to change a modification decision.[284] Since Fannie Mae began to report the information in June 2010, the number of complaints to the hotline, though small, has increased every month.[285]

c. Role of Freddie Mac

Treasury obligated $92 million to retain Freddie Mac to act as the HAMP compliance agent, responsible for ensuring that participating servicers satisfy their obligations under the HAMP SPAs.[286] Freddie Mac is required, among other tasks, to "conduct examinations and review servicer compliance with the published rules for the program and report results to the Treasury."[287]

Freddie Mac conducts periodic on-site examinations of servicers to evaluate readiness, governance, and implementation of HAMP requirements. In addition, Freddie Mac reviews the disbursements of incentive payments to servicers. Freddie Mac also performs periodic assessments of the use of the NPV model and an ongoing review of all servicers with recoded NPV models. Where issues are identified in these recoded models, servicers are asked to validate their results in the Treasury model.[288] If servicers' models do not meet Treasury's NPV specifications, Freddie Mac will require the servicers to discontinue use of their models and revert back to the NPV application available from Treasury through the MHA Servicer Portal.[289]

Freddie Mac is also authorized to conduct both unannounced and announced audits of servicers. It has chosen not to do any unannounced audits, stating that they are not practical because of the considerable coordination required to arrange a productive audit.[290] Freddie Mac, however, does conduct regularly scheduled announced audits of servicers. The frequency of these audits is determined by the size, risk, and volume of the servicer.[291] The ten largest servicers are subject to nearly continuous review and there are 42 servicers who have not yet been examined on any aspect of their performance. These 42 servicers are the smallest servicers and rep-

[284] Treasury conversations with Panel staff (Nov. 16, 2010).

[285] U.S. Department of the Treasury, *Making Home Affordable Program: Servicer Performance Report Through June 2010,* at 8 (Aug. 6, 2010) (online at www.financialstability.gov/docs/June%20MHA%20Public%20Revised%20080610.pdf); U.S. Department of the Treasury, *Making Home Affordable Program: Servicer Performance Report Through July 2010,* at 8 (Aug. 20, 2010) (online at www.financialstability.gov/docs/JulyMHAPublic2010.pdf); U.S. Department of the Treasury, *Making Home Affordable Program: Servicer Performance Report Through August 2010,* at 8 (Sept. 22, 2010) (online at www.financialstability.gov/docs/AugustMHAPublic2010.pdf) (hereinafter "Making Home Affordable Program: Servicer Performance Report Through August 2010"); U.S. Department of the Treasury, *Making Home Affordable Program: Servicer Performance Report Through September 2010,* at 9 (Oct. 25, 2010) (online at www.financialstability.gov/docs/Sept%20MHA%20Public%202010.pdf) (hereinafter "MHA Servicer Performance Report Through September 2010"); MHA Servicer Performance Report, *supra* note 38, at 8. In the most recent report, for October 2010, the complaint rate was at 5.7 percent.

[286] U.S. Department of the Treasury, *Financial Agency Agreement Between the U.S. Department of the Treasury and Freddie Mac,* at Exhibit A (Feb. 18, 2009) (Contract No. TOFA–09–FAA–0003) (online at www.financialstability.gov/docs/ContractsAgreements/Freddie%20Mac%20Financial%20Agency%20Agreement.pdf) (hereinafter "Financial Agency Agreement Between Treasury and Freddie Mac").

[287] *Id.* at Exhibit A.

[288] *Id.* at Exhibit A.

[289] TARP Two Year Retrospective, *supra* note 98, at 75.

[290] Treasury and Freddie Mac conversations with Panel staff (Sept. 27, 2010).

[291] The larger, riskier, and higher volume servicers are audited more frequently. Treasury and Freddie Mac conversations with Panel staff (Sept. 27, 2010).

resent a tiny fraction of the total volume of loans.[292] Freddie Mac stated that they will review these servicers at some point, but not necessarily within the first year. The schedule of reviews has been approved by Treasury.[293]

In cases of noncompliance, Freddie Mac may direct servicers to perform remediation activities in consultation with Treasury. For example, Freddie Mac may direct a servicer who failed to comply with its solicitation obligations to restrict foreclosure activities. It is Treasury's MHA Compliance Committee that can make decisions to impose financial remedies, which may include withholding or reducing incentive payments to servicers, requiring repayments of prior incentive payments made to servicers with respect to affected loans, or requiring additional servicer oversight.[294] Treasury, though, has eschewed levying penalties in favor of directing servicers to change their processes.[295] In some instances, though, this committee has ordered additional oversight, for example, requiring servicers to assess their solicitations' impact on borrowers.[296] Treasury also temporarily withheld incentive payments on approximately 1,400 loans until servicers resolved several data issues. After servicers complied, the payments that had been withheld were paid out, though there are still 132 loans with outstanding problems. For these 132 loans, Treasury is considering permanently withholding the incentive payments.[297]

In addition, Treasury asked Freddie Mac to develop a "second look" process to audit a sample of HAMP modification files in order to double-check the servicer's determination on the request.[298] Freddie Mac retrieves servicer source documents and loan files on a sample of their non-performing loans, as well as data from Fannie Mae's IR2 database of HAMP records. According to Treasury, individual borrowers whose files are being reviewed are not contacted in order to avoid added stress to borrowers. Freddie Mac then independently reviews the documents to ensure that it agrees with the decision the servicer reached on the modification.[299] If Freddie Mac disagrees with a decision, it can require further action, including requiring servicers to reevaluate loans that were not

[292] Congressional Oversight Panel, Written Responses of Phyllis Caldwell, chief of the Homeownership Preservation Office, U.S. Department of the Treasury, *COP Hearing on TARP Foreclosure Mitigation Programs,* at 1 (Oct. 27, 2010) (online at cop.senate.gov/documents/testimony-102710-caldwell-qfr.pdf).

[293] Treasury and Freddie Mac conversations with Panel staff (Sept. 27, 2010).

[294] TARP Two Year Retrospective, *supra* note 98, at 76.

[295] House Committee on Financial Services, *Transcript: Robo-Signing, Chain of Title, Loss Mitigation, and Other Issues in Mortgage Servicing* (Nov. 18, 2010) (publication forthcoming) (online at financialservices.house.gov/Hearings/hearingDetails.aspx?NewsID=1376). Treasury has stated that it may begin to use financial penalties more frequently as the programs mature. House Committee on Financial Services, Written Testimony of Phyllis Caldwell, chief of the Homeownership Preservation Office, U.S. Department of the Treasury, *Robo-signing, Chain of Title, Loss Mitigation, and Other Issues in Mortgage Servicing,* at 8–9 (Oct. 27, 2010) (financialservices.house.gov/Media/file/hearings/111/Caldwell111810.pdf).

[296] Treasury conversations with Panel staff (Oct. 21, 2010).

[297] Treasury conversations with Panel staff (Oct. 21, 2010).

[298] U.S. Department of the Treasury, *Making Home Affordable Program On Pace To Offer Help to Millions of Homeowners* (Aug. 4, 2009) (online at www.financialstability.gov/latest/tg252.html).

[299] Treasury conversations with Panel staff (Sept. 27, 2010). Second look reviews are frequently done on-site.

offered HAMP modifications,[300] to submit further documentation, to clarify a loan status, or to engage in process remediation, training, or policy clarification.[301]

Freddie Mac publicly releases some results from these second look reviews, including specific results for several servicers.[302] This disclosure, however, is limited. Freddie Mac only notes whether it disagreed with, could not yet determine, or agreed with a servicer's determination. This is not enough information for the public to evaluate the servicers effectively. For example, the public is unable to tell if Freddie Mac's determination that it disagrees with the servicer is the result of a technical difference or a gross violation. Furthermore, Freddie Mac has not focused follow-up reviews on the servicers with the worst records. Some servicers were reviewed twice, others once, but the servicers with the most questionable decisions in their first review were not those who were reviewed again.

More troublingly, recent statements raise questions about Freddie Mac's willingness to pursue servicers who violate program guidelines. In response to revelations that servicers have been using "robo-signers" to submit false affidavits in thousands of foreclosure cases, Freddie Mac noted that "we believe that our seller/servicers would be in violation of their servicing contracts with us to the extent that they improperly executed documents in foreclosure or bankruptcy proceedings."[303] Trying to enforce Freddie Mac contractual rights, however, "may negatively impact our relationships with these seller/servicers, some of which are among our largest sources of mortgage loans."[304] The Panel condemns this sentiment. If Freddie Mac is hesitant to jeopardize their relationships with servicers to enforce their rights in their own book of business, it is reasonable to worry that they may be similarly unwilling to risk these relationships on Treasury's behalf by aggressively overseeing HAMP servicers. It is important to note, though, that both Freddie Mac and Fannie Mae have threatened to penalize financially thousands of servicers if they did not fix their foreclosure practices,[305] and that FHFA is having the GSEs pursue re-

[300] If the home is in foreclosure when Freddie Mac requires the servicer to reevaluate the modification decision, the servicer must forestall the foreclosure sale. MHA Servicer Performance Report Through September 2010, *supra* note 285, at 1.

[301] MHA Servicer Performance Report Through September 2010, *supra* note 285, at 1.

[302] *See* U.S. Department of the Treasury, *Making Home Affordable Program: Servicer Performance Report Through May 2010,* at 6 (June 21, 2010) (online at www.financialstability.gov/docs/May%20MHA%20Public%20062110.pdf); MHA Servicer Performance Report Through September 2010, *supra* note 285, at 11.

[303] Federal Home Loan Mortgage Corporation, *Form 10–Q for the Quarterly Period Ended September 30, 2010,* at 190 (Nov. 3, 2010) (online at www.sec.gov/Archives/edgar/data/1026214/000102621410000053/f71398e10vq.htm) (hereinafter "Federal Home Loan Mortgage Corporation Form 10–Q").

[304] Federal Home Loan Mortgage Corporation Form 10–Q, *supra* note 303, at 190 ("While we believe that our seller/servicers would be in violation of their servicing contracts with us to the extent that they improperly executed documents in foreclosure or bankruptcy proceedings, as such contracts require that foreclosure proceedings be conducted in accordance with applicable law, it may be difficult, expensive, and time consuming for us to enforce our contractual rights. Our efforts to enforce our contractual rights may negatively impact our relationships with these seller/servicers, some of which are among our largest sources of mortgage loans.").

[305] American Bankers Association, *Fannie, Freddie Place Lenders on Notice in Foreclosure Debacle,* 2 Mortgage Lending Bulletin 15, at 5–6 (Oct. 21, 2010) (online at www.aba.com/NR/rdonlyres/A73585B8–6541–4A77–8184–1BEFB4AB2E60/69412/10222010MortgageLendingBulletin.pdf).

purchase requests from many of these same institutions.[306] Nevertheless, the potential conflict of interest raises concerns.

2. Current Oversight Mechanisms

Treasury has a comprehensive oversight structure in place to monitor Fannie Mae and Freddie Mac. Primary responsibility inside Treasury for overseeing the GSEs rests with the Office of Financial Agents (OFA), which monitors the GSEs in their role as financial agents. However, OFA has a collaborative relationship with three other offices inside Treasury's Office of Financial Stability (OFS): HPO, the Office of the Chief Financial Officer, and OFS–Compliance. HPO is particularly important in this collaboration as it is the program office and therefore makes the policy decisions on how HAMP is structured and implemented. In addition, Treasury has a Making Home Affordable program committee that meets weekly as well as several working committees (centered on compliance, budgeting, and governance issues) to oversee the GSEs. These committees meet on a regular basis and include interlocking membership from each of the different Treasury offices (referenced above) that are tasked with monitoring and oversight responsibilities for Fannie Mae and Freddie Mac.[307] Treasury's monitoring and supervision of the GSEs are also closely coordinated with general oversight and risk assessment by FHFA as part of the conservatorship process. Members of the FHFA conservatorship team continuously oversee Fannie Mae's and Freddie Mac's financial agency agreements, monitor the tasks that Treasury asks the GSEs to perform as a risk assessment measure, and help ensure that they are compensated appropriately for their work.[308]

Treasury uses several methods to evaluate and manage Fannie Mae's and Freddie Mac's performance and compliance with their financial agency agreements and the performance of their fiduciary obligation to Treasury. On the performance side, these include qualitative measures (such as assessments of cost containment, responsiveness, and nature of their business relationship with Treasury), and quantitative measures (such as how they process transactions, the timeliness and accuracy of their reports, and the number of servicer reviews conducted).[309] Treasury staff are also in frequent informal contact with GSE staff at many levels within each organization.[310]

On the compliance side, the GSEs are required to report to Treasury on internal controls, risk assessments, information technology security, employee training, and how they have revisited their conflicts of interest mitigation plans.[311] The financial agency

[306] Senate Committee on Banking, Housing, and Urban Affairs, Testimony of Edward DeMarco, acting director, Federal Housing Finance Agency, *Transcript: Problems in Mortgage Servicing From Modification to Foreclosure, Part II* (Dec. 1, 2010) (publication forthcoming) (online at banking.senate.gov/public/index.cfm?FuseAction=Hearings.LiveStream&Hearing__id=ea6d7672-f492-4b1f-be71-b0b658b48bef).

[307] Treasury and Fannie Mae conversations with Panel staff (Oct. 4, 2010).

[308] FHFA conversations with Panel staff (Oct. 4, 2010).

[309] Transcript Testimony of Gary Grippo, *supra* note 252.

[310] Treasury and Freddie Mac conversations with Panel staff (Sept. 27, 2010); Treasury and Fannie Mae conversations with Panel staff (Oct. 4, 2010).

[311] Financial Agency Agreement Between Treasury and Fannie Mae, *supra* note 255; Financial Agency Agreement Between Treasury and Freddie Mac, *supra* note 286.

agreements also require that Fannie Mae and Freddie Mac self-certify annually that they are complying with 11 selected terms of the agreements and review the effectiveness of their internal controls on an annual basis.[312] Also on an annual basis, Treasury staff conduct on-site visits to review the processes and controls of each agent at their offices.[313] Treasury also requires agents to submit information regarding conflicts of interest, which it reviews on an ongoing basis.[314]

3. Implementation Failures and Ways To Improve

Despite the intricate oversight mechanisms Treasury has developed to ensure the GSEs' performance, HAMP has suffered a number of implementation problems. First, there have been problems with the GSEs' oversight of the servicers. Secretary Geithner himself noted that "servicers have done a terrible job of making sure that they are doing everything they can to meet the needs of their customers . . . And they still have some distance to go to try to make up for that series of basic, how should I say it, mistakes, inadequacies, in performance."[315] Since this statement on June 22, 2010, servicers have made little progress. Of particular note are long-standing public complaints that servicers lose borrower documentation.[316] For example, the California Reinvestment Coalition surveyed more than 50 housing counselors from 40 different housing counseling agencies and found that 100 percent of the counselors said it was very common for servicers to request documents the counselors had already submitted.[317] A similar study by the National Counsel of La Raza found that 60 percent of counselors reported that servicers usually or always lost borrower documents.[318] Additionally, GAO reported in March 2010 that different servicers were applying different criteria in determining whether particular borrowers are at risk of imminent default, and therefore if they were eligible for HAMP, introducing inconsistencies into a standardized national program.[319] In June 2010, GAO found further servicer errors that created inconsistencies, including that 15

[312] Financial Agency Agreement Between Treasury and Fannie Mae, *supra* note 255, at § 16, Exhibit D; Financial Agency Agreement Between Treasury and Freddie Mac, *supra* note 286, at § 16, Exhibit D.

[313] Congressional Oversight Panel, Joint Written Testimony of Gary Grippo, deputy assistant secretary for fiscal operations and policy, and Ronald W. Backes, director of procurement services, U.S. Department of the Treasury, *COP Hearing on Treasury's Use of Private Contractors,* at 6 (Sept. 22, 2010) (online at cop.senate.gov/documents/testimony-092210-treasury.pdf).

[314] Treasury conversations with Panel staff (Sept. 16, 2010). For a more complete discussion of Treasury's monitoring of contractor and agent conflicts of interest, *see* October 2010 Oversight Report, *supra* note 250, at Sections B.3 & H.

[315] Congressional Oversight Panel, Testimony of Timothy Geithner, secretary, U.S. Department of the Treasury, *Transcript: COP Hearing With Treasury Secretary Timothy Geithner* (June 22, 2010) (publication forthcoming) (online at cop.senate.gov/hearings/library/hearing-062210-geithner.cfm).

[316] *See, e.g.,* October 2009 Oversight Report, *supra* note 15, at 107; Written Testimony of Deborah Goldberg, *supra* note 258; Written Testimony of Deborah Goldberg, *supra* note 258.

[317] Chasm Between Words and Deeds IV: HAMP Is Not Working, *supra* note 139, at 4.

[318] National Council of La Raza, *Saving Homes and Homeownership: Perspectives From Housing Counselors,* at 3 (Apr. 14, 2010) (online at www.nclr.org/index.php/publications/saving__homes__and__homeownership__perspectives__From__housing__counselors). Another survey, a random sample of 42 active cases conducted by a housing counselor organization, found that servicers had lost documentation in 28 percent of cases. E-mail from Cheyenne Martinez-Boyette, homeownership program lead, Mission Economic Development Agency, to Panel staff (Dec. 8, 2010).

[319] U.S. Government Accountability Office, *Troubled Asset Relief Program: Home Affordable Modification Program Continues To Face Implementation Challenges,* at 13–14 (Mar. 25, 2010) (GAO–10–556T) (online at www.gao.gov/new.items/d10556t.pdf).

of the largest 20 participating servicers did not comply with all program guidelines when implementing the NPV model.[320] And there is mounting evidence of widespread irregularities by servicers in foreclosure proceedings, including the use of "robo-signers." The failure of Fannie Mae and Freddie Mac to detect foreclosure irregularities by the servicers they hire as part of their own business raises questions as to their credibility in overseeing the servicers' adherence to HAMP standards.

There have also been several implementation failures on the part of the GSEs themselves. OFS initially had a number of concerns about Freddie Mac, including the use of unqualified staff to perform audits.[321] Treasury and Freddie Mac developed a detailed remediation plan, and Treasury has not reported any problems since.[322] In addition, in its October 2010 report, the Panel noted an instance when Fannie Mae publicly released a table with incorrect information. The error led Treasury to acknowledge that they lacked adequate controls with respect to the communication of program requirements and the validation of data.[323] Since then, Treasury has taken steps to improve its oversight, hiring MITRE Corporation to correct the table in question as well as to validate and improve Treasury's data production process for all HAMP reports. Though both GSEs have resolved these issues as they are identified, the fact that such significant errors were able to occur raises questions about how closely Treasury is overseeing the GSEs.

Notably, these problems are faults in implementation, not program design. Treasury must work to ensure that these sorts of errors do not continue to occur. These situations underscore the need to improve oversight of the GSEs, which will help prevent future problems and maximize HAMP's impact.

For example, OFA evaluates the GSEs on both qualitative measures (such as assessments of cost containment, responsiveness, and nature of their business relationship with Treasury), and quantitative measures (such as how they process transactions, the timeliness and accuracy of their reports, and the number of servicer reviews conducted).[324] These metrics are focused completely on the interaction between Treasury and the GSEs, not on how the servicers deal with borrowers. This incentivizes the GSEs to focus on developing intricate processes and not necessarily on ensuring that borrowers' needs are met. Treasury should instead adopt measures that track the end results Treasury wishes to see, such as the number of modifications a servicer is making as compared to its peers or the number of complaints a servicer receives. Treasury itself initially proposed several metrics, including "average borrower wait time in response to inquiries and response time for completed applications," but never adopted them.[325] Evaluating the

[320] GAO Report on Foreclosure Mitigation Programs, *supra* note 203, at 20–21.
[321] Office of the Special Inspector General for the Troubled Asset Relief Program, *Quarterly Report to Congress,* at 102 (Oct. 21, 2009) (online at www.sigtarp.gov/reports/congress/2009/October2009__Quarterly__Report__to__Congress.pdf).
[322] *Id.* at 102.
[323] Treasury conversations with Panel staff (Sept. 23, 2010).
[324] Transcript Testimony of Gary Grippo, *supra* note 252.
[325] Written Testimony of Seth Wheeler, *supra* note 261, at 6.

GSEs on the end results rather than on the processes they follow will encourage them to push servicers to do the same.

Another simple change Treasury could make is requiring Freddie Mac to call borrowers or their housing counselors during its Second Look reviews. At present, Freddie Mac looks at a servicer's source data and loan file, but does not call the borrowers to avoid adding to their stress. Calling borrowers or their counselors, however, is critical to assessing the accuracy of a servicer's determination. For example, without direct contact there is no way to validate that the servicer has all of the documentation the borrower sent. Establishing this fact is particularly important in light of the fact that servicers' losing documentation has been a consistent problem and that one of the most common causes of modifications being denied is missing documentation.

Similarly, Treasury should reform its process for escalating complaints. Despite having three different layers of review for complaints, it is the servicers themselves who ultimately choose whether to alter the borrower's modification decision.[326] The escalation process thus preserves servicers' discretion to decide on a modification, relying on them to determine if they made a mistake initially. Though the requirement in Supplemental Directive 10–15 that personnel who review escalated complaints in large servicers be independent from the staff that made the initial modification decision is a step in the right direction, it is not sufficient.[327] Treasury should remove the decision from the servicers' hands in favor of an independent and enforceable review. To maximize the HOPE Hotline's impact, moreover, Treasury should clearly inform borrowers that the hotline can be used to escalate complaints. For example, Treasury could easily post a notification to that effect on its Making Home Affordable Web site. In addition, Treasury should include the information in other communications with borrowers. The combination of these two changes would improve servicer accountability to borrowers, as it would provide borrowers a clear and independent pathway to challenge incorrect determinations. If Fannie Mae or Treasury were to track successful complaints, these changes would also allow Fannie Mae and Treasury to identify those servicers with the best, and the worst, decision-making records. By then rewarding or punishing them accordingly, servicers could be appropriately incentivized to focus on borrower outcomes.

Treasury should also make more prominent use of its available enforcement mechanisms against servicers. Treasury has emphasized the effectiveness of temporarily withholding incentive payments in resolving data issues with approximately 1,400 loans, but has only ever withheld incentive payments in that one instance.[328] It has not yet permanently stopped any incentive payments. As the Panel noted as early as October 2009, "[m]onitoring alone is ineffective unless accompanied by meaningful penalties for failure to comply."[329] Treasury should be more willing to use penalties to re-

[326] GAO Report on Foreclosure Mitigation Programs, *supra* note 203, at 25–26; Treasury conversations with Panel staff (Nov. 16, 2010).
[327] Supplemental Directive 10–15, *supra* note 216, at 3.
[328] Treasury conversations with Panel staff (Oct. 21, 2010).
[329] October 2009 Oversight Report, *supra* note 15, at 109.

solve long-standing problems, such as servicers losing borrower documentation.[330]

The Panel is pleased to note that Treasury has indicated that it will increase its public disclosure of particular servicers with problems.[331] Such "naming and shaming" can be an effective enforcement mechanism. Moreover, as the Panel noted in its October 2010 report, "[i]n order for compliance and enforcement to function as a deterrence mechanism and be exercised effectively, they must be sufficiently robust and transparent." Publicly noting problem servicers and their sanctions will help build a credible deterrent. Public exposure may also be the most effective enforcement mechanism for policing the GSEs. Monetary inducements are ineffective because Fannie Mae and Freddie Mac are performing their work at cost,[332] and even if Treasury were to fine one of the GSEs for failing to perform, this sanction would ultimately be paid by the taxpayers, not by the now almost non-existent GSE equity-holders.[333] Congress, however, is in the process of deciding on the GSEs' ultimate fate, so Fannie Mae and Freddie Mac may be sensitive to disclosures that would cast a negative light on their abilities. Treasury should regularly publish a detailed scorecard of the GSEs' performance, as well as disclose any particular problems or failures.

Alternatively, Treasury could work with FHFA to intervene more directly with Fannie Mae and Freddie Mac. FHFA can exercise the powers of the management and board of both the GSEs. These powers could be used to generate internal pressure to improve performance, even to the extent of holding senior officials individually responsible for poor outcomes.

I. Redefaults of Modified Mortgages

To ensure HAMP's success, Treasury should focus attention on trying to minimize redefaults of HAMP-modified loans. Redefaults, which occur when borrowers who have entered permanent modifications become delinquent on their loans, present a large potential pitfall for HAMP. This is in large part because every borrower who stops making monthly mortgage payments likely will not be able to keep his or her home in the long run. (There may be some benefit from the delay in foreclosures that results from failed modi-

[330] As noted in Section G.2.a, *supra,* the voluntary nature of the program generates the understandable concern that if servicers are penalized too much, they will simply leave the program. Treasury, however, raised the possibility that it may not be so easy for servicers to exit from HAMP. The SPAs do not contain any provision that allows servicer withdrawal. Treasury has not fully explored the ramifications of this absence, but did state that Treasury had discussed suing a servicer for specific performance if they attempted to withdraw unilaterally from the program. While Treasury may decide not to sue, or such a suit may not be successful, this possibility would complicate a servicer's exit. It may, therefore, create more space for Treasury to penalize servicers. Treasury conversations with Panel staff (Oct. 21, 2010).

[331] Treasury conversations with Panel staff (Oct. 21, 2010).

[332] *See* October 2010 Oversight Report, *supra* note 250, at 66.

[333] The original agreements with the GSEs included the possibility of incentive payments, but no incentive payments have been made, and Treasury has indicated that it has taken the incentive payment clause off the table indefinitely. Treasury conversations with Panel staff (Sept. 23, 2010). *See also* Congressional Oversight Panel, Testimony of Joy Cianci, senior vice president, Making Home Affordable Program, Fannie Mae, *Transcript: COP Hearing on Treasury's Use of Private Contractors* (Sept. 22, 2010) (publication forthcoming) (online at cop.senate.gov/hearings/library/hearing-092210-contracting.cfm) (stating that "[t]here was a provision in the original contract that provided for the potential for incentives. We have not received incentives to date. And we're in the process of working through a revision to that contract. My understanding is that there will not be an incentive framework forward.").

fications, since delays ease the downward pressure that foreclosures put on housing prices. But delays that do not address the underlying issues associated with mass foreclosures will not provide solutions.) On top of that, every redefault under HAMP represents a loss to taxpayers. This is a result of HAMP's structure: the program begins making incentive payments to borrowers, servicers, and investors after a loan is permanently modified. These payments continue for up to five years, so if a borrower redefaults after three years, the government will have paid thousands of dollars for an ultimately unsuccessful modification. In this sense, redefaults are more costly than HAMP trial modifications that fail to convert to permanent modifications, since no tax dollars are spent on trial modifications.

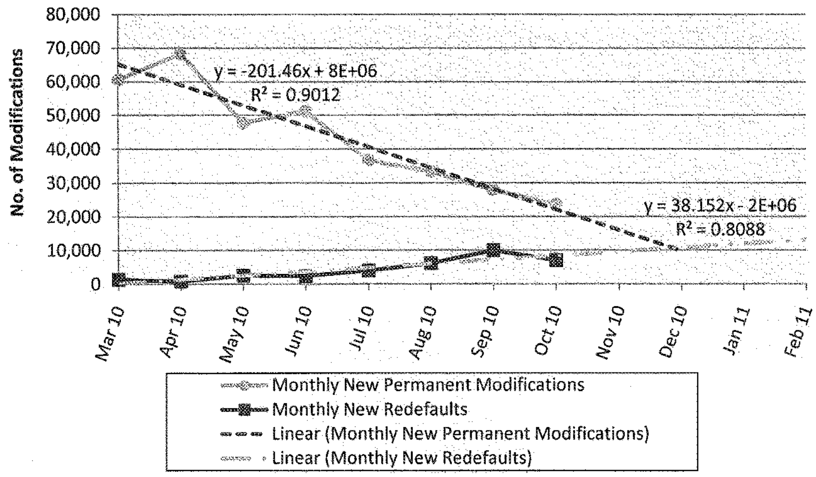
Treasury's initial estimated redefault rate over the five-year span of HAMP permanent modifications was 40 percent, but some private analysts estimate that the program's redefault rate will be higher. Barclays Capital has projected a 60 percent redefault rate for HAMP.[334] In addition, Standard & Poor's estimates that only 20 percent of HAMP trial modifications will ultimately succeed, an estimate that includes both the program's rate of conversion from trial modifications to permanent modifications and its redefault rate.[335]

Because HAMP permanent modifications have only been in effect for a maximum of about a year, it is difficult to evaluate the program's redefault rate in the context of Treasury's five-year estimate of a 40 percent redefault rate. So far, the 60+ day delinquency rate after three months in the program is 4.6 percent. After six months, the redefault rate is 9.8 percent. After nine months, the rate is 15.6 percent. And after 12 months, the rate is 25.4 percent.[336] (For a fuller discussion of HAMP redefaults, see Section I.4, below.)

In the context of the falling number of new HAMP permanent modifications, redefaults are an even greater concern. If present trends continue, the monthly number of new permanent modifications could actually fall below the monthly number of redefaults, as Figure 16 shows. If this happens, the overall number of homeowners being helped by HAMP would begin to fall.

[334] Barclays Capital e-mail to Panel staff (Nov. 1, 2010).
[335] Standard & Poor's, *U.S. Government Cost To Resolve and Relaunch Fannie Mae and Freddie Mac Could Approach $700 Billion* (Nov. 4, 2010).
[336] Data provided by Treasury.

FIGURE 16: MONTHLY REDEFAULTS AND NEW PERMANENT MODIFICATIONS IF CURRENT TRENDS CONTINUE[337]



To understand better how Treasury might seek to minimize redefaults, the Panel examined (1) the incidence of redefaults during the Great Depression, the only previous era in which the U.S. government instituted a nationwide foreclosure-prevention program, in order to draw lessons to apply in today's environment; (2) redefault rates for non-HAMP modifications during the current crisis; and (3) HAMP redefaults, analyzing the data by amount of equity held by the borrower and affordability, among other factors.

1. The Great Depression-Era Home Owners' Loan Corporation

The 1920s and 1930s represent one the largest boom-and-bust real-estate cycles in U.S. history. From 1920 until 1930, prices of owner-occupied homes rose by an average of 45 percent. Then between 1930 and 1940, nominal prices in those same cities fell by an average of 48.6 percent.[338] The market shocks were particularly severe in the early 1930s. Housing prices fell by 30 to 40 percent

[337] "Monthly New Permanent Modifications" and "Monthly New Redefaults" are derived from cumulative "All Permanent Modifications Started" and "Permanent Modifications Canceled" (excluding loans paid off) levels from March 2010 to October 2010 recorded in the Making Home Affordable Program's monthly Servicer Performance Reports. For these monthly reports, *see* Treasury Reports and Documents, *supra* note 48.

[338] Price V. Fishback et al., *The Influence of the Home Owner's Loan Corporation on Housing Markets During the 1930s,* National Bureau of Economic Research Working Paper No. 15824, at 5–6 (Mar. 2010) (online at www.nber.org/papers/w15824) (hereinafter "NBER Working Paper No. 15824"). These figures were derived from a sample of 278 of the largest cities across the country. In real terms, the price declines were lower because the U.S. economy was experiencing deflation. The Consumer Price Index fell by 16 percent between 1930 and 1940.

nationwide between 1929 and 1932.[339] The non-farm foreclosure rate reached 13 percent in 1933.[340]

In June 1933, in response to the housing crisis and an unemployment rate of 25 percent, Congress established the Home Owners' Loan Corporation (HOLC).[341] The HOLC was intended to assist homeowners who were in trouble largely through no fault of their own. It did so by purchasing mortgages from private lenders and offering homeowners refinanced mortgages that were intended to be more sustainable.[342] Initially, HOLC loans had 5 percent interest rates and amortizing, 15-year terms, which was a substantial improvement for borrowers.[343] HOLC loans also represented better terms than the private mortgage market was offering at the time. (Annex I provides an extended discussion of the HOLC.)

How did the HOLC's refinanced mortgages perform? In the HOLC's early years, the performance was relatively poor. In June 1936, 62.6 percent of HOLC borrowers were at least one month delinquent, and 39.5 percent of them were at least three months delinquent. But over time the delinquency statistics showed improvement. By June 1939, the one-month delinquency rate was 46.8 percent, and the three-month delinquency rate was 24.3 percent. By June 1942, the one-month delinquency rate was down to 28.2 percent, and the three-month delinquency rate was just 5.1 percent.[344]

This improvement was likely in part the result of improving economic conditions in the 1940s. It was also partly the result of the HOLC foreclosing on delinquent borrowers; once the loans were foreclosed, the HOLC no longer counted them as part of its loan inventory. Altogether, throughout the 18-year life of the HOLC, about 200,000 loans, or roughly 20 percent of the HOLC's portfolio, went into foreclosure or were voluntarily transferred by the borrower to the HOLC.

Another potential reason why the percentage of defaulted loans fell between 1936 and 1950 is that the HOLC went to great lengths to keep homeowners in their houses. At its peak, the HOLC had about 20,000 employees and offices in 48 states. In servicing loans, the HOLC relied heavily on personal contact aimed at helping distressed homeowners. Servicing practices varied by state and over time, but there were some common themes. In the second and third months of delinquency, the HOLC would insert special notices with

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[339] *Id.* at 5–6. The shocks were even more severe in certain regions; in Manhattan, home prices fell by a staggering 66 percent during the same four-year period. *See also* Tom Nicholas and Anna Scherbina, *Real Estate Prices During the Roaring Twenties and the Great Depression,* U.C. Davis Graduate School of Management Research Paper No. 18–09, at 16 (Jan. 29, 2010) (online at papers.ssrn.com/sol3/papers.cfm?abstract__id=1470448).

[340] David Wheelock, *The Federal Response to Home Mortgage Distress: Lessons from the Great Depression,* Federal Reserve Bank of St. Louis Review, at 139 (May/June 2008) (online at research.stlouisfed.org/publications/review/08/05/Wheelock.pdf) (hereinafter "Federal Reserve Bank of St. Louis Review Paper").

[341] Robert Van Giezen and Albert E. Schwenk, *Compensation From Before World War I Through the Great Depression,* Bureau of Labor Statistics Paper (Jan. 30, 2003) (online at www.bls.gov/opub/cwc/cm20030124ar03p1.htm).

[342] NBER Working Paper No. 15824, *supra* note 338, at 6–7.

[343] Residential mortgages in the 1920s typically required very large down payments and had relatively high interest rates and short loan terms, so borrowers were required to make balloon payments at the end of the term. By lowering the required down payment, extending the loan term, and lowering the interest rate, the HOLC was able to refinance many loans even in an environment of much lower property values. As Annex I discusses, the interest-only and negatively amortizing loans of the 2000s arguably offer a similar opportunity today.

[344] C. Lowell Harriss, *History and Policies of the Home Owners' Loan Corporation,* at 201–202, National Bureau of Economic Research (1951) (online at www.nber.org/books/harr51–1) (hereinafter "NBER Research Paper"). See Annex I for more detailed data.

the homeowner's monthly bill. If the homeowner was unresponsive, a form letter followed. Next came a personal letter. If there was no response, a HOLC staffer would make an in-person visit to the home. In some cases, HOLC employees helped homeowners or their relatives find jobs, and to collect insurance claims, unpaid debts, and pensions. HOLC employees even suggested ways of finding tenants or foster children to defray the homeowner's monthly mortgage payment.[345] C. Lowell Harriss, the author of a 1951 book about the HOLC, wrote: "The assistance given by the HOLC's service representatives is difficult to summarize adequately. The closest parallel, perhaps, is found in the social worker's helping individuals and families adjust to their own problems and to the community around them."[346] All of this stands in marked contrast, of course, to the highly automated, impersonal mortgage servicing practices of today. These differences are an important consideration in a comparison of redefault rates under the HOLC and HAMP.

It is difficult to analyze systematically the factors that drove HOLC delinquencies and foreclosures, since there is a relative lack of useful data. For example, the HOLC collected borrower income data only at the time it made the loan, not on an ongoing basis,[347] which makes it impossible to study the connection between mortgage affordability and delinquency. There has been research, though, on the connection between foreclosures and HOLC borrowers' equity stake in their homes. A study of a sample of HOLC loans in the New York region found that when the borrower's equity was equal to or greater than the amount of the HOLC loan, the foreclosure rate was 12 percent. That number rose as the borrower's equity got smaller, though. For borrowers whose equity was less than 25 percent of the loan value, the foreclosure rate topped 40 percent.[348]

The finding that HOLC loans were more likely to end in foreclosure if the borrower had little or no equity has important implications for HAMP. It suggests that borrowers with less equity or negative equity will be more likely to redefault on their modified loans, and thereby underscores the importance of principal reductions to the program's long-term success.

2. Redefaults in Other Loan Modification Efforts

Shortly after the FDIC took IndyMac Bank into receivership in July 2008, it instituted a mortgage modification program for delinquent borrowers. The program, also discussed in Section B, was applied to more than 60,000 residential mortgages that were 60 days or more past due.[349] The FDIC's program is similar to HAMP in several ways. Like HAMP, it uses an NPV test to determine whether a mortgage should be modified. And it uses interest rate reductions, term extensions and principal forbearance to make mortgages more affordable. The FDIC program is somewhat less aggressive than HAMP in seeking affordability; it reduces interest rates

[345] *Id.* at 66–67.
[346] *Id.* at 67.
[347] *Id.* at 87–88.
[348] *Id.* at 98.
[349] Federal Deposit Insurance Corporation, *The FDIC Loan Modification Program at IndyMac Federal Savings Bank,* presented by Richard A. Brown, Chief Economist, at the Mortgages and the Future of Housing Finance conference (Oct. 25, 2010).

as low as 3 percent, rather than 2 percent under HAMP, and it requires that first-lien mortgage payments exceed no more than 38 percent of income, rather than 31 percent under HAMP.[350]

The FDIC estimated that 33 percent of the IndyMac loans that it modified would eventually redefault.[351] So far, in the context of the IndyMac modifications, that projection has proven to be too optimistic. The FDIC recently published certain redefault data, and they show that the program's redefault rate rises steadily as modifications age. After modifications have been in the program for six months, the redefault rate is 18.5 percent. At one year, the redefault rate has risen to 42.1 percent. And at 18 months, the redefault rate is 59.0 percent.

The FDIC's data also show that depending on various characteristics of the loan and the borrower, the 18-month redefault rate may be as low as 40 percent or as high as 70 percent. For example, 18-month redefault rates on IndyMac loans modified when they were more than 180 days delinquent were 66.5 percent, while the redefault rate on loans modified when they were 60 days delinquent was 43.9 percent. Similarly, there was a divergence of redefault rates based on the borrower's original credit score. Homeowners with credit scores in the highest range had a redefault rate of 45.7 percent, while borrowers with credit scores in the lowest range had a redefault rate of 63.2 percent. There was also a large gap in redefault rates based on monthly payment reductions. For homeowners whose monthly payments dropped by 40 to 50 percent, the 18-month redefault rate was 42.8 percent. But for those whose payments fell by less than 20 percent, the redefault rate was around 70 percent. Perhaps the best news from the FDIC data is that redefault rates have been lower for more recent loan modifications than they were for earlier ones. For loans modified between September 2008 and April 2009, the 10-month redefault rate was 38.6 percent. But for loans modified during the following six months, the 10-month redefault rate fell to 27.1 percent.[352]

3. Current Trends in Loan Modifications and Redefaults

Two federal financial regulatory agencies, the Office of the Comptroller of the Currency (OCC) and the Office of Thrift Supervision (OTS), publish a quarterly statistical report on the U.S. mortgage market. This report, the OCC/OTS Mortgage Metrics Report, provides data on the performance of first-lien residential mortgages serviced by federally regulated banks and thrifts, which comprise 65 percent of all U.S. mortgages. So while the Mortgage Metrics Report is the most reliable source of nationwide data on mortgage delinquencies, loan modifications, and foreclosures, it does not include data from 35 percent of the mortgage market. The most recent Mortgage Metrics Report includes data through June 30, 2010. It shows that the number of loan modifications that are happening outside of HAMP, and therefore without incentive payments from the government, has exceeded the number of HAMP modifications each quarter since HAMP began in 2009. In the second quarter of

[350] Federal Deposit Insurance Corporation, *FDIC Loan Modification Program,* at 3 (online at www.fdic.gov/consumers/loans/loanmod/FDICLoanMod.pdf) (accessed Dec. 10, 2010).
[351] FDIC conversations with Panel staff (Oct. 28, 2010).
[352] FDIC data provided to Panel staff (Dec. 8, 2010).

2010, there were 164,473 permanent non-HAMP modifications and 108,946 permanent HAMP modifications.[353] It is still too early to draw any conclusions about the sustainability of modification programs that began in the last two years, since the ultimate success of those programs will hinge on whether the borrowers are able to stay in their homes over the long term. Still, it is instructive to review redefault data on modifications from non-government programs, since they shed light on how to make HAMP as effective as possible.

One must be cautious when comparing non-HAMP modifications with HAMP modifications because they do not necessarily have the same characteristics. For example, HAMP modifications generally result in larger decreases in monthly payments, and consequently result in better affordability, than non-HAMP modifications do. The Mortgage Metrics Report shows that in the second quarter of 2010, HAMP modifications resulted in an average monthly payment reduction of $608, compared to $307 for non-HAMP modifications.[354] Furthermore, homeowners in non-HAMP modifications, as a group, may be more likely to redefault than those in HAMP modifications, since certain factors that kept them from being approved for HAMP may also indicate that their personal finances are more precarious.

The data from the Mortgage Metrics Report show that redefault rates for all permanent loan modifications—a category that includes both HAMP and non-HAMP modifications—have been dropping each quarter since the start of 2009. For example, in the first quarter of 2009, 30.8 percent of modified loans were at least 60 days delinquent within just three months of the modification; by the fourth quarter of 2009, this figure had fallen to 11.4 percent. Similarly, in the first quarter of 2009, 42.8 percent of modified loans were at least 60 days delinquent within six months of the modification; by the fourth quarter, that figure had dropped to 20.7 percent.[355] Figure 17 shows the improvements in redefault rates since the start of 2009.

FIGURE 17: PERMANENT MODIFICATIONS AT LEAST 60 DAYS DELINQUENT, BY QUARTER [356]

	3-month Redefault Rate	6-month Redefault Rate	29-month Redefault Rate	12-month Redefault Rate
First Quarter 2009	30.8	42.8	51.5	55.0
Second Quarter 2009	18.7	33.5	40.9	43.2
Third Quarter 2009	14.7	27.7	32.7	—
Fourth Quarter 2009	11.4	20.7	—	—
First Quarter 2010	11.1	—	—	—

[356] OCC/OTS Mortgage Metrics Report, Second Quarter 2010, *supra* note 31, at 33.

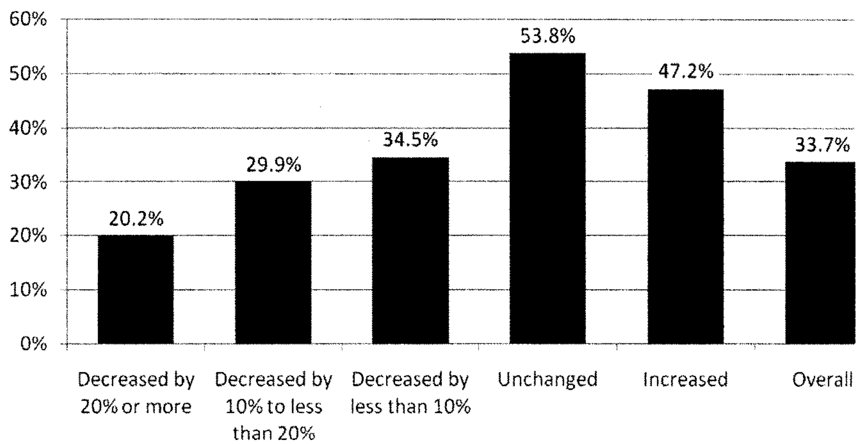
Data from nine mortgage servicers collected by the State Foreclosure Prevention Working Group confirm the notion that redefault rates on loan modifications have been improving. Rates of serious delinquency after six months fell from 30.8 percent for loans modified in August and September of 2008 to 15.3 percent for

[353] OCC/OTS Mortgage Metrics Report, Second Quarter 2010, *supra* note 31, at 21.
[354] OCC/OTS Mortgage Metrics Report, Second Quarter 2010, *supra* note 31, at 30–32.
[355] OCC/OTS Mortgage Metrics Report, Second Quarter 2010, *supra* note 31, at 33.

loans modified in August and September of 2009.[357] The State Foreclosure Prevention Working Group also found that in the same time period redefault rates have fallen by more than 60 percent for both modifications that result in significant payment reductions and for those that result in significant principal reductions.[358]

The Mortgage Metrics Report also shows that modifications resulting in large reductions in monthly payments have lower redefault rates than other modifications. This correlation is not surprising, given that HAMP, which produces greater reductions in monthly payments than other loan modification programs, has lower redefault rates than those programs, as shown below in Section I.4. The 2009 data show that 19.6 percent of modifications that resulted in payment reductions of at least 20 percent were at least 60 days delinquent within six months. The 60-day delinquency rates are higher for modifications that result in less relief—or in some cases, a greater payment burden—for borrowers.[359] Figure 18 shows 60+ day delinquency rates by change in monthly payment.

FIGURE 18: 60+ DAY DELINQUENCY RATES OF LOANS MODIFIED IN 2009 BY CHANGE IN PAYMENT[360]



4. HAMP Redefaults

a. Redefault Rates

Overall, through October 2010, 35,815 of 519,648 HAMP permanent modifications have redefaulted. This yields an overall redefault rate of 6.9 percent.[361] This statistic is misleading, however,

[357] State Foreclosure Prevention Working Group, *Redefault Rates Improve for Recent Loan Modifications,* at 5 (Aug. 2010) (online at www.csbs.org/regulatory/Documents/SFPWG/DataReportAug2010.pdf).

[358] *Id.* at 6 ("A comparison of five reporting servicers demonstrates how the improvement in redefault rate is evident even when controlling for the type of loan modification. For instance, the redefault rate at six months for loans with significant payment reductions fell from almost 31.4% for loans modified in August to September of 2008 to just 11.8% for loans modified in August to September of 2009, a more than 62% reduction. Similarly, the redefault rate for loans with significant principal reductions fell from 35.4% to 12.9%, over a 63% reduction.").

[359] OCC/OTS Mortgage Metrics Report, Second Quarter 2010, *supra* note 31, at 39.

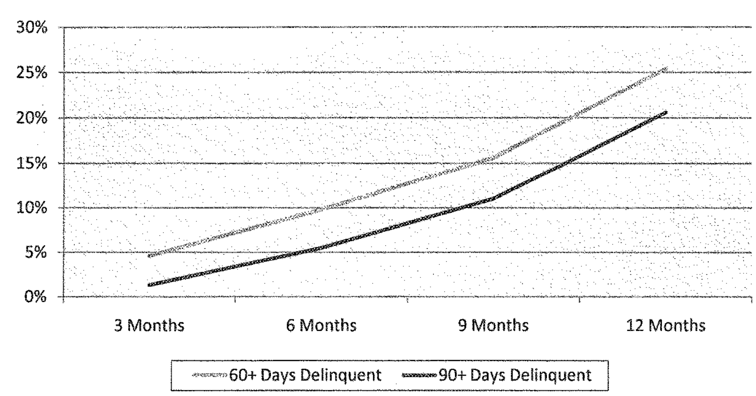
[360] OCC/OTS Mortgage Metrics Report, Second Quarter 2010, *supra* note 31, at 40.

[361] Data provided by Treasury.

in terms of predicting the ultimate redefault rate on HAMP permanent modifications. More than half of all HAMP permanent modifications were made between April and October 2010. Thus, the denominator in the overall redefault rate is tilted toward more recent modifications. As most redefaults do not happen immediately, the numerator is tilted toward older modifications, which are fewer.

A more complete picture of HAMP redefault rates emerges from the redefault rate for HAMP modifications at set numbers of months post-modification, as shown in Figure 19. Figure 19 shows that although only around 1 percent of permanent modifications are 90+ days delinquent within their first three months, the number jumps to 5.5 percent by month six and 11 percent by month nine; within a year, 21 percent of HAMP permanent modifications are 90 or more days delinquent, at which point they are disqualified from the program. This compares to a 40 percent redefault projection over five years. HAMP does not yet have redefault rates past one year, and it is not likely that the redefault rate will plateau at one year. Certain characteristics common to HAMP permanent modifications, such as balloon payments, deep negative equity, borrowers with severely damaged credit scores (which increase the borrowers' cost of credit for other obligations), and interest rates and payments that can rise after five years, may leave HAMP borrowers vulnerable to redefaults that peak over a somewhat longer time period. Doubtless, the state of the economy and unemployment will have a bearing on the performance of the modifications over the coming years. The 12-month redefault rate is well below Treasury's 40-percent assumption, but it is important to remember that the 40-percent number reflects the redefault rate over the five-year span of the modification. Only time will tell whether the assumption is too high, accurate, or too low.

FIGURE 19: HAMP REDEFAULT RATES BY MONTHS POST-MODIFICATION [362]

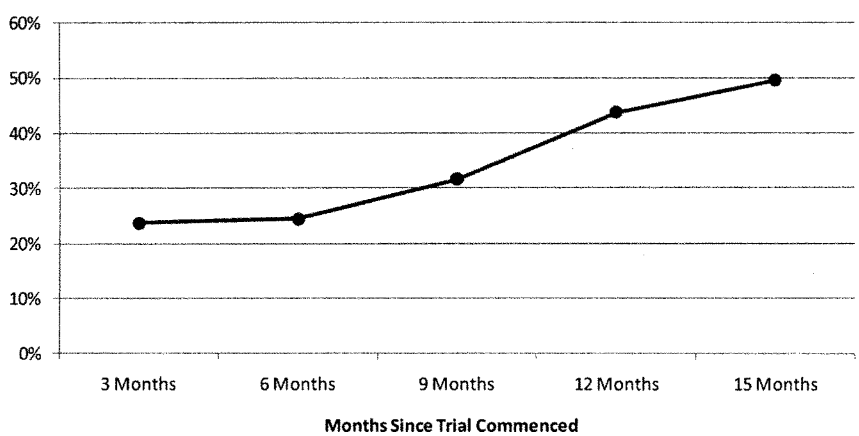


HAMP's trial period serves as an effective tool in reducing the investment of HAMP dollars towards borrowers who are more likely to redefault, as HAMP redefault rates do not include borrowers who default during the trial period. Without such a screening

[362] Data provided by Treasury.

mechanism, many additional loans would likely have redefaulted. In addition to the modifications experiencing traditional payment default during the permanent modification period (redefault), 146,031 HAMP trials were disqualified because of payment default. Had Treasury not utilized a trial period, these payment defaults would likely have combined with the traditional redefaults to yield a 44 percent redefault rate at 12 months and a 50 percent redefault rate at 15 months, as shown in Figure 20. The policy decision by Treasury to include a trial period helped screen out these borrowers who could not support a modified payment and contributed to more sustainable outcomes within HAMP. Recent changes made in June within HAMP requiring up-front verification to receive a trial modification further prevent less prepared borrowers from entering the trial period.

FIGURE 20: 90+ DAY DELINQUENCY RATE FOR ALL QUALIFIED HAMP MODIFICATIONS, TRIAL AND PERMANENT [363]



Data available in the OCC/OTS Mortgage Metrics report allow a comparison of HAMP modifications and non-HAMP modifications over the same time period. It is important to note, however, that the OCC/OTS data only cover approximately two-thirds of the mortgage market. According to that data, HAMP modifications are redefaulting at lower rates than other loan modifications, which likely stems from the more substantial relief generally received under the program as compared to non-HAMP modifications, as well as differences in borrower characteristics between borrowers in HAMP and borrowers receiving proprietary modifications. Among HAMP modifications initiated in the fourth quarter of 2009, 10.8 percent were at least 60 days delinquent within six months. This compares to 22.4 percent for non-HAMP modifications started during the same period.[364] Figure 21 compares the redefault rates

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[363] Data provided by Treasury. This figure assumes that there was only a three month trial period, which is what was called for by the original terms of HAMP. In fact some trial periods were extended considerably longer.
[364] OCC/OTS Mortgage Metrics Report, Second Quarter 2010, *supra* note 31, at 37.

for permanent HAMP modifications with those for permanent non-HAMP modifications.

FIGURE 21: HAMP VS. NON-HAMP 60+ DAY DELINQUENCY RATES [365]

	Number of Modifications	3 Months after Modification (Percent)	6 Months after Modification (Percent)
HAMP Fourth Quarter 2009	20,679	7.9	10.8
Other Fourth Quarter 2009	103,617	12.1	22.4
HAMP First Quarter 2010	100,269	10.5	—
Other First Quarter 2010	131,207	11.6	—

[365] OCC/OTS Mortgage Metrics Report, Second Quarter 2010, *supra* note 31, at 37.

b. Relationship Between Modification Characteristics and Redefault Rates

A full exploration of the relationship between modification characteristics and redefault rates would necessitate careful statistical analysis of loan-level data and is beyond the scope of this report. The Panel is surprised that Treasury has not undertaken such a statistical analysis itself, as it is fundamental to understanding what is and what is not working with HAMP. At this point there is already over a year's worth of performance history on many modifications. A better understanding of the relationship between modification characteristics and redefaults is critical for optimizing modifications and making the best use of TARP funds. The Panel strongly urges Treasury to undertake such analysis as soon as possible, with due attention to LTV ratios, back-end DTI ratios, the presence of second liens, hardship reasons, and state and ZIP code of the property's location, as well as these variables' interactions, and to make its findings public.

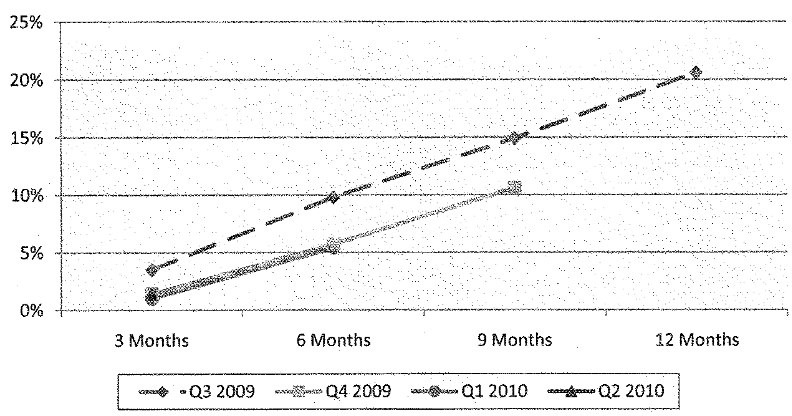
The Panel also urges Treasury to make loan-level data on HAMP modifications publicly available in a form that is readily accessible for data analysis. Enabling public analysis of the data (including analysis by researchers at other government agencies) will help provide feedback to Treasury that can be used to improve HAMP as well as to optimize the design of non-HAMP foreclosure mitigation programs. The Panel recognizes that there are legitimate concerns about protecting borrower privacy, but simply removing borrower names, Social Security numbers, and street addresses from the data would provide borrowers with the same level of privacy as is provided for data released under the Home Mortgage Disclosure Act.

Although this report does not undertake a loan-level statistical analysis, in this section it does explore the relationship between HAMP redefault rates and certain modification characteristics.

Vintage

HAMP's original vintage—permanent modifications from the third quarter of 2009—have performed consistently worse than more recent vintages. (See Figure 22.) The reason for this is not clear.

FIGURE 22: REDEFAULT RATES (90+ DAYS DELINQUENT) BY QUARTERLY VINTAGE [366]



Mark-to-Market Loan-to-Value Ratio

Mark-to-market loan-to-value ratio at the time of the modification has a strong impact on redefault rates. More deeply underwater loans redefault at higher rates. This suggests that if the goal is to lower redefaults, HAMP modifications should place greater emphasis on principal reduction instead of principal forbearance; however, that goal must be weighed against the possibility that fewer borrowers would receive modifications, unless the NPV model were changed. PRA attempts to consider these points, as it requires servicers to run two NPV analyses—one general analysis and one featuring principal reduction. Thus, the success of PRA could positively influence the success of HAMP.

Figure 25 shows that the distribution of loan-to-value ratios for permanent modifications is heavily tilted toward deeply underwater loans. For all of the categories shown in Figure 23, redefaults trend upward with time. However, at each point in time, the loans with higher LTVs had higher redefault rates as compared to the loans with lower LTVs. The trend becomes even more pronounced for 90+ day delinquencies, as depicted in Figure 24. This conclusion is worrisome, given that most HAMP modifications retain a high LTV post-modification. Also notable in Figures 23 and 24 is that there is little difference in performance once LTVs exceed 120 percent. Permanent modifications with LTVs of 120–150 percent performed similarly to those with LTVs of above 150 percent. These figures do not necessarily represent a break point for performance based on LTV, but they do indicate that if LTV is low enough, there is a noticeable improvement in long-term performance. Figure 25 reveals that the number of HAMP modifications with LTVs of over 100 percent, meaning that the homeowner is underwater, far exceed the number of modifications in which the homeowner is above-water. Unless housing prices increase, or un-

[366] Data provided by Treasury.

less negative equity is addressed in some other manner, LTV represents a risk for HAMP going forward.[367]

FIGURE 23: 60+ DAY REDEFAULT RATES BY MARK-TO-MARKET LOAN-TO-VALUE RATIO[368]

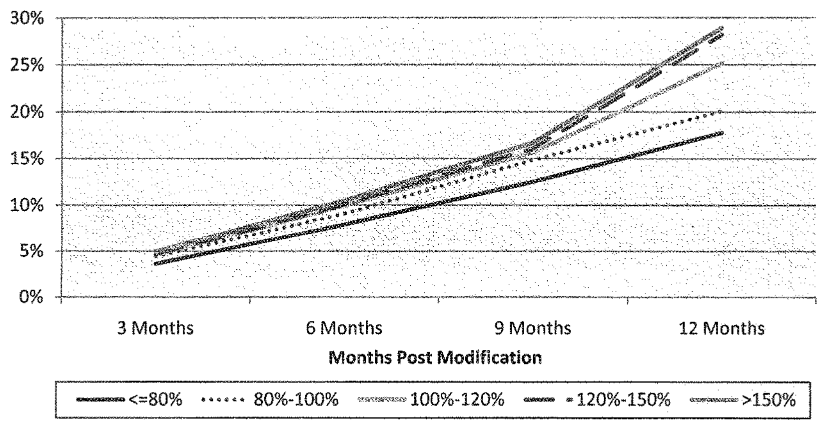
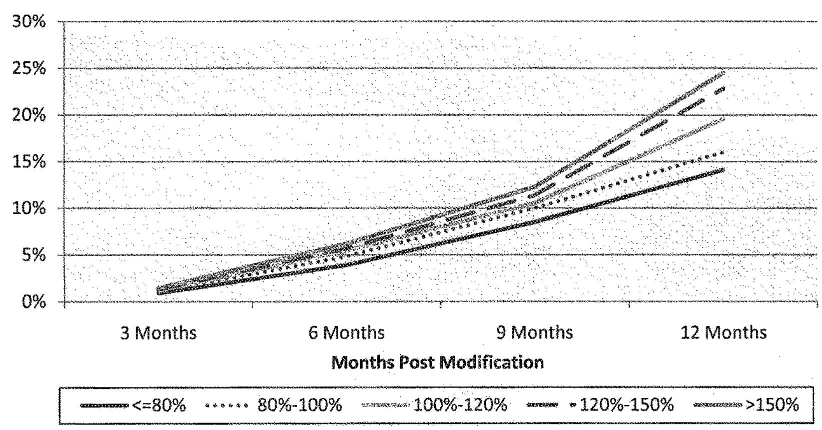
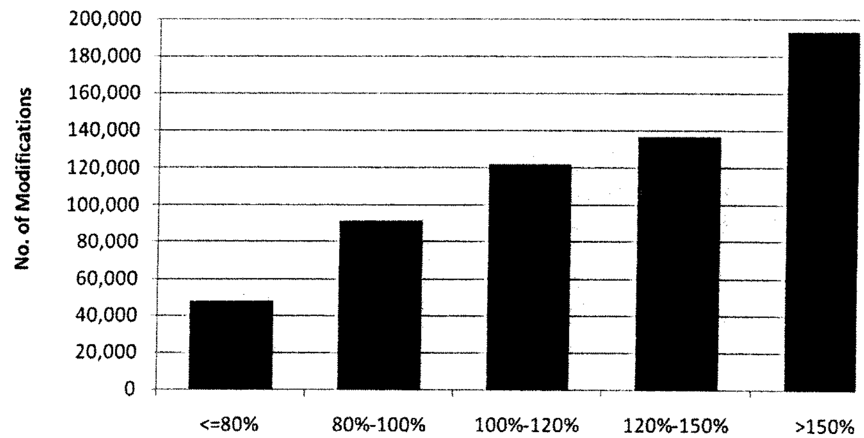


FIGURE 24: 90+ DAY REDEFAULT RATES BY MARK-TO-MARKET LOAN-TO-VALUE RATIO[369]



[367] Data provided by Treasury.
[368] Data provided by Treasury.
[369] Data provided by Treasury.

FIGURE 25: NUMBER OF PERMANENT MODIFICATIONS BY MARK-TO-MARKET LOAN-TO-VALUE RATIO [370]



Back-End DTI Ratio

Surprisingly, back-end DTI ratios, which provide a measure of homeowners' total indebtedness, seem to have no correlation with redefault rates. (See Figures 26 and 27.) [371] Redefaults are actually more frequent on modifications for borrowers who have lower back-end DTI ratios than they are for those with higher ratios.[372] It is not clear what implications to draw from this. It is possible that borrowers given a second chance through HAMP but still saddled with high total debt have managed to stay current for the term of the modification to date, generally less than a year. After all, many borrowers will prioritize a mortgage payment, especially a reduced payment, lest the family lose its home. It is unclear whether homeowners will be able to stay afloat under such a debt load over a longer term, particularly if the economy and unemployment do not improve. While DTI has not proven to be correlated with redefault to date, this is an important point to monitor over the coming years, as the situation could change dramatically. A counter intuitive result is often the result of a hidden correlation, which is why it is so important for Treasury to engage in sophisticated analysis of redefault data. It is striking, as Figure 28 shows, that nearly one-third of HAMP permanent modifications have back-end DTI ratios of more than 80 percent.[373]

[370] Data provided by Treasury.
[371] Data provided by Treasury.
[372] *See also* Federal Reserve Bank of Atlanta Working Paper, *supra* note 88 (finding that borrowers' DTI ratios at their loans' originations are not strong predictors of the likelihood that they will default on their mortgages).
[373] Data provided by Treasury.

FIGURE 26: 60+ DAY REDEFAULT RATES BY BACK-END DEBT-TO-INCOME RATIO[374]

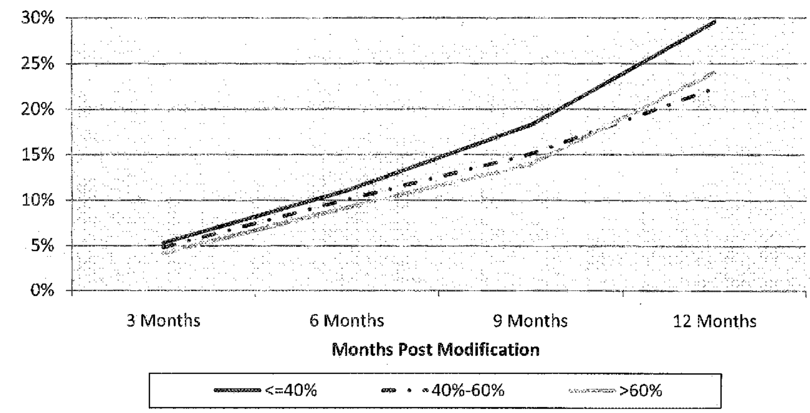
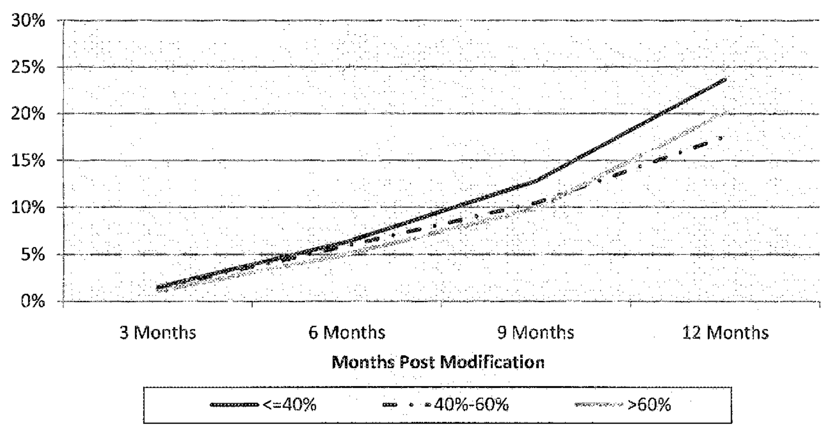
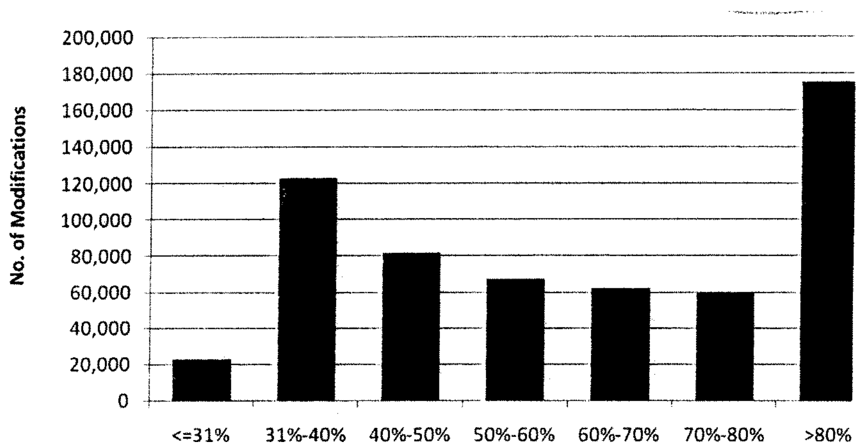


FIGURE 27: 90+ DAY REDEFAULT RATES BY BACK-END DEBT-TO-INCOME RATIO[375]



[374] Data provided by Treasury.
[375] Data provided by Treasury.

FIGURE 28: NUMBER OF PERMANENT MODIFICATIONS BY BACK-END DEBT-TO-INCOME RATIO[376]



Payment Reduction

The magnitude of the borrower's payment reduction under HAMP also clearly affects redefault rates. As Figures 29 and 30 show, redefault rates are much lower on loans with a larger percentage decrease in payments. It is not clear why the percentage of payment reduction would matter, whereas the absolute debt burden level would not, as discussed above. As Figure 31 shows, the majority of permanent modifications at least three months old in September 2010 had payment reductions of more than 30 percent.[377]

[376] Data provided by Treasury.
[377] Data provided by Treasury.

FIGURE 29: 60+ DAY REDEFAULT RATES BY REDUCTION IN MONTHLY PAYMENT [378]

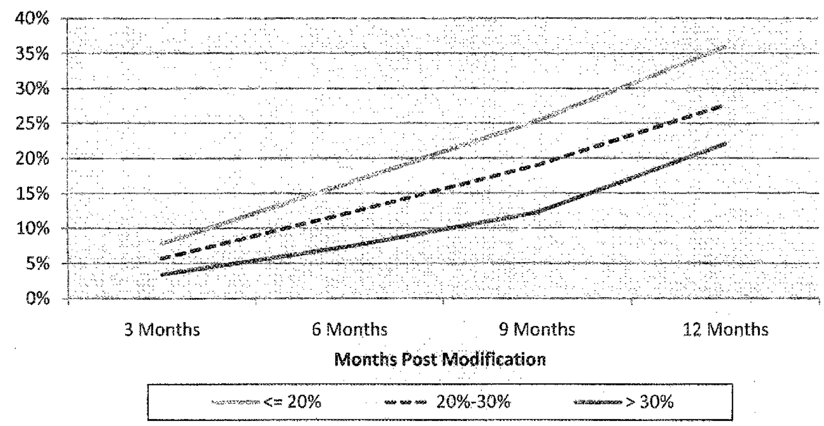
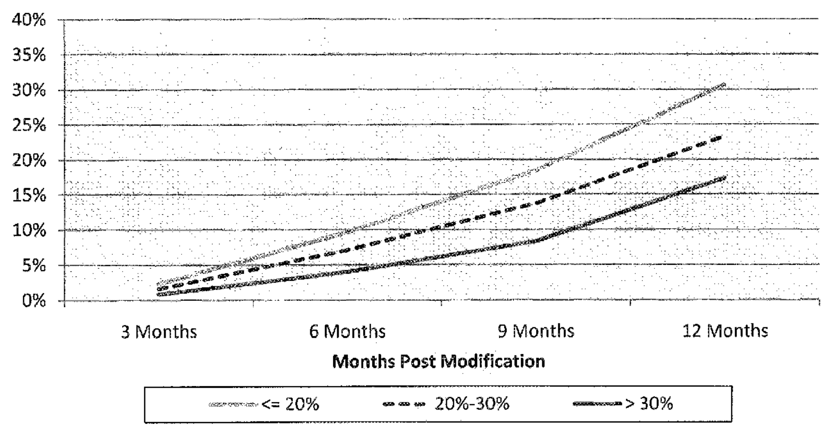
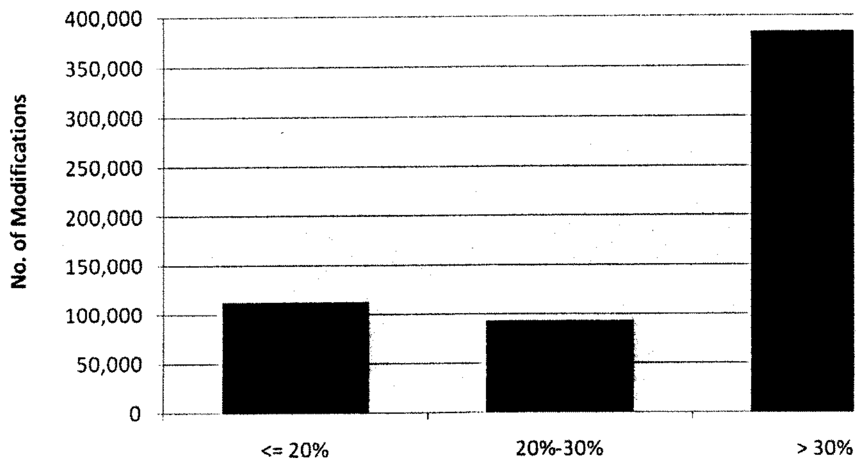


FIGURE 30: 90+ DAY REDEFAULT RATES BY REDUCTION IN MONTHLY PAYMENT [379]



[378] Data provided by Treasury.
[379] Data provided by Treasury.

FIGURE 31: NUMBER OF PERMANENT MODIFICATIONS BY PAYMENT REDUCTION PERCENTAGE [380]



Conclusions and Recommendations

In completing its fourth report on foreclosure mitigation efforts, the Panel remains concerned that the choices made by Treasury concerning issues such as program structure, transparency, and data collection have not left borrowers well served. Nearly two years after the announcement of MHA and HAMP, foreclosures remain largely unabated, and while the foreclosure level may be leveling off in some regions, it remains extremely high in others.

Under EESA, Treasury still has an obligation to use TARP funds in a manner that "protects home values" and "preserves homeownership." [381] The expiration of its ability to allocate additional money or create new programs does not mean that it cannot make strides toward meeting that mandate.

1. Treasury Should Announce Clear, Measurable Goals for HAMP

Nearly two years after HAMP was announced, it remains virtually impossible for oversight bodies and the public to determine whether the program is a success because Treasury has failed to offer a definition of success. This has been especially frustrating, given the clear shortcomings of the program. Yet, because tradeoffs are inevitable, any foreclosure mitigation program will be imperfect. However the fact that tradeoffs are inevitable does not mean that all of HAMP's flaws are acceptable. Unfortunately, the Panel is hamstrung in its attempts to distinguish between these types of problems—the unavoidable and the avoidable—because Treasury has provided so few goals and metrics for foreclosure prevention.

[380] Data provided by Treasury.

[381] 12 U.S.C. § 5201(2)(A)–(B). For a discussion of the authority of the Secretary of the Treasury to use TARP funds to create a program such as HAMP, please see Appendix III of the Panel's April 2010 Oversight Report, *supra* note 1, at 147.

Most fundamentally, how many foreclosures was HAMP intended to prevent? What percentage of temporary modifications did Treasury intend to convert to permanent status? What redefault rate did Treasury consider acceptable for permanent modifications? How frequently were servicers expected to misplace paperwork? In short, how many of HAMP's shortcomings were expected and inevitable, and how many were unexpected and potentially resolvable? Despite repeated urgings from the Panel and others, Treasury still has not answered these questions.

Treasury continues to have the ability to resolve this problem. It should announce clear, measurable goals for HAMP. Specifically, Treasury should announce a clear metric regarding how many foreclosures will be prevented, the only real measure of success. Up to 13 million foreclosures are expected over the coming years, and the American people should know how many will be averted with the $30 billion Treasury says it intends to spend on HAMP.

Announcing clear, measurable goals will help create much needed transparency for the program. Because the program lacks any metrics, Treasury has continued to focus on unrealistic expectations. For example, Treasury continues to state that HAMP will expend approximately $30 billion in TARP funds, yet CBO recently estimated that Treasury will spend only $12 billion out of the $45.6 billion allocated for all TARP foreclosure mitigation programs, including both HAMP and the Hardest Hit Fund. While CBO did not publish any detail on how it expects the projected $12 billion to be spent, if one assumes that states that are recipients of Hardest Hit Fund grants will spend the $7.6 billion allocated to them, that would leave only $4.4 billion to be spent on HAMP and the other TARP housing programs. Had Treasury faced up to HAMP's problems before the TARP expired, it could have taken more concrete steps, such as making material program changes or reallocating money. Absent a dramatic and unexpected increase in HAMP enrollment, many billions of dollars set aside for foreclosure mitigation will be left unused because Treasury failed to recognize HAMP's shortcomings.

2. Treasury Should Collect More Data on HAMP's Progress and on Loan Modifications

Treasury is to be commended for its improvement in HAMP data collection, yet additional data would provide valuable new information. In outlining the need for federal data collection, the Panel's March 2009 report noted, "While there is a clear picture of rising foreclosures and loss mitigation efforts that fail to keep pace, they do not provide sufficient information to determine *why* so many loans are defaulting and why foreclosure, rather than workouts, have been the dominant response and why modifications have often been unsuccessful. . . . Absent more complete and accurate information, legislators, regulators, and market participants are flying blind."[382] In particular, Treasury still does not collect sufficient information about why loans are moving to foreclosure rather than workouts, nor does it monitor closely enough any loan modifications performed outside of HAMP. Treasury should also explore

[382] March 2009 Oversight Report, *supra* note 10, at 15.

further public reporting of compliance matters, findings, and remediation activities by servicers.

While Treasury should collect and report more data generally, the Panel is particularly frustrated that data sufficient for analysis is lacking for any of Treasury's foreclosure mitigation programs, save HAMP. This is the Panel's fourth foreclosure mitigation report, and the paucity of available data has been a theme in each. Nearly two years after the general foreclosure mitigation initiative was announced, Treasury indicated that it does not have data available on its second lien programs.[383] More than six months after some of its add-on programs were announced, Treasury still does not even have a system of record to accept data.[384] For other areas, such as redefaults, Treasury is still considering what data it wishes to collect.[385] From the perspective of being able to demonstrate results and fix shortcomings, most Treasury programs are still at the very beginning stages. Because the add-on programs represent efforts to supplement HAMP's narrow focus, it is critical that they demonstrate results. Additional delays in data collection and reporting could mean that many programs do not even begin reporting data until the foreclosure mitigation programs are scheduled to stop making additional modifications at the end of 2012.

Further, because redefaults of permanent modifications pose a particular risk to HAMP's ultimate success, Treasury should focus its data analysis on identifying borrower characteristics that correlate to a higher risk of redefault. Treasury must also ensure that servicers are complying with data reporting requirements related to redefaults. At this point, some servicers are taking six months or longer to report new modifications to the system of record. Should redefaults be reported in a similarly tardy fashion, Treasury could end up improperly paying incentives to servicers for loans that have already redefaulted. Finally, Treasury should expand the range and frequency of its data reporting on redefaults.

3. Treasury Should Use HAMP's Existing Authorities as Effectively as Possible To Prevent Foreclosures

The TARP's expiration has ended Treasury's ability to change HAMP's structure or to dedicate additional money to the program. Even so, Treasury can focus on preventing as many foreclosures as possible under the existing program structure.

Treasury Should Enable Borrowers To Apply for HAMP as Easily as Possible. Treasury should ensure that the web portal is expanded to provide direct access for borrowers, allowing them to apply for modifications and to track the status of their applications online. A one-stop website for HAMP would end one of the biggest obstacles that borrowers have identified to their participation in the program. In addition, Treasury should work with HAMP servicers to encourage them to push the LoanPort as their primary point of entry for applications.

Treasury Must Hold Servicers Accountable for Failing To Complete Loan Modifications Appropriately. For example, to determine how frequently loan servicers are losing paperwork,

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[383] Transcript Testimony of Phyllis Caldwell, *supra* note 108.
[384] SIGTARP Quarterly Report to Congress, *supra* note 25, at 202.
[385] Treasury conversations with Panel staff (Oct. 28, 2010).

Freddie Mac should expand its Second Look loan reviews to include contacting borrowers or their representatives to verify whether documents were submitted properly. Further, although Fannie Mae and Freddie Mac serve as Treasury's agents in administering HAMP, Treasury bears ultimate responsibility for the program's success or failure. As such, it should take greater steps to hold Fannie Mae and Freddie Mac accountable. This is especially critical in light of statements from the GSEs indicating a potential conflict of interest between their own business interests and their role as financial agents. Performance reviews of Fannie Mae and Freddie Mac should be expanded to include borrower oriented qualitative and quantitative measures. Compliance activities must focus on borrowers and outcomes, not merely process. Treasury should also be more willing to use its power to withhold or clawback incentive payments. It should then publicly detail its sanctions for non-compliance by both its financial agents and HAMP servicers.

Treasury Should Provide a Meaningful, Independent Appeals Process from Servicer Decisions. Currently, the primary mechanism for escalating complaints, the HOPE Hotline, preserves servicers' discretion to decide on a modification, relying on them to determine if they make a mistake initially. Treasury should remove the decision from the servicers' hands in favor of an independent and enforceable review. As previously suggested by the Panel, this would be an appropriate role for the Office of Homeowner Advocate or an ombudsman. In addition, to maximize the impact of the appeals process, Treasury should clearly inform borrowers that the hotline can be used to escalate complaints.

Treasury Must Address the Obstacles Presented by Second Liens. Since its initial report on foreclosure mitigation in March 2009, the Panel has consistently highlighted the modification obstacles created by second liens. Treasury is to be commended for creating programs to address second liens, such as 2MP and 2LP; however, it is extremely disappointing that nearly two years later the programs have no track record of success. It is critical that Treasury get the programs fully operational and produce data on which they can be evaluated. Further, given the important role second liens play in affecting a loan modification, Treasury should explore the implications of adding borrower-specific junior lien information directly into the NPV model. In particular, Treasury should consider the effect on the number of borrowers served and the impact on modification sustainability.

Treasury Should Consider Ways To Increase Participation. Although Treasury no longer has the ability to make material changes to the foreclosure mitigation programs, it can make more modest changes designed to incentivize participation further. In rolling out PRA, Treasury held discussions with the industry to find ways to increase participation in the new initiative. Based on that feedback, Treasury included authorization, but not a requirement, for equity sharing arrangements subject to borrower protection provisions. Treasury should monitor PRA to determine whether authorization for equity sharing does indeed appear to increase participation. If so, Treasury should consider authorizing equity sharing arrangements in other programs.

Treasury Should Encourage Loan Servicers To Offer More Effective, Sustainable Modifications. The Panel remains concerned regarding the long-term sustainability of HAMP modifications. High, persistent unemployment continues to present problems for many borrowers. HAMP modifications leave borrowers with continuing high levels of negative equity, and even after receiving a modification, half of HAMP borrowers are still paying 63 percent of pre-tax income towards debt. Treasury must continue to adapt its programs to address more effectively these root causes of foreclosure. Treasury can determine, based on data collected to date, which types of modifications have a lower correlation of redefault. Treasury should encourage servicers to make more of these types of modifications and fewer of the types of modifications that tend to end in redefault. Redefaults, after all, represent the worst failure of HAMP, as each redefault represents thousands of taxpayer dollars that have been spent merely to delay rather than prevent a foreclosure.

Treasury Should Identify and Consider Intervening in Cases of Potential Redefault. Once borrowers make it into the modification program, Treasury must focus on keeping them there, as unchecked redefaults have the potential to undermine even the modest progress made by HAMP. One lesson to be taken from the HOLC program during the Great Depression was the importance of ongoing intervention to hold down redefault rates. The HOLC experienced success with early intervention upon delinquency, such as targeted borrower outreach, and Treasury should encourage the same approach. Delinquencies that are flagged in their early stages can potentially be brought current through a repayment plan. Such early intervention could be done at minimal cost. In more serious situations or when early intervention is ineffective, Treasury should assess the cost of any additional intervention and the likelihood that such intervention would keep borrowers in their homes before spending additional resources. As part of this evaluation Treasury must consider whether resources are best directed to providing additional assistance to those already in the program or helping borrowers who have not yet entered the program.

Although HAMP has managed to prevent some number of foreclosures, the program as currently structured will never have the reach necessary to put an appreciable dent into the foreclosure crisis. Nonetheless, HAMP continues to have the authority to spend $30 billion in taxpayer funds. Treasury must ensure that every dollar spent is used as effectively as possible to prevent foreclosures.

ANNEX I: LESSONS FROM THE HOME OWNERS' LOAN CORPORATION OF THE 1930s AND 1940s

Prior to the current foreclosure crisis, the 1930s is the most recent era when U.S. housing prices have fallen on a sustained nationwide basis. The Depression-era decline in home prices led to a flood of foreclosures, which caused tremendous harm to families and communities. The federal government responded by enacting numerous policies aimed at helping affected homeowners and supporting the faltering mortgage market. One of the most significant steps was the establishment in June 1933 of the Home Owners' Loan Corporation (HOLC). The HOLC's goal was to provide relief to borrowers who were in trouble largely through no fault of their own. It did so by purchasing mortgages from private lenders and offering refinancing to homeowners on more favorable terms. This section examines the HOLC in the context of the U.S. mortgage market when it was established, compares the HOLC with HAMP, and draws lessons from the HOLC that provide perspective on challenges facing HAMP today.

A. Background

The mortgage market of the 1920s was substantially different than the modern system to which Americans have become accustomed. There was no national mortgage market, as there is today, meaning that interest rates could vary substantially in different parts of the country. In some geographic areas, even as home prices soared during the 1920s, banks did not offer real estate loans, so local residents turned to insurance companies for mortgages.[386] In addition, borrowers typically had to make down payments equal to 40 to 60 percent of the property's value. Loans typically lasted 10 years or less and required payment of interest only; after the loan term, a balloon payment equal to the loan's principal was due. Because most borrowers did not have the cash to pay off the principal, they typically refinanced into a new loan.[387] The booming real-estate market of the 1920s also had some features that would be familiar to modern-day Americans. Lending standards became looser during the 1920s, with many homeowners taking out amortizing second liens that allowed them to borrow an additional 30 percent of their home's value.[388]

When property values contracted sharply in the early 1930s, obtaining a refinanced mortgage became much more difficult. As in the current crisis, relatively few homeowners received the kinds of private mortgage modifications that made it easier for them to

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[386] Senate Committee on Banking and Currency, Subcommittee on Home Mortgages, Etc., Testimony of Horace Russell, general counsel, Federal Home Loan Bank Board of Atlanta, *Home Owners Loan Act,* 73rd Congress, at 7–8 (Apr. 20 and 22, 1933) (hereinafter "Testimony of Horace Russell") (estimating that in 1933, one-third of U.S. counties did not have banks that made real estate loans, and noting that in many of these communities there had never been banks that made such loans).

[387] While some lenders did offer amortizing loans, even those had relatively short terms. NBER Working Paper No. 15824, *supra* note 338, at 6–7.

[388] Kenneth A. Snowden, *The Anatomy of a Residential Mortgage Crisis: A Look Back to the 1930s,* National Bureau of Economic Research Working Paper No. 16244, at 9–10 (July 2010) (online at www.nber.org/papers/w16244.pdf).

keep their homes.[389] One study of mortgage modifications in the New York metropolitan area found that 5 percent of loans originated from 1920–1939 received a modification that might be considered a concession by the lender, while almost 14 percent of those loans ended in a foreclosure or an agreement by the borrower to provide a deed in lieu of foreclosure.[390] Lenders may have been cautious about offering concessions to homeowners because they had trouble distinguishing between the mortgages that needed a modification in order to avert a foreclosure and those that did not. Modern credit scores were not available in the 1930s,[391] and DTI ratios, which today's lenders use to determine whether a borrower can afford a mortgage, were apparently not widely used.[392]

By 1933, the government estimated that 20 to 25 percent of the nation's $20 billion in home mortgage debt ($336 billion in today's dollars) was in default.[393]

B. The HOLC's Operations

The HOLC was established by the Home Owners Loan Act of 1933 as a government corporation to be administered by the recently established Federal Home Loan Bank Board. The legislation, which had broad support in Congress,[394] was proposed by President Roosevelt. Roosevelt argued at the time that the "broad interests of the Nation require that specific safeguards should be thrown around home ownership as a guarantee of social and economic stability, and that to protect home owners from inequitable enforced liquidation in a time of general distress is a proper concern of the Government."[395] The HOLC was capitalized with $200 million ($3.4 billion in today's dollars). It was also given the authority to issue up to $2 billion in government bonds ($33 billion today).

HOLC refinance loans were restricted to borrowers in default.[396] Homeowners whose homes were worth $20,000 or less—this figure is equivalent to $336,000 today, and the vast majority of U.S. homeowners qualified under the standard—were eligible to apply for a refinancing. The government provided refinancings of up to 80 percent of the property's value, or $14,000, whichever was higher. Initially, under the terms of the refinanced loans, the homeowner paid 5 percent interest, which was 1–2 percent below prevailing market rates,[397] and the loans fully amortized over 15 years. Second liens could also be refinanced, although total obligations on the

[389] *See, e.g.,* Jonathan D. Rose, *The Incredible HOLC? Mortgage Relief During the Great Depression,* at 25 (Nov. 9, 2009) (online at www.uncg.edu/bae/econ/seminars/2010/Rose.pdf) (hereinafter "The Incredible HOLC? Mortgage Relief During the Great Depression") ("Mortgage lenders were reluctant during the Depression to engage in much serious refinancing, especially debt reductions, and they appear similarly reluctant today.")

[390] Andra C. Ghent, *Residential Mortgage Renegotiation During the Great Depression,* at 20 (June 15, 2010) (online at papers.ssrn.com/sol3/papers.cfm?abstract_id=1604664) (hereinafter "Residential Mortgage Renegotiation During the Great Depression").

[391] There were credit reports at the time, and the HOLC used them to obtain information on applicants. NBER Research Paper, *supra* note 344, at 2, National Bureau of Economic Research.

[392] Residential Mortgage Renegotiation During the Great Depression, *supra* note 390.

[393] Testimony of Horace Russell, *supra* note 386, at 6, 9.

[394] The vote in the House of Representatives was 383–4. No record vote was taken in the Senate.

[395] Franklin D. Roosevelt, *Message to Congress on Small Home Mortgage Foreclosures* (Apr. 13, 1933) (online at www.presidency.ucsb.edu/ws/?pid=14618).

[396] NBER Research Paper, *supra* note 344, at 1, National Bureau of Economic Research.

[397] Testimony of Horace Russell, *supra* note 386, at 15, 17.

property could not exceed 100 percent of the appraisal value.[398] Delinquent property tax payments could be financed, including for people who owned their homes outright, which helped boost revenue for local governments.[399] The HOLC addressed the problem of unemployment by allowing three-year term extensions for borrowers who were unable to pay. The program did not offer loans for new home purchases,[400] but it did lend money for the reconditioning of homes.[401]

Lenders who agreed to sell their mortgages to the government received the appraised value of the property. Appraisals were also used to determine whether a homeowner had the 20 percent equity needed to qualify for a HOLC mortgage. Because housing markets were not functioning properly at the time, determining appraised values was difficult. The HOLC's chairman, William Stevenson, acknowledged this problem when the program was established, saying, "The matter of appraisal is the most difficult problem to be dealt with by the Corporation on account of the chaotic condition of the country with reference to values."[402] HOLC appraisals were supposed to weigh three factors equally: the property's estimated current market price; the cost of a similar lot, plus the cost of reproducing the building, minus depreciation; and the capitalization of the reasonable monthly rental value for the last 10 years.[403] Despite the establishment of this standard, research has shown that ensuring accurate appraisals was a problem for the HOLC, and appraisal standards varied significantly across the country.[404]

Jonathan Rose, an economist with the Federal Reserve Board, concludes in a recent paper that the HOLC set appraisals at high levels,[405] which benefitted private lenders, since they received more than they expected to earn from their delinquent mortgages, and resulted in fewer principal reductions for homeowners than would have occurred at lower appraisal values. Mr. Rose concludes that the inflated appraisals seem to have been deliberate, with the likely goals having been to encourage lenders to participate and to support prices in the housing market. "The conclusion is that in many ways the HOLC was a lenders' program," Mr. Rose writes. "Fundamentally, with a median decline in housing prices of 33 percent, large adjustments were needed to debts undertaken during the 1920s. Under the HOLC, the bulk of this adjustment was left to the borrowers, while many lenders were absolved completely. Borrowers certainly benefitted from the HOLC's lenient mortgage

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[398] NBER Research Paper, *supra* note 344, at 35–39, National Bureau of Economic Research.

[399] Rosalind Tough, *The Life Cycle of the Home Owners' Loan Corporation,* Land Economics (1951) (hereinafter "The Life Cycle of the Home Owners' Loan Corporation").

[400] Home Owner's Loan Corporation, *Statement by Chairman William F. Stevenson Relative to the Method and Procedure of Procuring Loans from the Federal Home Owners' Loan Corporation* (June 6, 1933) (hereinafter "Statement by Chairman William F. Stevenson").

[401] NBER Research Paper, *supra* note 344, at 4, National Bureau of Economic Research.

[402] Statement by Chairman William F. Stevenson, *supra* note 400.

[403] NBER Research Paper, *supra* note 344, at 2, National Bureau of Economic Research.

[404] The Incredible HOLC? Mortgage Relief During the Great Depression, *supra* note 389, at 23.

[405] Mr. Rose adds: "The fact that generous appraisals were made was not a secret, although it is not widely known today. A 1933 pamphlet published by the HOLC to give information to potential borrowers described the appraisal as being an estimate of 'fair worth' rather than 'technical market value.' The Federal Home Loan Bank Review . . . stated that HOLC loans 'were permitted to be equal to 80 per cent of liberal appraisals. They were intended to be generous and may have frequently approached or sometimes exceeded market values at that time.'" The Incredible HOLC? Mortgage Relief During the Great Depression, *supra* note 389, at 1–2.

structure, but lenders also benefitted greatly from the removal of poorly performing assets off of their balance sheets."[406]

Private lenders who sold mortgages to the HOLC usually were not paid in cash. Instead, they generally received government bonds. Initially, these were 18-year bonds that paid 4 percent interest. Although these bonds were often worth less than the face value of the original mortgages, the private lenders benefited from the government's guarantee of the bonds, as well as their favorable tax treatment.[407] If a lender refused to sell the loan except for cash, and the loan was worth 40 percent or less of the property's value, the government would pay cash, and then refinance the borrower into a 6-percent interest loan.[408]

When Congress established the HOLC, it was aware that the program's thin spread—the HOLC was collecting 5 percent interest, and its bonds paid 4 percent—combined with the likelihood of defaults, meant that the program might prove to be unprofitable. Given the harsh economic circumstances, Congress was willing to accept losses from the program.[409] As it turned out, the HOLC benefitted greatly from the low interest rates of the era. Although the HOLC initially paid 4 percent interest on its bonds, its average borrowing cost between 1933 and 1949 was 2.24 percent.[410] Over the life of the program, even though the interest rate charged to HOLC borrowers fell to 4.5 percent in 1939, the HOLC's spread was about 2.5 percentage points.[411]

The HOLC established offices in every state, and its employees worked with homeowners to keep them in their homes. The window of time to obtain a HOLC loan was relatively short—from August 1933 until June 1936. By the end, the HOLC received 1.886 million applications. The applicants sought a total of $6.2 billion in loans, or an average of $3,272 per application. According to one estimate, these applications accounted for about 20 percent of the non-farm, owner-occupied homes in the United States, and about 40 percent of mortgaged properties that qualified for the HOLC. Close to half of the applications were withdrawn or rejected, either because the homeowner was deemed not to be in sufficient trouble or because the loan was deemed too risky.[412] The HOLC ultimately issued 1.02 million refinance loans. The loans averaged $3,039, for a total of $3.1 billion.[413] According to one historian who studied the HOLC, applications from people who were unemployed would probably have been rejected, but most of the people who qualified had relatively modest incomes, and most had suffered financially dur-

[406] The Incredible HOLC? Mortgage Relief During the Great Depression, *supra* note 389, at 1–2. *See also* The Life Cycle of the Home Owners' Loan Corporation, *supra* note 399 ("What actually happened between 1933 and 1936—the emergency period during which the H.O.L.C. extended loans—was that the new organization bailed out not only the home owners of the United States but also the banking institutions.").

[407] The bonds were exempt from all federal, state, and local taxes except for estate taxes, surtaxes, inheritance taxes, and gift taxes. NBER Research Paper, *supra* note 344, at 11, National Bureau of Economic Research.

[408] Statement by Chairman William F. Stevenson, *supra* note 400.

[409] Senate Committee on Banking and Currency, Subcommittee on Home Mortgages, Etc., Statement of Senator James Couzens, *Home Owners Loan Act,* 73rd Cong., at 15 (Apr. 20 and 22, 1933).

[410] NBER Research Paper, *supra* note 344, at 5.

[411] NBER Research Paper, *supra* note 344, at 162–163.

[412] NBER Working Paper No. 15824, *supra* note 338, at 6–8.

[413] NBER Research Paper, *supra* note 344, at 1.

ing the Depression.[414] The HOLC reported in 1938 that, "Almost without exception, the cost to the home owner under the HOLC amortized mortgage is less than rent for a home of corresponding value. In addition, it permits the borrower actually to acquire final ownership free of debt."[415]

In 1933, the HOLC accounted for 12 percent of all new mortgages on one-to-four-family homes. That figure rose to 71 percent in 1934 before falling to 26 percent in 1935, and to 6 percent in 1936. The HOLC's share of the nation's outstanding mortgage debt peaked at 19 percent in 1935.[416] The HOLC purchased $770 million in mortgages from building & loans, many of which became savings & loans around this time; $525 million from commercial banks; $410 million from mutual savings banks; $165 million from insurance companies; and $880 million from other mortgage holders, including individuals.[417]

Over time, some of the HOLC's initial parameters changed. In 1934, Congress extended the government guarantee of the HOLC's bonds, which originally only covered interest, to include principal.[418] In 1935, Congress increased the HOLC's bonding authority to $4.75 billion. In 1939, the interest rate on HOLC loans was reduced from 5 percent to 4.5 percent, and Congress authorized an extension of HOLC loan terms from 15 years to 25 years.[419]

As discussed in Section I.1, above, the delinquency rate on HOLC mortgages was initially high, but it fell sharply over the life of the program. Figure 32 shows the fall in three-month delinquency rates until 1950, shortly before the HOLC finished liquidating its portfolio. Likely contributors to the falling delinquency rate include the improving economy of the 1940s and the fact that HOLC foreclosures pushed down the program's default rate by eliminating those loans from the overall pool of HOLC mortgages. In addition, the HOLC had a reputation as a lenient loan servicer, and often went to great lengths in an effort to keep families in their homes.[420] Starting in 1937, for example, the HOLC extended many defaulted loans by adding arrearages to the loan and, in many cases, giving the borrower several years to become current, with the goal of giving the borrower a fresh start psychologically.[421]

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[414] NBER Research Paper, *supra* note 344, at 50.

[415] Federal Home Loan Bank Board, *Sixth Annual Report for the Period Covering July 1, 1937–June 30, 1938,* at 95 (Oct. 1, 1938) (online at fraser.stlouisfed.org/publications/holc/issue/3013/download/40596/1937_38annualrpt.pdf).

[416] Federal Reserve Bank of St. Louis Review Paper, *supra* note 340, at 142.

[417] Charles Courtemanche and Kenneth Snowden, *Repairing a Mortgage Crisis: HOLC Lending and Its Impact on Local Housing Markets,* National Bureau of Economic Research Working Paper No. 16245, at 30 (July 2010) (online at www.nber.org/papers/w16245) (hereinafter "NBER Working Paper No. 16245").

[418] Federal Home Loan Bank Board, *Second Annual Report of the Home Owners' Loan Corporation Covering the Year 1934,* at 81 (Feb. 11, 1935) (online at fraser.stlouisfed.org/publications/holc/issue/3008/download/40940/1934_annualrpt_pt2.pdf). This decision was seen as an important way to encourage participation by lenders; after the government's guarantee was extended, the HOLC's bonds were considered as credit-worthy as U.S. Treasury bonds.

[419] Federal Home Loan Bank Board, *Eighth Annual Report for the Period July 1, 1939, through June 30, 1940,* at 126 (Oct. 1, 1940) (online at fraser.stlouisfed.org/publications/holc/issue/3016/download/40989/1939_40annualrpt_pt7.pdf). By the end of 1942, 30 percent of outstanding loans had received these extensions. NBER Research Paper, *supra* note 344, at 136.

[420] For more detail about the HOLC's loan servicing practices, see Section I.1, *supra.*

[421] NBER Research Paper, *supra* note 344, at 69.

FIGURE 32: PERCENTAGE OF HOLC MORTGAGES AT LEAST THREE MONTHS DELINQUENT, BY YEAR[422]

Year	Loans 3-plus Months Late	Total Loans	Percentage of Loans 3-plus Months Late
1936	397,533	1,005,988	39.5
1937	331,664	930,049	35.7
1938	270,144	878,017	30.8
1939	205,582	845,630	24.3
1940	100,027	854,233	11.7
1941	57,348	843,175	6.8
1942	41,607	808,219	5.1
1943	25,942	741,390	3.5
1944	16,009	641,446	2.5
1945	11,405	532,495	2.1
1946	9,349	430,307	2.2
1947	8,672	351,127	2.5
1948	9,407	278,189	3.4
1949	7,017	200,782	3.5
1950	2,420	73,965	3.3

[422] All data were reported in June of the specified year.

Despite its efforts to avoid foreclosure, the HOLC eventually acquired nearly 200,000 homes from borrowers who failed to make payments. These property acquisitions were mostly through foreclosure proceedings, though some involved a voluntary transfer of the property by the borrower. More than half of HOLC foreclosures involved borrowers who were a year and a half or more delinquent.[423] The HOLC often rented the foreclosed homes it owned, spending an average of $51 on reconditioning and $135 on maintenance before selling the homes.[424] The HOLC sold the foreclosed homes for an average of 93 percent of the original HOLC loan amount. Its average loss per foreclosed property was $1,568, for a total net loss of $310 million on properties acquired.[425]

As discussed in Section I.1, research indicates that when HOLC borrowers had less equity, they were more likely to lose their homes in foreclosures. Figure 33 shows this pattern in a sample of HOLC loans from the New York region.

FIGURE 33: FORECLOSURE RATES BY BORROWER'S EQUITY FOR A SAMPLE OF HOLC LOANS IN THE NEW YORK REGION

Borrower's Equity as Percentage of Loan Amount	Loans Made	Foreclosure Rate (Percent)
Less than 0%	561	46
0–24%	968	40
25–49%	920	37
50–74%	498	22
75–99%	258	22
100% or more	405	12

[423] NBER Research Paper, *supra* note 344, at 3, 101 ("There was no precedent for a real estate management situation of this size and complexity. Most of the foreclosed properties presented difficult problems of repair, reconditioning, rental, insurance, tax payment, and eventual sale. They were widely distributed geographically, many were twenty years old when acquired, and virtually all had been neglected by their defaulting owners.").

[424] NBER Research Paper, *supra* note 344, at 3. The HOLC also offered loans in connection with the sale of foreclosed properties.

[425] NBER Research Paper, *supra* note 344, at 4.

Mr. Rose recently reached a related conclusion. Mr. Rose's 2009 study looked at loan-level HOLC data from New York, New Jersey, and Connecticut. There was wide variation between HOLC foreclosure rates in different states, ranging from just 4.4 percent in Nevada to 42.9 percent in New York and 38.4 percent in New Jersey. One reason why foreclosures on HOLC loans may have been so common in New York and New Jersey, the paper concludes, is that those states used appraisal practices that overvalued the properties being refinanced, even in comparison to other states.[426] The paper notes that HOLC offices in New York and New Jersey paid more generous prices than elsewhere and concludes that these practices "likely contributed to the weak performance" of HOLC loans in those states.[427] HOLC borrowers in New York and New Jersey had less equity on average than HOLC borrowers elsewhere, and their loans foreclosed at higher rates.

There had been fears that the HOLC would lose up to $500 million, and these concerns occasionally led to the introduction of bills in Congress to force the early liquidation of the HOLC's loans.[428] Such calls went unheeded, though, and when the HOLC was liquidated in 1951, it reported a net profit of $14.2 million, based on net income of $352.2 million and losses of $338 million.[429] This accounting, however, did not include certain costs. The HOLC had borrowed from Treasury, and the costs of that borrowing, which were later pegged at $91.9 million, were not included in the HOLC's calculations. One recent estimate pegged the HOLC's losses in the general vicinity of $100 million.[430] In addition to the higher than expected spread between the HOLC's borrowing costs and its earnings, the HOLC also benefited from the nation's rising prosperity during World War II. Incomes rose, which led to falling delinquencies and lower servicing costs.[431]

Recent research by Kenneth Snowden and Charles Courtemanche of the University of North Carolina Greensboro found that the HOLC increased home values and home ownership rates—by repairing credit channels and by shutting off the destructive cycle by which foreclosures hurt nearby home values, which leads to more foreclosures. The researchers also found that the HOLC did not lead to an increase in home building.[432] The HOLC played a key role in the gradual reshaping of the U.S. mortgage market. Over time, the five-year interest-only loans of the 1920s

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[426] Other factors likely contributed to the wide variations in foreclosure rates. The HOLC attributed the differences, at least in part, to regional variations in real-estate price levels, in the duration and severity of the economic downturn, in real-estate tax rates, and in levels of mortgage indebtedness prior to 1933. The Life Cycle of the Home Owners' Loan Corporation, *supra* note 399, at 327.

[427] The Incredible HOLC? Mortgage Relief During the Great Depression, *supra* note 389, at 1–3, 8, 13. For the 3,032 loans that Mr. Rose reviewed from New York, New Jersey, and Connecticut, the average mark-up from the estimated market price to the final appraisal was 4.2 percent. Using the estimated market price rather than the appraised value, Mr. Rose calculated that 50.1 percent of the homeowners in this sample had less than 20 percent equity in their properties, and 19 percent had negative equity.

[428] The Life Cycle of the Home Owners' Loan Corporation, *supra* note 399, at 329–300.

[429] NBER Research Paper, *supra* note 344, at 160.

[430] NBER Working Paper No. 15824, *supra* note 338, at 9. Also omitted were the HOLC's free use of the U.S. Postal Service, which saved it $6 million and cost the government $3 million. Furthermore, the HOLC benefitted by virtue of its exemption from state and local business taxes, as well as from Social Security taxes. NBER Research Paper, *supra* note 344, at 160–162, National Bureau of Economic Research.

[431] NBER Research Paper, *supra* note 344, at 163–165.

[432] NBER Working Paper No. 16245, *supra* note 417, at 6, 26.

were replaced by 15-year, and later, 25-year, government-backed amortizing loans. And 20 percent down payments became a new standard in the mortgage industry.

C. How the HOLC Compares to HAMP

The differences between the HOLC and HAMP are considerable. This section distills some of the most important differences.

1. Scale of Programs

The HOLC operated on a significantly larger scale in relation to the U.S. housing market than HAMP has operated to date. The HOLC provided refinancing for about 10 percent of all non-farm, owner-occupied homes in the country, and for about 20 percent of all mortgaged homes.[433] For HAMP to achieve a comparable scale, it would have to yield between 7.6 million–10.1 million permanent modifications.[434] Through September 2010, less than 500,000 homeowners have received permanent HAMP modifications.[435] Of course, the scale of the 1930s mortgage crisis and the larger economic crisis of the Great Depression were comparatively larger than those of today. The number of non-farm foreclosures between 1929 and 1938 was 1.89 million,[436] at a time when the United States had approximately 10 million non-farm, owner-occupied homes.[437] Since July 2007, there have been approximately 8 million foreclosure starts in the United States,[438] while the number of U.S. owner-occupied homes is around 76 million.[439]

2. Nature of Government's Role

The HOLC, by purchasing mortgages from private lenders in an effort to prevent foreclosures, directly intervened in the mortgage market. HAMP, by contrast, intervenes in the market in an indirect way: by providing incentive payments to private lenders that agree to modify their loans within certain parameters. As a result of the fact that HAMP's market intervention is indirect, the government is not in a good position to use loan servicing policies as a tool for preventing foreclosures, as the HOLC did during the Depression. (It is important to note that two other government pro-

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[433] NBER Research Paper, *supra* note 344, at 1–2.

[434] In 2009, there were 76.4 million owner-occupied homes in the United States. Ten percent of those homes equals 7.6 million. There were 50.5 million mortgaged homes in the United States. Twenty percent of those homes equals 10.1 million. U.S. Census Bureau, *American Housing Survey National Tables: 2009,* Table 2–1 and Table 3–15 (online at www.census.gov/hhes/www/housing/ahs/ahs09/ahs09.html) (accessed Dec. 10, 2010) (hereinafter "American Housing Survey National Tables: 2009").

[435] MHA Servicer Performance Report Through September 2010, *supra* note 285, at 2.

[436] U.S. Department of Commerce, Bureau of the Census, *Historical Statistics of the United States: Colonial Times to 1970, Part 2,* at 651 (online at www2.census.gov/prod2/statcomp/documents/CT1970p2–02.pdf).

[437] *See* NBER Research Paper, *supra* note 344, at 1–2, National Bureau of Economic Research (stating that the HOLC made roughly one million loans, which provided aid to the owners of approximately one out of 10 non-farm, owner-occupied homes).

[438] *See* HOPE NOW Alliance, *National Data July 2007 to November 2009, Appendix—Mortgage Loss Mitigation Statistics,* at 7 (online at www.hopenow.com/industry-data/HOPE%20NOW%20National%20Data%20July07%20to%20Nov09%20v2%20%282%29.pdf) (showing 5.91 million foreclosure starts between July 2007 and November 2009); HOPE NOW Alliance, *Data Report May 2010,* at 8 (online at www.hopenow.com/industry-data/HOPE NOW Data Report (May) 06–21–2010 DRAFT2.pdf) (showing approximately 890,000 foreclosure starts between December 2009 and March 2010); HOPE NOW Alliance Industry Extrapolations and Metrics, *supra* note 4 (showing approximately 1.04 million foreclosure starts between April 2010 and September 2010).

[439] American Housing Survey National Tables: 2009, *supra* note 434.

grams during the current foreclosure crisis, HOPE for Homeowners and the FHA Short Refinance Program, aim to purchase mortgages from private lenders and thus represent direct interventions in the mortgage market. Neither program, though, has made a significant impact thus far.)

3. Enrollment Rate

The HOLC received 1.89 million applications, of which 1.02 million resulted in refinanced loans, for an enrollment rate of 54 percent. Because HAMP is structured differently than the HOLC, it does not have a directly comparable enrollment rate. The most comparable measures involve HAMP's permanent modifications started as a percentage of its trial modification offers, and HAMP's permanent modifications started as a percentage of its trial modifications started. The former rate is 32 percent; the latter rate is 37 percent.[440]

4. Homeowner Equity

Homeowners who participated in the HOLC had an average LTV ratio of 68.6 percent,[441] which suggests that their equity at the time of the refinancing was equal to nearly one-third of their homes' value. This figure is dependent, though, on the accuracy of HOLC appraisals, and those appraisals were often higher than what the housing market actually would bear at the time.[442] But even after accounting for inflated appraisals, it seems reasonable to assume that in most cases the homeowner had at least some equity at the time of the HOLC refinancing. This is in sharp contrast to HAMP, where most homeowners have substantial negative equity after their mortgage is modified. As of October 2010, half of all homeowners entering HAMP had an LTV ratio of greater than 120 percent. Their homes would have to appreciate by 20 percent before they would have any equity at all. This disparity between the HOLC and HAMP is critical because, as the data in Section I.4.b. illustrate, homeowners with little or no equity have less incentive to try to keep their homes, and are more likely to redefault on modified loans than homeowners who have more equity.

5. Duration of Relief

Because the HOLC refinanced loans, participating homeowners got new loans that generally offered permanently lower interest rates than in their previous mortgages. By contrast, despite the fact that Treasury refers to HAMP modifications as permanent, HAMP-modified loans can reset after five years to a higher interest rate.

6. Risk/Reward for Government

HOLC loans represented a substantial risk to the government, but one with the possibility of a profit. If a HOLC borrower defaulted, the government stood to lose a considerable amount of

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[440] Through October 2010, 1,647,474 trial modifications had been offered; 1,395,543 trial modifications had started; and 519,648 permanent modifications had started. MHA Servicer Performance Report, *supra* note 38, at 2; Data provided by Treasury.

[441] NBER Research Paper, *supra* note 344, at 25.

[442] NBER Research Paper, *supra* note 344, at 25 ("In most areas appraisals were sufficiently generous to permit loans nearly as large—possibly larger—than current market price.").

money in a foreclosure. If the borrower paid off the loan, the government not only got its money back, it made a small profit. HAMP's structure is quite different, with both less potential downside and less potential upside. The government's potential liability for each loan is limited to a series of incentive payments over a five-year period, but it has no opportunity to earn any of that money back.

7. Data Availability

The HOLC closed its doors in 1951, prior to the popularization of computers. The HOLC therefore relied on employees using paper to collect data about borrowers and loans, a process that was inefficient, time-consuming, and inaccurate by today's standards. One important advantage that HAMP has over the HOLC is the availability of tools to collect and analyze vast quantities of data. These tools should allow Treasury and outside observers to gain a better understanding of what is working and what is not working in HAMP, in a way that was not possible during the 1930s and 1940s.

D. Lessons From the HOLC

In the context of today's foreclosure crisis, the size and breadth of the HOLC's work is striking. The HOLC bought up 10 percent of the residential mortgages in the United States; it hired 20,000 employees at a time when the U.S. population was only about 40 percent of today's population; and by amortizing and extending mortgages, it reshaped the mortgage contract in a fundamental way. This is not to say that a comparably large government intervention would be appropriate in the present-day situation. Indeed, the need for relief was substantially greater during the 1930s than it is today. And the scale of the present-day U.S. foreclosure problem will depend in large part on the future trajectory of home prices.

It is at least arguable that the residential mortgage market of the 1920s—which in some ways resembles the market for construction loans today—offered a better opportunity for government intervention than today's residential mortgage market. Because many homeowners with mortgages from the 1920s were not building equity, they had little incentive to continue making payments when the price of their homes plummeted. By adjusting home values to more realistic levels, and by giving homeowners a chance to build equity, the HOLC gave homeowners much more reason to try to stay in their homes. On the other hand, certain reckless mortgage products in the 2000s, such as interest-only loans and negatively amortizing loans with rate resets, do offer low-hanging fruit for the government. Indeed, these are the kinds of loans that HAMP was designed to address.

Lastly, the HOLC's servicing practices, which involved extraordinary efforts by the government to avoid foreclosures, shed light on some of the problems that HAMP has encountered. Whereas the HOLC was a purely governmental effort, HAMP, by its design, relies on private servicers to carry out public-policy aims. This creates a principal-agent problem—there may be a divergence of interests between Treasury and the servicers it is paying—which could be problematic even if HAMP were a mandatory program. Unfortunately, the voluntary nature of HAMP exacerbates the problem, because Treasury has few tools available to ensure that servicers fulfill their obligations under the program. As was described earlier in the report, if Treasury enforces the servicers' contractual obligations more stringently, the servicers may have the option of simply dropping out of the program.

SECTION TWO: ADDITIONAL VIEWS

A. J. Mark McWatters and Professor Kenneth Troske

We concur with the issuance of the December report and offer the additional observations below. We appreciate the efforts the Panel staff made incorporating our suggestions offered during the drafting of the report.

The issue discussed in this month's report—foreclosures and the government's efforts to help keep families in their homes—remain quite contentious and fraught with strong feelings among people debating this issue. However, when considering the effectiveness of programs designed to mitigate foreclosures, it is important to keep in mind that one of our primary goals should be returning the economy to a place where it can begin to grow at a pace that helps everyone currently in distress.

Certainly all of us would like to return to a world where we have steadily rising housing prices, low unemployment rates, and an economy that is growing at 4 percent to 5 percent per year. However, this is not the world in which we currently live. Instead, we are in an economy where housing prices nationwide have fallen by 14 percent from their peak,[443] where prices in the largest metropolitan areas have fallen by almost one-third,[444] and annual existing home sales have plunged by over 40 percent.[445] Without a doubt, the housing market has been in disequilibrium for several years, even before the recent discoveries of problems with foreclosures. The important question is what are the best policies for helping the housing market return to stability? Because until we achieve stability in the housing market, the economy will continue to limp along at 1 percent to 2 percent growth per year and unemployment will remain unacceptably high.

One of the main problems with the housing market is that in 2005 and 2006 many people borrowed money to purchase houses, or took out home-equity loans, predicated on the belief that housing prices would continue rising. It is important to note that few of these borrowers were first-time home buyers. Instead these were people who had a mortgage and decided to refinance in order to extract some of the equity they had built up in their house to purchase other goods. As long as home values kept rising, homeowners and other investors could refinance these loans at lower rates based on the accumulation of equity. When housing prices started to decline in 2006, many of these people were left with mortgages where the amount they owed was less than the value of the home. The question is, what if anything should the government do to fix this problem?

As we point out in the report, the Administration's foreclosure mitigation programs—primarily HAMP—have failed to provide meaningful relief to distressed homeowners and, disappointingly,

[443] Federal Housing Finance Agency, *U.S. and Census Division Monthly Purchase Only Index* (Instrument: USA, Seasonally Adjusted) (online at www.fhfa.gov/Default.aspx?Page=87) (accessed Dec. 10, 2010) (hereinafter "U.S. and Census Division Monthly Purchase Only Index").

[444] Standard and Poor's, *S&P/Case-Shiller Home Price Indices* (Instrument: Case-Shiller 20-City Composite Seasonally Adjusted, Frequency: Monthly) (online at www.standardandpoors.com/ indices/sp-case-shiller-home-price-indices/en/us/?indexId=spusa-cashpidff__p-us__) (accessed Dec. 10, 2010) (hereinafter "S&P/Case-Shiller Home Price Indices").

[445] Data accessed through Bloomberg Data Service (Dec. 10, 2010).

the Administration has inadvertently created a sense of false expectations among millions of homeowners who reasonably anticipated that they would have the opportunity to modify or refinance their troubled mortgage loans under HAMP. In our view, the primary reason for HAMP's lack of success lies in the confusing and illogical basis for the program. Under HAMP, the government pays lenders and borrowers to modify a mortgage only when the estimated value of the modified mortgage (estimated using a procedure specified by the government) exceeds the estimated value of the foreclosed loan (again estimated using government rules). In short, under HAMP, Treasury is planning on paying $30 billion to lenders and borrowers to do something that they should be willing to do without receiving any money from the government. The fact that a program which should be an unmitigated success—paying people money for nothing—has had such limited success should be a clue that the situation is far more complicated then it appears.

To begin with, the structure of HAMP indicates that it is likely to have only limited success. HAMP works by reducing the monthly mortgage payments of borrowers through a capitalization of arrearages, a term extension, forbearance, and/or a reduction of interest rates or principal for up to five years. Then the program ends and the interest rate will gradually rise to the prevailing rate in place at the time the modification was made. Given the structure of the program, it seems unlikely that borrowers, especially those with negative equity, will be able to keep their homes unless we see dramatic improvements in the housing market, which also seems unlikely. The median borrower in the program had monthly debt payments equal to 80 percent of their pre-tax income.[446] On an after-tax basis, even after all the modifications have been done, after making their new monthly mortgage payment and all the other payments to lenders, the typical HAMP participant has $444 per month left over for expenses such as food, clothing, and health care, so it is hard to imagine how any modification is going to be successful.[447] Additionally, instead of being directed at borrowers who are in trouble because of some sudden, unexpected occurrence, such as losing a job or having the value of their home fall below the balance of their mortgage, this program is primarily focused on borrowers who can't make their monthly payments even though they are currently employed and not under water. This despite evidence from researchers at the Federal Reserve Banks of Atlanta and Boston showing that helping workers who have experienced temporary shocks is much more likely to result in those owners keeping their homes.[448]

There are also a myriad of details and rules that limit the ability and/or willingness of lenders to modify loans. For example, for loans in which there are multiple liens, if the first lien holder modifies the loan without reaching an agreement with the other lien holders, then the first lien holder might have to take a subordinated position to the other lien holders. Given that over 40 percent of current mortgages have two or more liens; this significantly

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[446] Data provided by Treasury.
[447] *See* footnote 52 *supra,* for further discussion of after-tax debt-to-income ratios.
[448] Federal Reserve Bank of Atlanta Working Paper, *supra* note 88.

increases the cost of modifying a mortgage.[449] In addition, since a lender must recognize losses once a loan is modified, for banks holding a large number of underwater mortgages, this has the potential to impose a significant financial strain on the institution, a strain they will try to avoid.

We are also troubled that HAMP itself may have exacerbated the mortgage loan delinquency and foreclosure problem by encouraging homeowners to refrain from remitting their monthly mortgage installments based upon the expectation that they would ultimately receive a favorable restructure or principal reduction subsidized by the taxpayers. The curious incentives offered by HAMP arguably converts the concept of home ownership into the economic equivalent of a "put option"—as long as a homeowner's residence continues to appreciate in value, the homeowner will not exercise the put option, but as soon as the residence falls in value, the homeowner will elect to exercise the put option and walk away—or threaten to walk away—if a favorable bailout is not offered.

We remain unconvinced that government-sponsored foreclosure mitigation programs are necessarily capable of lifting millions of American families out of their underwater home mortgage loans. From our perspective, the best foreclosure mitigation tool is a steady job at a fair wage and not a hodgepodge of government-subsidized programs that create and perpetuate moral hazard risks and all but establish the government as the implicit guarantor of distressed homeowners. In the end it appears that, for most participants, HAMP will only postpone the inevitable.

So, what would be the downside if all HAMP does is postpone foreclosures for a few years? Well, as one of us has pointed out in an earlier Panel report,[450] despite all the attention they have received, homeowners with unaffordable mortgages were not the only group hurt by the financial crisis. Millions of homeowners who didn't have mortgages or who had affordable mortgages saw the value of their home plummet, and this was devastating for those who were going to use the equity in their home to finance their retirement. Millions of others saw the value of their retirement savings decline significantly, and families lost substantial amounts in their children's college savings accounts. For all of these people, relief will only come once the economy starts growing again. That growth will only occur once the housing market has stabilized, and that stability will not develop until people move out of homes with mortgages they cannot afford and into housing they can afford. So to the extent that HAMP simply kicks the foreclosure can down the road, it ends up hurting all of the people who are desperate for the economy to start growing again so that their lives can return to normal.

HAMP carries a 100 percent subsidy rate according to the Congressional Budget Office (CBO).[451] This means that the U.S. government expects to recover *none* of the $30 billion of taxpayer-sourced TARP funds invested in HAMP. Since Treasury is charged

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[449] Amherst Securities Group LP, Amherst Mortgage Insight, *2nd Liens—How Important,* at 3 (Jan. 29, 2010).

[450] April 2010 Oversight Report, *supra* note 1, at 179–180 (from the additional views of J. Mark McWatters).

[451] CBO Report on the TARP—November 2010, *supra* note 113, at 7.

with protecting the interests of the taxpayers who fund HAMP and the other TARP programs, we recommend that Treasury's foreclosure mitigation efforts be structured so as to incorporate an effective exit strategy by allowing Treasury to participate in any subsequent appreciation in the home equity of any mortgagor whose loan is modified under HAMP or any other taxpayer-subsidized program. An equity appreciation right—the functional equivalent of a warrant in a non-commercial transaction—will also mitigate the moral hazard risk of homeowners who may undertake risky loans in the future based on the assumption that the government will act as a backstop with no strings attached.

This analysis is in no way intended to diminish the financial hardship that many Americans are suffering as they attempt to modify or refinance their underwater home mortgage loans, and we fully acknowledge and empathize with the stress and economic uncertainty created from the bursting of the housing bubble. It is particularly frustrating—although not surprising—that many of the hardest hit housing markets are also suffering from seemingly intractable rates of unemployment and underemployment. We also recognize that there have been serious mistakes, and perhaps fraud, committed by servicers and lenders in the lending and foreclosure process, and any illegal activity on the part of banks needs to be fully prosecuted. In addition, we know that many homeowners are rightfully frustrated and angry over the treatment they have received by lenders and servicers once they begin to experience financial distress. As such, we encourage each mortgage loan and securitized debt investor and servicer to work with each of their borrowers in a good faith, transparent, and accountable manner to reach an economically reasonable resolution prior to pursuing foreclosure. In our view, foreclosure should serve as the exception to the rule that only follows from the transparent and objective failure of the parties to modify or refinance a troubled mortgage loan pursuant to market-based terms. It is regrettable that HAMP creates disincentives for investors and servicers as well as homeowners by rewarding their dilatory and inefficient behavior with the expectation of enhanced taxpayer-funded subsidies. Since any intermediate to long-term resolution of the housing crisis must reside substantially with the private sector lenders and investors who hold the mortgage notes and liens, instead of spending an additional $30 billion on a government-sponsored foreclosure mitigation effort, we believe Treasury would be best served by strongly encouraging these participants to engage in good faith, market-based negotiations with their distressed borrowers. In our opinion, this is the best way to bring stability to the housing market so that the economy can start growing again.

SECTION THREE: CORRESPONDENCE WITH TREASURY

Patricia Geoghegan, the Special Master for TARP Executive Compensation, sent a letter to Senator Ted Kaufman, the Panel's Chairman, on November 18, 2010.[452] The letter responds to a series of questions presented by the Panel seeking additional information about TARP executive compensation restrictions following the Panel's October 21, 2010 hearing on the topic.[453]

[452] See Appendix I, *infra*.
[453] See Appendix I of the Panel's November 2010 Oversight Report, *supra* note 79, at 125.

SECTION FOUR: TARP UPDATES SINCE LAST REPORT

A. GM IPO

General Motors held an initial public offering on November 18, 2010, after three quarters of posting profit. Treasury received $11.7 billion in net proceeds on November 23 for the sale of 358,546,795 shares of common stock. As widely expected, underwriters exercised their over-allotment option, and on December 2, Treasury received $1.8 billion in net proceeds from the sale of 53,782,019 additional shares of common stock. In total, these sales reduced Treasury's share of GM's outstanding common stock from 60.8 percent to 33.3 percent. Treasury's remaining stock in General Motors consists of 500,065,254 shares of common stock. Treasury's total receipt from the IPO was $13.5 billion.

B. Stress-Tested Banks

The Federal Reserve has requested that bank holding companies that participated in the Supervisory Capital Assessment Program (SCAP) consult with Federal Reserve staff before taking actions that could result in a diminished capital base, such as increasing dividends, repurchasing common stock, and other planned capital actions. Stress-tested BHCs have been requested to file a Comprehensive Capital Plan by January 7, 2011. This plan should incorporate a stress-testing framework that will estimate potential capital needs under a range of circumstances from normal to very severe. The Federal Reserve will use this and supervisory actions, in addition to firms' risk profiles, in order to assess the BHC's capital adequacy. Stress-tested BHCs are expected to complete reimbursement of U.S. government investment before undertaking any other capital actions. Five SCAP institutions—Fifth Third Bancorp, SunTrust, Regions Financial, KeyCorp, and GMAC/Ally Financial—have yet to repay their TARP assistance.

C. Citigroup Stock Sale

Treasury announced on December 6, 2010 that it was commencing an underwritten public offering of approximately 2.4 billion shares of Citigroup Inc. common stock. Treasury converted its common shares at $3.25 per share in July 2009 and the stock was sold to investors at $4.35 on December 6, 2010, which will result in an estimated profit of $2.64 billion. This offering will dispose of Treasury's remaining shares of Citigroup common stock, although Treasury will still hold warrants and be entitled to receive up to $800 million of CitigroupTrust Preferred securities from the FDIC. As of the time of the writing of this report, the sale has not officially closed, and thus the Panel has not incorporated the results of this sale in this month's financial update section.

D. Metrics

Each month, the Panel's report highlights a number of metrics that the Panel and others, including Treasury, the Government Accountability Office (GAO), Special Inspector General for the Troubled Asset Relief Program (SIGTARP), and the Financial Stability

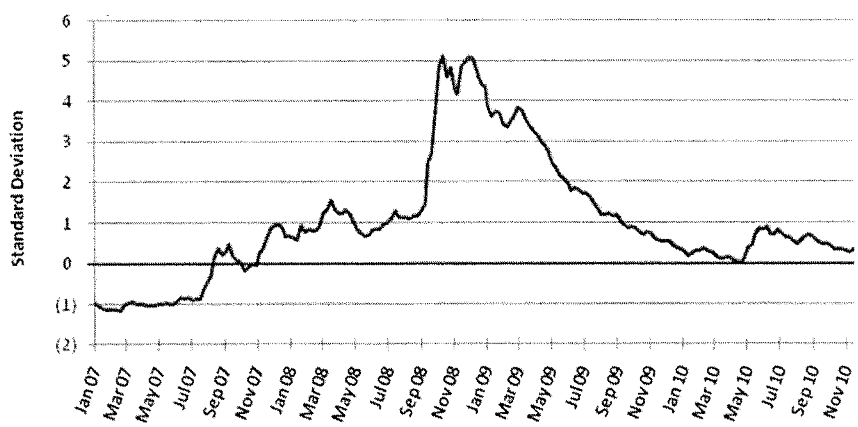
Oversight Board, consider useful in assessing the effectiveness of the Administration's efforts to restore financial stability and accomplish the goals of EESA. This section discusses changes that have occurred in several indicators since the release of the Panel's November 2010 report.

1. Financial Indices

a. Overview

The St. Louis Financial Stress Index, a proxy for financial stress in the U.S. economy, has remained relatively stable since the Panel's November report.[454] The index has decreased more than 60 percent since its post-crisis peak in June 2010. The recent trend in the index suggests that financial stress continues moving toward its long-run norm. The index has decreased by more than three standard deviations since EESA was enacted in October 2008.

FIGURE 34: ST. LOUIS FEDERAL RESERVE FINANCIAL STRESS INDEX

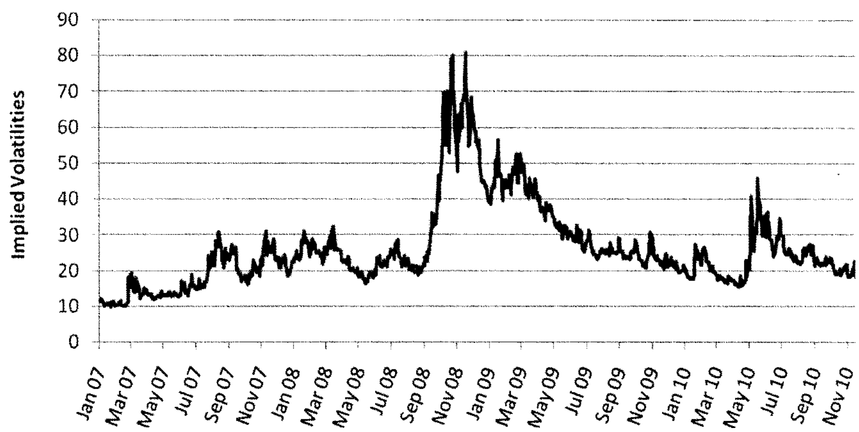


Stock market volatility, as measured by the Chicago Board Options Exchange Volatility Index (VIX), continues to decrease. The VIX has fallen by more than half since the post-crisis peak in May 2010 and has decreased 4 percent since the Panel's November re-

[454] Federal Reserve Bank of St. Louis, *Series STLFSI: Business/Fiscal: Other Economic Indicators* (Instrument: St. Louis Financial Stress Index, Frequency: Weekly) (online at research.stlouisfed.org/fred2/series/STLFSI) (accessed Dec. 1, 2010). The index includes 18 weekly data series, beginning in December 1993 to the present. The series are: effective federal funds rate, 2-year Treasury, 10-year Treasury, 30-year-Treasury, Baa-rated corporate, Merrill Lynch High Yield Corporate Master II Index, Merrill Lynch Asset-Backed Master BBB-rated, 10-year Treasury minus 3-month Treasury, Corporate Baa-rated bond minus 10-year Treasury, Merrill Lynch High Yield Corporate Master II Index minus 10-year Treasury, 3-month LIBOR–OIS spread, 3-month TED spread, 3-month commercial paper minus 3-month Treasury, the J.P. Morgan Emerging Markets Bond Index Plus, Chicago Board Options Exchange Market Volatility Index, Merrill Lynch Bond Market Volatility Index (1-month), 10-year nominal Treasury yield minus 10-year Treasury Inflation Protected Security yield, and Vanguard Financials Exchange-Traded Fund (equities). The index is constructed using principal components analysis after the data series are de-meaned and divided by their respective standard deviations to make them comparable units. The standard deviation of the index is set to 1. For more details on the construction of this index, *see* Federal Reserve Bank of St. Louis, *National Economic Trends Appendix: The St. Louis Fed's Financial Stress Index* (Jan. 2010) (online at research.stlouisfed.org/publications/net/NETJan2010Appendix.pdf).

port. However, as of December 1, 2010, volatility was 35 percent higher than its post-crisis low on April 12, 2010.

FIGURE 35: CHICAGO BOARD OPTIONS EXCHANGE VOLATILITY INDEX [455]



b. Interest Rates, Spreads, and Issuance

As of December 1, 2010, the 3-month and 1-month London Interbank Offer Rates (LIBOR), the prices at which banks lend and borrow from each other, were 0.30 and 0.27, respectively.[456] Rates have increased slightly since the Panel's November report. However, the 3-month and 1-month LIBOR remain below their post-crisis highs in June 2010. Over the longer term, however, interest rates remain extremely low relative to pre-crisis levels, reflecting the impact of the actions of central banks and institutions' perceptions of reduced risk in lending to other banks.

FIGURE 36: 3-MONTH AND 1-MONTH LIBOR RATES (AS OF DECEMBER 1, 2010)

Indicator	Current Rates	Percent Change From Data Available at Time of Last Report (11/3/2010)
3-Month LIBOR [457]	0.30	3.4
1-Month LIBOR [458]	0.27	8.0

[457] Data accessed through Bloomberg data service (Dec. 1, 2010).
[458] Data accessed through Bloomberg data service (Dec. 1, 2010).

As of December 1, 2010, the conventional mortgage rate spread, which measures the difference between 30-year mortgage rates and 10-year Treasury bond yields, remained unchanged since the Panel's November report.[459] The TED spread, which captures the dif-

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[455] Data accessed through Bloomberg data service (Dec. 1, 2010). The CBOE VIX is a key measure of market expectations of near-term volatility. Chicago Board Options Exchange, *The CBOE Volatility Index—VIX,* 2009 (online at www.cboe.com/micro/vix/vixwhite.pdf) (accessed Dec. 1, 2010).

[456] Data accessed through Bloomberg data service (Dec. 1, 2010).

[459] Board of Governors of the Federal Reserve System, *Federal Reserve Statistical Release H.15: Selected Interest Rates: Historical Data* (Instrument: Conventional Mortgages, Frequency: Weekly) (online at www.federalreserve.gov/releases/h15/data/Weekly_Thursday_/H15_MORTG_NA.txt) (accessed Dec. 1, 2010) (hereinafter "Federal Reserve Statistical Release H.15").

ference between the 3-month LIBOR and the 3-month Treasury bill rates, serves as an indicator for perceived risk in the financial markets.[460] As of December 1, 2010, the spread was 14.3 basis points, declining approximately two basis points in November. As shown in Figure 37 below, the spread remains below pre-crisis levels.

The LIBOR–OIS (Overnight Index Swap) spread serves as an indicator of the health of the banking system, as it reflects what banks believe to be the risk of default associated with interbank lending.[461] The spread increased over threefold from early April to July, before falling in mid-July.[462] Decreases in the LIBOR–OIS spread and the TED spread suggest that hesitation among banks to lend to counterparties has receded. The LIBOR–OIS spread remained fairly constant since the Panel's November report, averaging approximately 11 basis points during the month.

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[460] Federal Reserve Bank of Minneapolis, *Measuring Perceived Risk—The TED Spread* (Dec. 2008) (online at www.minneapolisfed.org/publications_papers/pub_display.cfm?id=4120).

[461] Federal Reserve Bank of St. Louis, *What the LIBOR–OIS Spread Says* (May 11, 2009) (online at research.stlouisfed.org/publications/es/09/ES0924.pdf).

[462] Data accessed through Bloomberg data service (Dec. 1, 2010).

FIGURE 37: TED SPREAD[463]

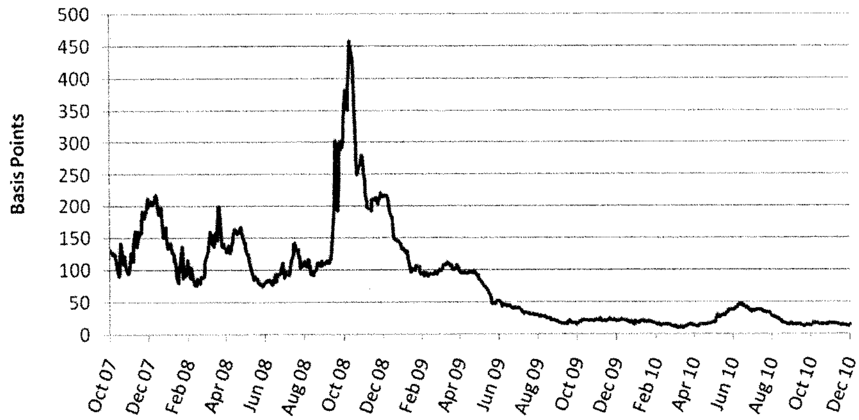
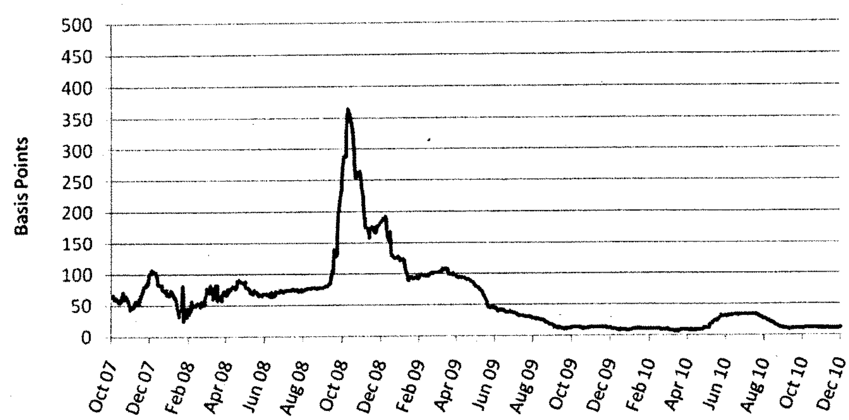


FIGURE 38: LIBOR–OIS SPREAD[464]



The interest rate spread for AA asset-backed commercial paper, which is considered mid-investment grade, decreased by more than five percent since the Panel's November report. The interest rate spread on A2/P2 commercial paper, a lower grade investment than AA asset-backed commercial paper, fell by approximately 10 percent. These declining spreads indicate healthier fundraising conditions for corporations.

[463] Data accessed through Bloomberg data service (Dec. 1, 2010).
[464] Data accessed through Bloomberg data service on (Dec. 1, 2010).

FIGURE 39: INTEREST RATE SPREADS (AS OF DECEMBER 1, 2010)

Indicator	Current Spread	Percent Change Since Last Report (11/1/2010)
Conventional mortgage rate spread [465]	1.56	0.0
TED Spread (basis points)	14.34	(8.0)
Overnight AA asset-backed commercial paper interest rate spread [466]	0.07	(5.4)
Overnight A2/P2 nonfinancial commercial paper interest rate spread [467]	0.12	(10.1)

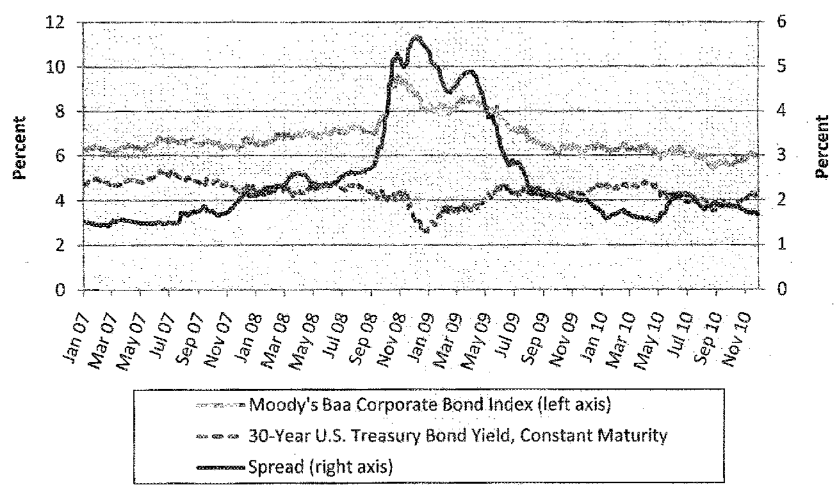
[465] Federal Reserve Statistical Release H.15, *supra* note 459; Board of Governors of the Federal Reserve System, *Federal Reserve Statistical Release H.15: Selected Interest Rates: Historical Data* (Instrument: U.S. Government Securities/Treasury Constant Maturities/Nominal 10–Year, Frequency: Weekly) (online at www.federal reserve.gov/releases/h15/data/Weekly_Friday_/H15_ TCMNOM_Y10.txt) (accessed Dec. 1, 2010).

[466] The overnight AA asset-backed commercial paper interest rate spread reflects the difference between AA asset-backed commercial paper discount rate and the AA nonfinancial commercial paper discount rate. Board of Governors of the Federal Reserve System, *Federal Reserve Statistical Release: Commercial Paper Rates and Outstandings: Data Download Program* (Instrument: AA Asset-Backed Discount Rate, Frequency: Daily) (online at www.federalreserve.gov/DataDownload/Choose.aspx?rel=CP) (accessed Dec. 1, 2010); Board of Governors of the Federal Reserve System, *Federal Reserve Statistical Release: Commercial Paper Rates and Outstandings: Data Download Program* (Instrument: AA Nonfinancial Discount Rate, Frequency: Daily) (online at www.federalreserve.gov/DataDownload/Choose.aspx?rel=CP) (accessed Dec. 1, 2010). In order to provide a more complete comparison, this metric utilizes the average of the interest rate spread for the last five days of the month.

[467] The overnight A2/P2 nonfinancial commercial paper interest rate spread reflects the difference between A2/P2 nonfinancial commercial paper discount rate and the AA nonfinancial commercial paper discount rate. Board of Governors of the Federal Reserve System, *Federal Reserve Statistical Release: Commercial Paper Rates and Outstandings: Data Download Program* (Instrument: A2/P2 Nonfinancial Discount Rate, Frequency: Daily) (online at www.federalreserve.gov/DataDownload/Choose.aspx?rel=CP) (accessed Dec. 1, 2010); Board of Governors of the Federal Reserve System, *Federal Reserve Statistical Release: Commercial Paper Rates and Outstandings: Data Download Program* (Instrument: AA Nonfinancial Discount Rate, Frequency: Daily) (online at www.federalreserve.gov/DataDownload/Choose.aspx?rel=CP) (accessed Dec. 1, 2010). In order to provide a more complete comparison, this metric utilizes the average of the interest rate spread for the last five days of the month.

The spread between Moody's Baa Corporate Bond Yield Index and 30-year constant maturity U.S. Treasury Bond, which indicates the difference in perceived risk between corporate and government bonds, doubled from late April to mid-June 2010. During November, the spread declined over 5 percent, and has decreased 22 percent since its post-crisis peak in mid-June. The declining spread could indicate waning concerns about the riskiness of corporate bonds.

FIGURE 40: MOODY'S BAA CORPORATE BOND INDEX AND 30-YEAR U.S. TREASURY YIELD [468]

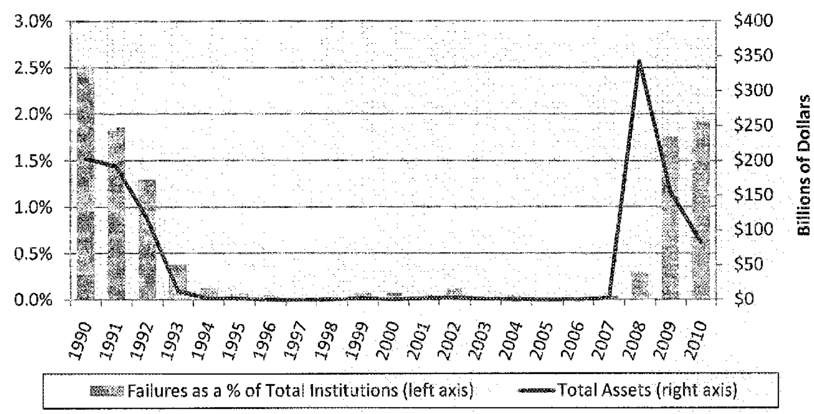


[468] Federal Reserve Bank of St. Louis, *Series DGS30: Selected Interest Rates* (Instrument: 30–Year Treasury Constant Maturity Rate, Frequency: Daily) (online at research.stlouisfed.org/fred2/) (accessed Dec. 1, 2010) (hereinafter "Series DGS30: Selected Interest Rates"). Corporate Baa rate data accessed through Bloomberg data service (Dec. 1, 2010).

c. Condition of the Banks

During November, year-to-date bank failures surpassed the 2009 level of 140 failures. As of November 25, 2010, 149 banks have been placed into receivership. Despite exceeding the total number of bank failures in 2009, banks that have failed in 2010 thus far had $90.5 billion in total assets, which represents only half of the total assets of failed institutions in 2009.[469] Most failures in 2010 involved institutions with less than $10 billion in assets. Of the 10 banks that failed in November, two were CPP recipients.

FIGURE 41: BANK FAILURES AS A PERCENTAGE OF TOTAL BANKS AND BANK FAILURES BY TOTAL ASSETS (1990–2010) [470]



2. Unemployment and Underemployment

The unemployment rate increased in November to 9.8 percent after three consecutive months at 9.6 percent, while the underemployment rate remained unchanged at 17.0 percent. The median duration of unemployment increased by approximately half a week, to 21.6 weeks, in November.

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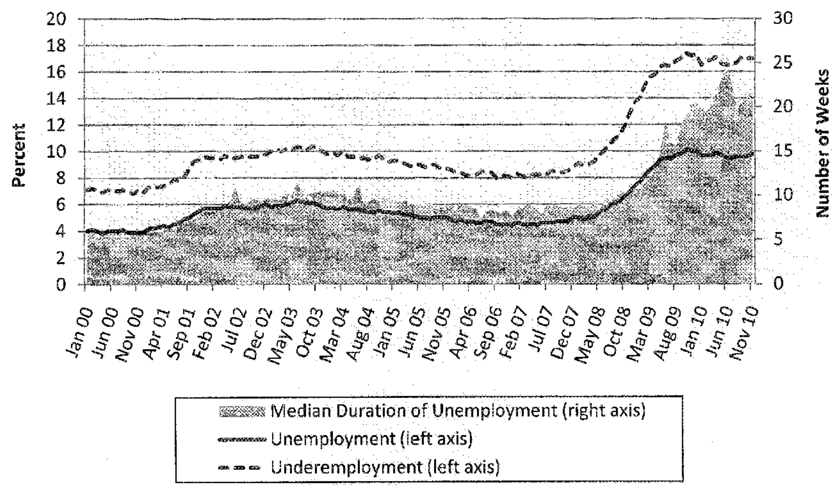
[469] Federal Deposit Insurance Corporation, *Failures & Assistance Transactions* (online at www2.fdic.gov/hsob/SelectRpt.asp?EntryTyp=30) (accessed Dec. 1, 2010) (hereinafter "Failures & Assistance Transactions").

[470] The disparity between the number of and total assets of failed banks in 2008 is driven primarily by the failure of Washington Mutual Bank, which held $307 billion in assets. The 2010 year-to-date percentage of bank failures includes failures through November. The total number of FDIC-insured institutions as of September 30, 2010 is 7,760 commercial banks and savings institutions, which represents a decline of 70 institutions since June 30, 2010. Failures & Assistance Transactions, *supra* note 469; Federal Deposit Insurance Corporation, *Quarterly Banking Profile, Third Quarter 2010: Statistics At A Glance* (online at www.fdic.gov/bank/statistical/stats/2010sep/industry.pdf) (accessed Dec. 10, 2010). Asset totals have been adjusted for deflation into 2005 dollars using the GDP implicit price deflator. The quarterly values were averaged into a yearly value. Series DGS30: Selected Interest Rates, *supra* note 468.

FIGURE 42: UNEMPLOYMENT, UNDEREMPLOYMENT, AND MEDIAN DURATION OF UNEMPLOYMENT[471]

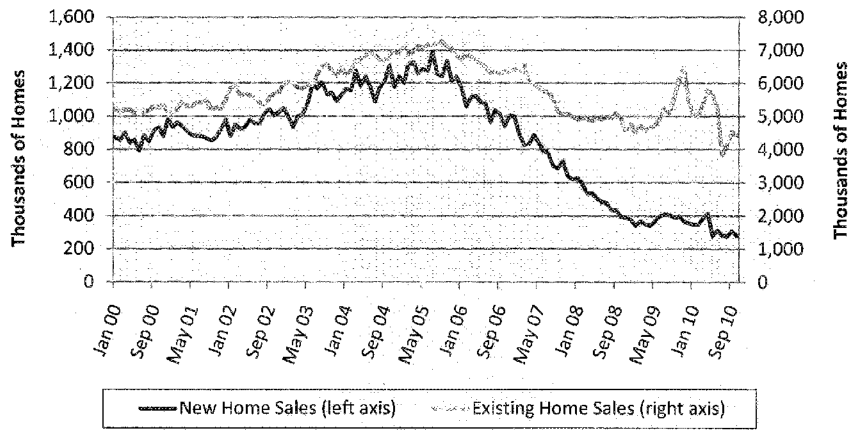


3. Housing Indices

New home sales saw a month-over-month decrease in October, declining 8 percent during the month. New home sales as measured by the U.S. Census Bureau totaled 283,000 units. With respect to existing home sales, National Association of Realtors estimates a 2 percent month-over-month decline in October, to 4.4 million homes sold. Although existing home sales in October remained below the 10-year historical average, current levels are above the July 2010 level, when existing home sales reached their lowest point in more than a decade.

[471] It is important to note that the measures of unemployment and underemployment do not include people who have stopped actively looking for work altogether. While the Bureau of Labor Statistics (BLS) does not have a distinct metric for "underemployment," the U–6 category of Table A–15 "Alternative Measures of Labor Underutilization" is used here as a proxy. BLS defines this measure as: "Total unemployed, plus all persons marginally attached to the labor force, plus total employed part time for economic reasons, as a percent of the civilian labor force plus all persons marginally attached to the labor force." U.S. Department of Labor, *International Comparisons of Annual Labor Force Statistics* (online at www.bls.gov/webapps/legacy/cpsatab15.htm) (accessed Dec. 3, 2010); Series DGS30: Selected Interest Rates, *supra* note 468.

FIGURE 43: NEW AND EXISTING HOME SALES (2000–2010) [472]



Foreclosure actions, which consist of default notices, scheduled auctions, and bank repossessions, increased 4.4 percent in October to 332,172.[473] Since the enactment of EESA, there have been approximately 8.1 million foreclosure filings.[474] Both the Case-Shiller Composite 20–City Composite Home Price Index and the FHFA Housing Price Index decreased approximately 1 percent in September 2010. The Case-Shiller and FHFA indices are 7 percent and 6 percent, respectively, below their October 2008 levels.[475]

Case-Shiller futures prices indicate a market expectation that home-price values for the major Metropolitan Statistical Areas (MSAs) will decrease through 2011.[476] These futures are cash-set-

[472] Data accessed through Bloomberg Data Service (Dec. 1, 2010). Spikes in both new and existing home sales in January 2009 and November 2009 correlate with the tax credits extended to first-time and repeat home buyers during these periods. After both tax credits were extinguished on April 30, 2010, existing home sales dropped to 3.8 million homes in July, their lowest level in a decade. National Association of Realtors, *July Existing-Home Sales Fall as Expected but Prices Rise* (Aug. 24, 2010) (online at www.realtor.org/press_room/news_releases/2010/08/ehs_fall).

[473] RealtyTrac, *Foreclosure Activity Decreases 4 Percent in October* (Nov. 11, 2010) (online at www.realtytrac.com/content/press-releases/foreclosure-activity-decreases-4-percent-in-october-6182) (hereinafter "Foreclosure Activity Decreases 4 Percent in October").

[474] Data accessed through Bloomberg data service (Dec. 1, 2010).

[475] The most recent data available are for September 2010. *See* S&P/Case-Shiller Home Price Indices, *supra* note 444; U.S. and Census Division Monthly Purchase Only Index, *supra* note 443. S&P has cautioned that the seasonal adjustment is probably being distorted by irregular factors. These factors could include distressed sales and the various government programs. *See* Standard and Poor's, *S&P/Case-Shiller Home Price Indices and Seasonal Adjustment* (Apr. 2010) (online at www.standardandpoors. com/ servlet/ BlobServer?blobheadername3= MDT–Type&blobcol=urldata&blobtable= MungoBlobs&blobheadervalue2= inline;+filename%3DCase Shiller_SeasonalAdjustment2,0.pdf&blobheadername2=Content- Disposition&blobheadervalue1= application/pdf&blobkey=id&blobheadername1=content-type&blobwhere=1243679046081&blobheadervalue3=UTF–8). For a discussion of the differences between the Case-Shiller Index and the FHFA Index, *see* April 2010 Oversight Report, *supra* note 1, at 98.

[476] Data accessed through Bloomberg data service on December 1, 2010. The Case-Shiller Futures contract is traded on the Chicago Mercantile Exchange (CME) and is settled to the Case-Shiller Index two months after the previous calendar quarter. For example, the February contract will be settled against the spot value of the S&P Case-Shiller Home Price Index values representing the fourth calendar quarter of the previous year, which is released in February one day after the settlement of the contract. Note that most close observers believe that the accuracy of these futures contracts as forecasts diminishes the farther out one looks.

A Metropolitan Statistical Area is defined as a core area containing a substantial population nucleus, together with adjacent communities having a high degree of economic and social inte-

Continued

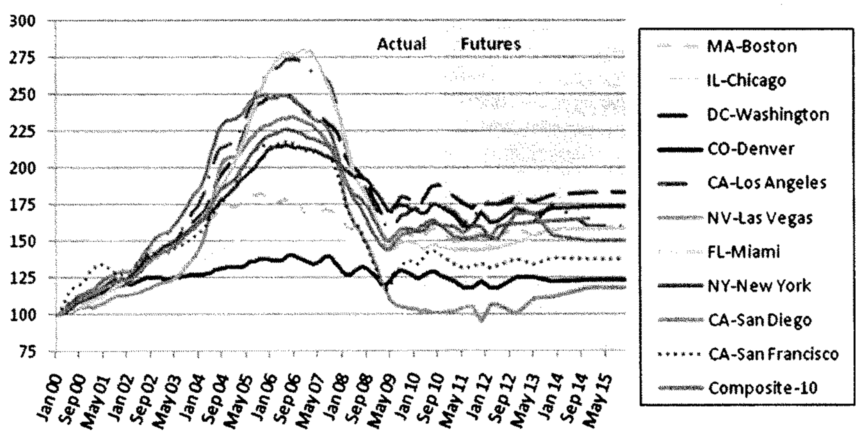
tled to a weighted composite index of U.S. housing prices in the top 10 MSAs, as well as to those specific markets. They are used to hedge by businesses whose profits and losses are related to any area of the housing industry, and to balance portfolios by businesses seeking exposure to an uncorrelated asset class. As such, futures prices are a composite indicator of market information known to date and can be used to indicate market expectations for home prices.

FIGURE 44: HOUSING INDICATORS

Indicator	Most Recent Monthly Data	Percent Change from Data Available at Time of Last Report	Percent Change Since October 2008
Monthly foreclosure actions [477]	332,172	(4.4)	18.8
S&P/Case-Shiller Composite 20 Index [478]	145.47	(1.0)	(6.9)
FHFA Housing Price Index [479]	190.47	(1.2)	(5.7)

[477] Foreclosure Activity Decreases 4 Percent in October, *supra* note 473. The most recent data available are for October 2010.
[478] S&P/Case-Shiller Home Price Indices, *supra* note 444. The most recent data available are for September 2010.
[479] U.S. and Census Division Monthly Purchase Only Index, *supra* note 443. The most recent data available are for September 2010.

FIGURE 45: CASE-SHILLER HOME PRICE INDEX AND FUTURES VALUES [480]



E. Financial Update

Each month, the Panel summarizes the resources that the federal government has committed to the rescue and recovery of the financial system. The following financial update provides: (1) an updated accounting of the TARP, including a tally of dividend income, repayments, and warrant dispositions that the program has received as of October 31, 2010; and (2) an updated accounting of the full federal resource commitment as of November 26, 2010.

gration with the core. U.S. Census Bureau, *About Metropolitan and Micropolitan Statistical Areas* (online at www.census.gov/population/www/metroareas/aboutmetro.html) (accessed Dec. 10, 2010).

[480] All data normalized to 100 at January 2000. Futures data accessed through Bloomberg data service on December 1, 2010. S&P/Case-Shiller Home Price Indices, *supra* note 444.

1. The TARP

a. Program Updates [481]

Treasury's spending authority under the TARP officially expired on October 3, 2010. Though it can no longer make new funding commitments, Treasury can continue to provide funding for programs for which it has existing contracts and previous commitments. To date, $395.1 billion has been spent under the TARP's $475 billion ceiling.[482] Of the total amount disbursed, $223.0 billion has been repaid. Treasury has also incurred $6.1 billion in losses associated with its CPP and Automotive Industry Financing Program (AIFP) investments. A significant portion of the $166.7 billion in TARP funds currently outstanding relates to Treasury's investments in AIG and assistance provided to the automotive industry.

CPP Repayments

As of November 26, 2010, 114 of the 707 banks that participated in the CPP have fully redeemed their preferred shares either through capital repayment or exchanges for investments under the Community Development Capital Initiative (CDCI). During the month of November, Treasury received an $11.3 million full repayment from Central Jersey Bancorp, a $5.83 million full repayment from Leader Bancorp, Inc. and a $6.25 million partial repayment from Horizon Bancorp. A total of $152.9 billion has been repaid under the program, leaving $49.4 billion in funds currently outstanding.

b. Income: Dividends, Interest, and Warrant Sales

In conjunction with its preferred stock investments under the CPP and the TIP, Treasury generally received warrants to purchase common equity.[483] As of November 26, 2010, 45 institutions have repurchased their warrants from Treasury at an agreed upon price. Treasury has also sold warrants for 15 other institutions at auction. To date, income from warrant dispositions totals $8.1 billion.

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[481] U.S. Department of the Treasury, *Cumulative Dividends, Interest and Distributions Report as of September 30, 2010* (Oct. 11, 2010) (online at financialstability.gov/docs/dividends-interest-reports/September%202010%20Dividends%20&%20Interest%20 Report.pdf) (hereinafter "Cumulative Dividends, Interest and Distributions Report"); U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010* (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf) (hereinafter "Treasury Transactions Report").

[482] The original $700 billion TARP ceiling was reduced by $1.26 billion as part of the Helping Families Save Their Homes Act of 2009. 12 U.S.C. § 5225(a)–(b); *Helping Families Save Their Homes Act of 2009,* Pub. L. No. 111–22 § 202(b) (2009) (online at financialservices.house.gov/FinancialSvcsDemMedia/file/public%20laws/111–22.pdf). On June 30, 2010, the House-Senate Conference Committee agreed to reduce the amount authorized under the TARP from $700 billion to $475 billion as part of the Dodd-Frank Wall Street Reform and Consumer Protection Act that was signed into law on July 21, 2010. *See Dodd-Frank Wall Street Reform and Consumer Protection Act,* Pub. L. No. 111–203 (2010); The White House, *Remarks by the President at Signing of Dodd-Frank Wall Street Reform and Consumer Protection Act* (July 21, 2010) (online at www.whitehouse.gov/the-press-office/remarks-president-signing-dodd-frank-wall-street-reform-and-consumer-protection-act).

[483] For its CPP investments in privately held financial institutions, Treasury also received warrants to purchase additional shares of preferred stock, which it exercised immediately. Similarly, Treasury also received warrants to purchase additional subordinated debt that were also immediately exercised along with its CPP investments in subchapter S corporations. Treasury Transactions Report, *supra* note 481, at 14.

In addition to warrant proceeds, Treasury also receives dividend payments on the preferred shares that it holds under the CPP, 5 percent per annum for the first five years and 9 percent per annum thereafter.[484] For preferred shares issued under the TIP, Treasury received a dividend of 8 percent per annum.[485] In total, Treasury has received approximately $25.8 billion in net income from warrant repurchases, dividends, interest payments, and other proceeds deriving from TARP investments (after deducting losses).[486] For further information on TARP profit and loss, see Figure 46.

c. TARP Accounting

FIGURE 46: TARP ACCOUNTING (AS OF NOVEMBER 26, 2010)

[Dollars in billions][i]

Program	Maximum Amount Allotted	Actual Funding	Total Repayments/ Reduced Exposure	Total Losses	Funding Currently Outstanding	Funding Available
Capital Purchase Program (CPP)	$204.9	$204.9	[ii] $(152.9)	[iii] $(2.6)	$49.5	$0
Targeted Investment Program (TIP)	40.0	40.0	(40.0)	0	0	0
Asset Guarantee Program (AGP)	5.0	[iv] 5.0	[v] (5.0)	0	0	0
AIG Investment Program (AIGIP)	69.8	[vi] 47.5	0	0	47.5	22.3
Auto Industry Financing Program (AIFP)	81.3	81.3	(24.3)	[vii] (3.5)	[viii] 53.6	0
Auto Supplier Support Program (ASSP) [ix]	0.4	0.4	(0.4)	0	0	0
Term Asset-Backed Securities Loan Facility (TALF)	[x] 4.3	[xi] 0.1	0	0	0.1	4.2
Public-Private Investment Program (PPIP) [xii]	22.4	[xiii] 14.9	[xiv] (0.4)	0	14.4	7.5
SBA 7(a) Securities Purchase	0.4	[xv] 0.4	0	0	0.4	[xvi] 0
Home Affordable Modification Program (HAMP)	29.9	0.7	0	0	0.7	29.2
Hardest Hit Fund (HHF)	[xvii] 7.6	[xviii] 0.1	0	0	0.1	7.5
FHA Refinance Program	8.1	[xix] 0.1	0	0	0.1	8.0
Community Development Capital Initiative (CDCI)	0.8	[xx] 0.6	0	0	0.6	0
Total	**$475.0**	**$395.9**	**$(223.0)**	**$(6.0)**	**$167.0**	**$78.8**

[i] Figures affected by rounding. Unless otherwise noted, data in this table are from the following source: U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010* (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

[ii] As of October 29, 2010, Treasury had sold 4.1 billion Citigroup common shares for $16.4 billion in gross proceeds. Amount repaid under CPP includes $13.4 billion Treasury received as part of its sales of Citigroup common stock. The difference between these two numbers represents the $3.0 billion in net profit Treasury has received from the sale of Citigroup common stock. In June 2009, Treasury exchanged $25 billion in Citigroup preferred stock for 7.7 billion shares of the company's common stock at $3.25 per share.

Total CPP repayments also include amounts repaid by institutions that exchanged their CPP investments for investments under the CDCI, as well as proceeds earned from the sale of preferred stock issued by South Financial Group, Inc. and TIB Financial Corp and warrants. *See* U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 2, 13–15 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf); U.S. Department of the Treasury, *Troubled Asset Relief Program: Two-Year Retrospective,* at 25 (Oct. 2010) (online at www.financialstability.gov/docs/TARP%20Two%20Year%20Retrospective_10%2005%2010_transmittal%20letter.pdf); U.S. Department of the Treasury, *Treasury Commences Plan to Sell Citigroup Common Stock* (Apr. 26, 2010) (online at ustreas.tpaq.treasury.gov/press/releases/tg660.htm).

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[484] U.S. Department of the Treasury, *Capital Purchase Program* (Oct. 3, 2010) (online at www. financial stability.gov/ roadtostability/capitalpurchaseprogram.html).

[485] U.S. Department of the Treasury, *Targeted Investment Program* (Oct. 3, 2010) (online at www. financial stability.gov/roadtostability/ targetedinvestmentprogram.html).

[486] Cumulative Dividends, Interest and Distributions Report, *supra* note 481; Treasury Transactions Report, *supra* note 481. Treasury also received an additional $1.2 billion in participation fees from its Guarantee Program for Money Market Funds. U.S. Department of the Treasury, *Treasury Announces Expiration of Guarantee Program for Money Market Funds* (Sept. 18, 2009) (online at www.ustreas.gov/press/releases/tg293.htm).

[iii] On the TARP Transactions Report, Treasury has classified the investments it made in two institutions, CIT Group ($2.3 billion) and Pacific Coast National Bancorp ($4.1 million), as losses. In addition, Treasury sold its preferred ownership interests, along with warrants, in South Financial Group, Inc. and TIB Financial Corp. to non-TARP participating institutions. These shares were sold at prices below the value of the original CPP investment, at respective losses of $217 million and $25 million. Therefore, Treasury's net current CPP investment is $49.5 billion due to the $2.6 billion in losses thus far. *See* U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 13–14 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

[iv] The $5.0 billion AGP guarantee for Citigroup was unused since Treasury was not required to make any guarantee payments during the life of the program. U.S. Department of the Treasury, *Troubled Asset Relief Program: Two-Year Retrospective,* at 31 (Oct. 2010) (online at www.financialstability.gov/docs/TARP%20Two%20Year%20Retrospective_10%2005%2010_transmittal%20letter.pdf); U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 20 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

[v] Although this $5.0 billion is no longer exposed as part of the AGP, Treasury did not receive a repayment in the same sense as with other investments. Treasury did receive other income as consideration for the guarantee, which is not a repayment and is accounted for in Figure 46. *See* U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 20 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

[vi] AIG has completely utilized the $40 billion that was made available on November 25, 2008, in exchange for the company's preferred stock. *See* U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 21 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf). It has also drawn down $7.5 billion of the $29.8 billion made available on April 17, 2009. American International Group, Inc., *Form 10–Q for the Fiscal Year Ended September 30, 2010,* at 119 (Nov. 5, 2010) (online at sec.gov/Archives/edgar/data/5272/000104746910009269/a2200724z10-q.htm). This figure does not include $1.6 billion in accumulated but unpaid dividends owed by AIG to Treasury due to the restructuring of Treasury's investment from cumulative preferred shares to non-cumulative shares. *See* U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 21 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf). AIG expects to draw down up to $22.3 billion in unutilized funds from the TARP as part of its plan to repay the revolving credit facility provided by the Federal Reserve Bank of New York. American International Group, Inc., *AIG Announces Plan to Repay U.S. Government* (Sept. 30, 2010) (online at www.aigcorporate.com/newsroom/2010_September/AIGAnnouncesPlantoRepay30Sept2010.pdf);

[vii] On May 14, 2010, Treasury accepted a $1.9 billion settlement payment for its $3.5 billion loan to Chrysler Holding. The payment represented a $1.6 billion loss from the termination of the debt obligation. *See* U.S. Department of the Treasury, *Chrysler Financial Parent Company Repays $1.9 Billion in Settlement of Original Chrysler Loan* (May 17, 2010) (online at www.financialstability.gov/latest/pr_05172010c.html); U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 18–19 (Nov. 30, 2010) (online at www.financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf). Also, following the bankruptcy proceedings for Old Chrysler, which extinguished the $1.9 billion debtor-in-possession (DIP) loan provided to Old Chrysler, Treasury retained the right to recover the proceeds from the liquidation of specified collateral. Although Treasury does not expect a significant recovery from the liquidation proceeds, Treasury is not yet reporting this loan as a loss in the Transaction Report. To date, Treasury has collected $40.2 million in proceeds from the sale of collateral. Treasury includes these proceeds as part of the $10.8 billion repaid under the AIFP. U.S. Department of the Treasury, *Troubled Assets Relief Program Monthly 105(a) Report—September 2010* (Oct. 12, 2010) (online at financialstability.gov/docs/105CongressionalReports/September 105(a) report_FINAL.pdf); Treasury conversations with Panel staff (Aug. 19, 2010 and Nov. 29, 2010); U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 18 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

[viii] On the TARP Transactions Report, the $1.9 billion Chrysler debtor-in-possession loan, which was extinguished April 30, 2010, was deducted from Treasury's AIFP investment amount. U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 18 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf). *See* endnote vii, *supra,* for details on losses from Treasury's investment in Chrysler.

[ix] On April 5, 2010, Treasury terminated its commitment to lend to the GM SPV under the ASSP. On April 7, 2010, it terminated its commitment to lend to the Chrysler SPV. In total, Treasury received $413 million in repayments from loans provided by this program ($290 million from the GM SPV and $123 million from the Chrysler SPV). Further, Treasury received $101 million in proceeds from additional notes associated with this program. U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 19 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

[x] For the TALF program, $1 of TARP funds was committed for every $10 of funds obligated by the Federal Reserve. The program was intended to be a $200 billion initiative, and the TARP was responsible for the first $20 billion in loan-losses, if any were incurred. The loan was incrementally funded. When the program closed in June 2010, a total of $43 billion in loans was outstanding under the TALF program, and the TARP's commitments constituted $4.3 billion. The Federal Reserve Board of Governors agreed that it was appropriate for Treasury to reduce TALF credit protection from TARP to $4.3 billion. Board of Governors of the Federal Reserve System, *Federal Reserve Announces Agreement with the Treasury Department Regarding a Reduction of Credit Protection Provided for the Term Asset-Backed Securities Loan Facility (TALF)* (July 20, 2010) (online at www.federalreserve.gov/newsevents/press/monetary/20100720a.htm).

[xi] As of December 1, 2010, Treasury had provided $106 million to TALF LLC. This total is net of accrued interest payable to Treasury. Board of Governors of the Federal Reserve System, *Factors Affecting Reserve Balances (H.4.1)* (Dec. 2, 2010) (online at www.federalreserve.gov/releases/h41/20101202/).

[xii] As of September 30, 2010, the total value of securities held by the PPIP managers was $19.3 billion. Non-agency Residential Mortgage-Backed Securities represented 82 percent of the total; Commercial Mortgage-Backed Securities represented the balance. U.S. Department of the Treasury, *Legacy Securities Public-Private Investment Program, Program Update—Quarter Ended September 30, 2010,* at 4 (Oct. 20, 2010) (online at financialstability.gov/docs/External%20Report%20-%2009-10%20vFinal.pdf).

[xiii] U.S. Department of the Treasury, *Troubled Assets Relief Program Monthly 105(a) Report—October 2010,* at 4 (Nov. 10, 2010) (online at www.financialstability.gov/docs/October 105(a) Report.pdf).

[xiv] As of November 26, 2010, Treasury has received $428 million in capital repayments from two PPIP fund managers. U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 23 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

[xv] As of November 26, 2010, Treasury's purchases under the SBA 7(a) Securities Purchase Program totaled $364.2 million. U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 22 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

[xvi] Treasury will not make additional purchases pursuant to the expiration of its purchasing authority under EESA. U.S. Department of the Treasury, *Troubled Asset Relief Program: Two-Year Retrospective,* at 43 (Oct. 2010) (online at www.financialstability.gov/docs/TARP%20Two%20Year%20Retrospective_10%2005%2010_transmittal%20letter.pdf).

[xvii] On June 23, 2010, $1.5 billion was allocated to mortgage assistance through the Hardest Hit Fund (HHF). Another $600 million was approved on August 3, 2010. U.S. Department of the Treasury, *Obama Administration Approves State Plans for $600 million of 'Hardest Hit Fund' Foreclosure Prevention Assistance* (Aug. 3, 2010) (online at www.financialstability.gov/latest/pr_08042010.html). As part of its revisions to TARP allocations upon enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Treasury allocated an additional $2 billion in TARP funds to mortgage assistance for unemployed borrowers through the HHF. U.S. Department of the Treasury, *Obama Administration Announces Additional Support for Targeted Foreclosure-Prevention Programs to Help Homeowners Struggling with Unemployment* (Aug. 11, 2010) (online at www.financialstability.gov/latest/pr_08112010.html). Another $3.5 billion was allocated among the 18 states and the District of Columbia currently participating in HHF. The amount each state received during this round of funding is proportional to its population. U.S. Department of the Treasury, *Troubled Asset Relief Program: Two Year Retrospective,* at 72 (Oct. 2010) (online at www.financialstability.gov/docs/TARP%20Two%20Year%20Retrospective_10%2005%2010_transmittal%20letter.pdf).

[xviii] As of December 1, 2010, a total of $103.6 million has been disbursed to 12 state Housing Finance Agencies (HFAs). Data provided by Treasury (Dec. 2, 2010).

[xix] This figure represents the amount Treasury disbursed to fund the advance purchase account of the Letter of Credit issued under the FHA Short Refinance Program. The $53.3 million in the FHA Short Refinance program is broken down as follows: $50 million for a deposit into an advance purchase account as collateral to the initial $50 million Letter of Credit, $2.9 million for the closing and funding of the Letter of Credit, $115,000 in trustee fees, $175,000 in claims processor fees, and $156,000 for an unused commitment fee for the Letter of Credit. Data provided by Treasury (Dec. 2, 2010).

[xx] U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 1–13, 16–17 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf). Treasury closed the program on September 30, 2010, after investing $570 million in 84 CDFIs. U.S. Department of the Treasury, *Treasury Announces Special Financial Stabilization Initiative Investments of $570 Million in 84 Community Development Financial Institutions in Underserved Areas* (Sept. 30, 2010) (online at financialstability.gov/latest/pr_09302010b.html).

FIGURE 47: TARP PROFIT AND LOSS

[Dollars in millions]

TARP Initiative [xxi]	Dividends [xxii] (as of 10/31/2010)	Interest [xxiii] (as of 10/31/2010)	Warrant Disposition Proceeds [xxiv] (as of 11/26/2010)	Other Proceeds (as of 10/31/2010)	Losses [xxv] (as of 11/26/2010)	Total
Total	**$16,725**	**$1,061**	**$8,160**	**$5,852**	**($6,034)**	**$25,764**
CPP	9,860	49	6,905	[xxvi] 3,015	(2,576)	17,252
TIP	3,004	—	1,256	—	—	4,260
AIFP	[xxvii] 3,418	931	—	[xxviii] 15	(3,458)	906
ASSP	—	15	—	[xxix] 101	—	116
AGP	443	—	—	[xxx] 2,246	—	2,689
PPIP	—	66	—	[xxxi] 199	—	264
SBA 7(a)	—	1	—	—	—	1
Bank of America Guarantee	—	—	—	[xxxii] 276	—	276

[xxi] AIG is not listed in this table because no profit or loss has been recorded to date for AIG. Its missed dividends were capitalized as part of the issuance of Series E preferred shares and are not considered to be outstanding. Treasury currently holds non-cumulative preferred shares, meaning AIG is not penalized for non-payment. Therefore, no profit or loss has been realized on Treasury's AIG investment to date.

HAMP is not listed in this table because HAMP is a 100% subsidy program and there is no profit expected.

[xxii] U.S. Department of the Treasury, *Cumulative Dividends, Interest and Distributions Report as of October 31, 2010* (Nov. 11, 2010) (online at financialstability.gov/docs/dividends-interest-reports/October%202010%20Dividends%20&%20Interest%20Report.pdf).

[xxiii] U.S. Department of the Treasury, *Cumulative Dividends, Interest and Distributions Report as of October 31, 2010* (Nov. 11, 2010) (online at financialstability.gov/docs/dividends-interest-reports/October%202010%20Dividends%20&%20Interest%20Report.pdf).

[xxiv] U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010* (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

[xxv] In the TARP Transactions Report, Treasury classified the investments it made in two institutions, CIT Group ($2.3 billion) and Pacific Coast National Bancorp ($4.1 million), as losses. Treasury has also sold its preferred ownership interests and warrants from South Financial Group, Inc. and TIB Financial Corp. This represents a $241.7 million loss on its CPP investments in these two banks. Two TARP recipients, UCBH Holdings, Inc. ($298.7 million) and a banking subsidiary of Midwest Banc Holdings, Inc. ($89.4 million), are currently in bankruptcy proceedings. As of November 26, three TARP recipients, Pierce County Bancorp, Sonoma Valley Bancorp, and Tifton Banking Company, had entered receivership. Cumulatively, they had received $19.3 million in TARP funding. U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010* (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

[xxvi] This figure represents net proceeds to Treasury from the sale of Citigroup common stock to date. For details on Treasury's sales of Citigroup common stock, see endnote ii, *supra.* U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 15 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf); U.S. Department of the Treasury, *Troubled Asset Relief Program: Two-Year Retrospective,* at 25 (Oct. 2010) (online at www.financialstability.gov/docs/TARP%20Two%20Year%20Retrospective_10%2005%2010__transmittal%20letter.pdf).

[xxvii] This figure includes $815 million in dividends from Ally preferred stock, trust preferred securities, and mandatory convertible preferred shares. The dividend total also includes a $748.6 million senior unsecured note from Treasury's investment in General Motors. U.S. Department of the Treasury, *Cumulative Dividends, Interest and Distributions Report as of October 31, 2010* (Nov. 11, 2010) (online at financialstability.gov/docs/dividends-interest-reports/October%202010%20Dividends%20&%20Interest%20Report.pdf); Data provided by Treasury (May 7, 2010).

[xxviii] Treasury received proceeds from an additional note connected with the loan made to Chrysler Financial on January 16, 2009. U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 18 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

[xxix] This represents the total proceeds from additional notes connected with Treasury's investments in GM Supplier Receivables LLC and Chrysler Receivables SPV LLC. U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 19 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

[xxx] As a fee for taking a second-loss position of up to $5 billion on a $301 billion pool of ring-fenced Citigroup assets as part of the AGP, Treasury received $4.03 billion in Citigroup preferred stock and warrants. Treasury exchanged these preferred stocks for trust preferred securities in June 2009. Following the early termination of the guarantee in December 2009, Treasury cancelled $1.8 billion of the trust preferred securities, leaving Treasury with $2.23 billion in Citigroup trust preferred securities. On September 30, 2010, Treasury sold these securities for $2.25 billion in total proceeds. At the end of Citigroup's participation in the FDIC's TLGP, the FDIC may transfer $800 million of $3.02 billion in Citigroup Trust Preferred Securities it received in consideration for its role in the AGP to Treasury. U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 20 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf); U.S. Department of the Treasury, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, and Citigroup Inc., *Termination Agreement,* at 1 (Dec. 23, 2009) (online at www.financialstability.gov/docs/Citi%20AGP%20Termination%20Agreement%20-%20Fully%20Executed%20Version.pdf); U.S. Department of the Treasury, *Treasury Announces Further Sales of Citigroup Securities and Cumulative Return to Taxpayers of $41.6 Billion* (Sept. 30, 2010) (online at financialstability.gov/latest/pr_09302010c.html); Federal Deposit Insurance Corporation, *2009 Annual Report,* at 87 (June 30, 2010) (online at www.fdic.gov/about/strategic/report/2009annualreport/AR09final.pdf).

[xxxi] As of October 31, 2010, Treasury has earned $264.2 million in membership interest distributions from the PPIP. Additionally, Treasury has earned $20.6 million in total proceeds following the termination of the TCW fund. *See* U.S. Department of the Treasury, *Cumulative Dividends, Interest and Distributions Report as of October 31, 2010,* at 14 (Nov. 11, 2010) (online at financialstability.gov/docs/dividends-interest-reports/October%202010%20Dividends%20&%20Interest%20Report.pdf); U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 23 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

[xxxii] lthough Treasury, the Federal Reserve, and the FDIC negotiated with Bank of America regarding a similar guarantee, the parties never reached an agreement. In September 2009, Bank of America agreed to pay each of the prospective guarantors a fee as though the guarantee had been in place during the negotiations period. This agreement resulted in payments of $276 million to Treasury, $57 million to the Federal Reserve, and $92 million to the FDIC. U.S. Department of the Treasury, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, and Bank of America Corporation, *Termination Agreement,* at 1–2 (Sept. 21, 2009) (online at www.financialstability.gov/docs/AGP/BofA%20-%20Termination%20Agreement%20-%20executed.pdf).

d. CPP Unpaid Dividend and Interest Payments [487]

As of October 31, 2010, 123 institutions have missed at least one dividend payment on preferred stock issued under CPP outstanding.[488] Among these institutions, 97 are not current on cumulative dividends, amounting to $110.8 million in missed payments. Another 26 banks have not paid $8 million in non-cumulative dividends. Of the $49.5 billion currently outstanding in CPP funding, Treasury's investments in banks with non-current dividend payments total $3.8 billion. A majority of the banks that remain delinquent on dividend payments have under $1 billion in total assets on their balance sheets. Also, there are 22 institutions that no longer have outstanding unpaid dividends, after previously deferring their quarterly payments.[489]

Six banks have failed to make six dividend payments, while one bank has missed all seven quarterly payments. These institutions have received a total of $207.1 million in CPP funding. Under the terms of the CPP, after a bank fails to pay dividends for six periods, Treasury has the right to elect two individuals to the company's board of directors.[490] Figure 48 below provides further details on the distribution and the number of institutions that have missed dividend payments.

In addition, eight CPP participants have missed at least one interest payment, representing $3.6 million in cumulative unpaid interest payments. Treasury's total investments in these non-public institutions represent less than $1 billion in CPP funding.

[487] U.S. Department of the Treasury, *Cumulative Dividends, Interest, and Distributions Report as of October 31, 2010,* at 20 (Nov. 10, 2010) (online at www.financialstability.gov/docs/dividends-interest-reports/October%202010%20Dividends%20&%20Interest%20Report.pdf) (hereinafter "Cumulative Dividends, Interest, and Distributions Report as of October 31, 2010").

[488] Does not include banks with missed dividend payments that have either repaid all delinquent dividends, exited TARP, gone into receivership, or filed for bankruptcy.

[489] Includes institutions that have either (a) fully repaid their CPP investment and exited the program or (b) entered bankruptcy or its subsidiary was placed into receivership. Cumulative Dividends, Interest, and Distributions Report as of October 31, 2010, *supra* note 487, at 20.

[490] U.S. Department of the Treasury, *Frequently Asked Questions Capital Purchase Program (CPP): Related to Missed Dividend (or Interest) Payments and Director Nomination* (online at www.financialstability.gov/docs/CPP/CPP%20Directors%20FAQs.pdf) (accessed Dec. 10, 2010).

FIGURE 48: CPP MISSED DIVIDEND PAYMENTS (AS OF OCTOBER 31, 2010)[491]

Number of Missed Payments	1	2	3	4	5	6	7	Total
Cumulative Dividends								
Number of Banks, by asset size	30	20	18	16	10	3	0	97
Under $1B	22	17	14	11	7	1	0	72
$1B–$10B	6	3	3	5	3	2	0	22
Over $10B	2	0	1	0	0	0	0	3
Non-Cumulative Dividends								
Number of Banks, by asset size	2	5	7	3	5	3	1	26
Under $1B	1	5	6	3	5	3	1	24
$1B–$10B	1	0	1	0	0	0	0	2
Over $10B	0	0	0	0	0	0	0	0
Total Missed Payments								123

[491] Cumulative Dividends, Interest, and Distributions Report as of October 31, 2010, *supra* note 487, at 17–20. Data on total bank assets compiled using SNL Financial data service (accessed Nov. 3, 2010).

e. CPP Losses

As of November 26, 2010, Treasury has realized a total of $2.6 billion in losses from investments in four CPP participants. CIT Group Inc. and Pacific Coast National Bancorp have both completed bankruptcy proceedings, and the preferred stock and warrants issued by the South Financial Group and TIB Financial Corp. were sold to third-party institutions at a discount. Excluded from Treasury's total losses are investments in institutions that have pending receivership or bankruptcy proceedings, as well as an institution that is currently the target of an acquisition.[492] Settlement of these transactions and proceedings would increase total losses in the CPP to $3.0 billion. Figure 49 below details settled and unsettled investment losses from CPP participants that have declared bankruptcy, been placed into receivership, or renegotiated the terms of their CPP contracts.

[492] Treasury Transactions Report, *supra* note 481, at 13.

FIGURE 49: CPP SETTLED AND UNSETTLED LOSSES [493]

Institution	Investment Amount	Investment Disposition Amount	Warrant Disposition Amount	Dividends & Interest	Possible Losses/ Reduced Exposure	Action
Cadence Financial Corporation.	$44,000,000	$38,000,000	–	$2,970,000	$(6,000,000)	10/29/2010: Treasury agreed to sell preferred stock and warrants issued by Cadence Financial to Community Bancorp LLC for $38 million plus accrued and unpaid dividends. Completion of the sale subject to fulfillment of certain closing conditions.
Capital Bank Corporation [494]	41,279,000	–	–	3,457,117	(20,639,500)	11/9/2010: Capital Bank Corp. is seeking to enter an agreement with Treasury pursuant to which the company will repurchase outstanding TARP preferred shares at 50 percent of liquidation value, plus accrued unpaid dividends. The company will use cash proceeds from its acquisition by North American Financial Holdings Inc. As of Nov. 30, 2010, no agreement has been reached between Capital Bank Corp. and Treasury.
CIT Group Inc.*	2,330,000,000	–	–	43,687,500	(2,330,000,000)	12/10/2009: Bankruptcy reorganization plan for CIT Group Inc. became effective. CPP preferred shares and warrants were extinguished and replaced with contingent value rights (CVR). On Feb. 8, 2010, the CVRs expired without value.
Midwest Banc Holdings, Inc.	89,388,000	–	–	824,289	(89,388,000)	5/14/2010: Midwest Banc Holdings, Inc. subsidiary, Midwest Bank and Trust, Co., placed into receivership. Midwest Banc Holdings is currently in bankruptcy proceedings.
Pacific Coast National Bancorp.*	4,120,000	–	–	18,088	(4,120,000)	2/11/2010: Pacific Coast National Bancorp dismissed its bankruptcy proceedings without recovery to creditors or investors. Investments, including Treasury's CPP investments, were extinguished.
Pierce County Bancorp	6,800,000	–	–	207,948	(6,800,000)	11/5/2010: Pierce County Bancorp subsidiary, Pierce Commercial Bank, placed into receivership.

Sonoma Valley Bancorp	8,653,000	–	–	347,164	(8,653,000)	8/20/2010: Sonoma Valley Bancorp subsidiary, Sonoma Valley Bank, placed into receivership.
South Financial Group*	347,000,000	130,179,219	$400,000	16,386,111	(216,820,781)	9/30/2010: Preferred stock and warrants sold to Toronto-Dominion Bank.
The Bank of Currituck ..	4,021,000	1,752,850	–	169,834	(2,268,150)	11/5/2010: Treasury agreed to sell all preferred stock (including preferred stock received upon exercise of warrants) to the Bank of Currituck.
TIB Financial Corp.*	37,000,000	12,119,637	40,000	1,284,722	(24,880,363)	9/30/2010: Preferred stock and warrants sold to North American Financial Holdings.
Tifton Banking Company	3,800,000	–	–	223,208	(3,800,000)	11/12/2010: Tifton Banking Company placed into receivership.
UCBH Holdings, Inc.	298,737,000	–	–	7,509,920	(298,737,000)	11/6/2009: United Commercial Bank, a wholly-owned subsidiary of UCBH Holdings, Inc., was placed into receivership. UCBH Holdings is currently in bankruptcy proceedings.
Total	**$3,214,798,000**	**$182,051,706**	**440,000**	**77,085,901**	**$(3,012,106,794)**	

493 Treasury Transactions Report, *supra* note 481, at 14. The asterisk ("*") denotes recognized losses on Treasury's Transactions Report.

494 Capital Bank Corporation, *Schedule 14A,* at 5 (Nov. 19, 2010) (online at www.sec.gov/Archives/edgar/data/1071992/000095012310107474/g25191ddef14a.htm).

f. Rate of Return

As of December 2, 2010, the average internal rate of return for all public financial institutions that participated in the CPP and fully repaid the U.S. government (including preferred shares, dividends, and warrants) remained at 8.4 percent, as no institutions exited the program in November.[495] The internal rate of return is the annualized effective compounded return rate that can be earned on invested capital.

g. Warrant Disposition

FIGURE 50: WARRANT REPURCHASES/AUCTIONS FOR FINANCIAL INSTITUTIONS WHO HAVE FULLY REPAID CPP FUNDS (AS OF DECEMBER 2, 2010)

Institution	Investment Date	Warrant Repurchase Date	Warrant Repurchase/ Sale Amount	Panel's Best Valuation Estimate at Disposition Date	Price/ Estimate Ratio	IRR (Percent)
Old National Bancorp	12/12/2008	5/8/2009	$1,200,000	$2,150,000	0.558	9.3
Iberiabank Corporation	12/5/2008	5/20/2009	1,200,000	2,010,000	0.597	9.4
Firstmerit Corporation	1/9/2009	5/27/2009	5,025,000	4,260,000	1.180	20.3
Sun Bancorp, Inc.	1/9/2009	5/27/2009	2,100,000	5,580,000	0.376	15.3
Independent Bank Corp.	1/9/2009	5/27/2009	2,200,000	3,870,000	0.568	15.6
Alliance Financial Corporation	12/19/2008	6/17/2009	900,000	1,580,000	0.570	13.8
First Niagara Financial Group	11/21/2008	6/24/2009	2,700,000	3,050,000	0.885	8.0
Berkshire Hills Bancorp, Inc.	12/19/2008	6/24/2009	1,040,000	1,620,000	0.642	11.3
Somerset Hills Bancorp	1/16/2009	6/24/2009	275,000	580,000	0.474	16.6
SCBT Financial Corporation	1/16/2009	6/24/2009	1,400,000	2,290,000	0.611	11.7
HF Financial Corp.	11/21/2008	6/30/2009	650,000	1,240,000	0.524	10.1
State Street	10/28/2008	7/8/2009	60,000,000	54,200,000	1.107	9.9
U.S. Bancorp	11/14/2008	7/15/2009	139,000,000	135,100,000	1.029	8.7
The Goldman Sachs Group, Inc.	10/28/2008	7/22/2009	1,100,000,000	1,128,400,000	0.975	22.8
BB&T Corp.	11/14/2008	7/22/2009	67,010,402	68,200,000	0.983	8.7
American Express Company	1/9/2009	7/29/2009	340,000,000	391,200,000	0.869	29.5
Bank of New York Mellon Corp	10/28/2008	8/5/2009	136,000,000	155,700,000	0.873	12.3
Morgan Stanley	10/28/2008	8/12/2009	950,000,000	1,039,800,000	0.914	20.2
Northern Trust Corporation	11/14/2008	8/26/2009	87,000,000	89,800,000	0.969	14.5
Old Line Bancshares Inc.	12/5/2008	9/2/2009	225,000	500,000	0.450	10.4
Bancorp Rhode Island, Inc.	12/19/2008	9/30/2009	1,400,000	1,400,000	1.000	12.6
Centerstate Banks of Florida Inc.	11/21/2008	10/28/2009	212,000	220,000	0.964	5.9
Manhattan Bancorp	12/5/2008	10/14/2009	63,364	140,000	0.453	9.8
CVB Financial Corp	12/5/2008	10/28/2009	1,307,000	3,522,198	0.371	6.4
Bank of the Ozarks	12/12/2008	11/24/2009	2,650,000	3,500,000	0.757	9.0
Capital One Financial	11/14/2008	12/3/2009	148,731,030	232,000,000	0.641	12.0
JPMorgan Chase & Co.	10/28/2008	12/10/2009	950,318,243	1,006,587,697	0.944	10.9
CIT Group Inc.	12/31/2008	—	—	—	—	(97.2)
TCF Financial Corp	1/16/2009	12/16/2009	9,599,964	11,825,830	0.812	11.0
LSB Corporation	12/12/2008	12/16/2009	560,000	535,202	1.046	9.0
Wainwright Bank & Trust Company	12/19/2008	12/16/2009	568,700	1,071,494	0.531	7.8
Wesbanco Bank, Inc.	12/5/2008	12/23/2009	950,000	2,387,617	0.398	6.7
Union First Market Bankshares Corporation (Union Bankshares Corporation)	12/19/2008	12/23/2009	450,000	1,130,418	0.398	5.8
Trustmark Corporation	11/21/2008	12/30/2009	10,000,000	11,573,699	0.864	9.4
Flushing Financial Corporation	12/19/2008	12/30/2009	900,000	2,861,919	0.314	6.5
OceanFirst Financial Corporation	1/16/2009	2/3/2010	430,797	279,359	1.542	6.2

[495] Calculation of the internal rate of return (IRR) also includes CPP investments in public institutions not repaid in full (for reasons such as acquisition by another institution) in the Transaction Report, e.g., The South Financial Group and TIB Financial Corporation. The Panel's total IRR calculation now includes CPP investments in public institutions recorded as a loss on the TARP Transaction Report due to bankruptcy, e.g., CIT Group Inc. Going forward, the Panel will continue to include losses due to bankruptcy when Treasury determines that any associated contingent value rights have expired without value. When excluding CIT Group from the calculation, the resulting IRR is 10.4 percent. Treasury Transactions Report, *supra* note 481.

FIGURE 50: WARRANT REPURCHASES/AUCTIONS FOR FINANCIAL INSTITUTIONS WHO HAVE FULLY REPAID CPP FUNDS (AS OF DECEMBER 2, 2010)—Continued

Institution	Investment Date	Warrant Repurchase Date	Warrant Repurchase/ Sale Amount	Panel's Best Valuation Estimate at Disposition Date	Price/ Esti- mate Ratio	IRR (Percent)
Monarch Financial Holdings, Inc.	12/19/2008	2/10/2010	260,000	623,434	0.417	6.7
	[496] 10/28/2008 [497] 1/9/2009					
Bank of America	[498] 1/14/2009	3/3/2010	1,566,210,714	1,006,416,684	1.533	6.5
Washington Federal Inc./Washington Federal Savings & Loan Association	11/14/2008	3/9/2010	15,623,222	10,166,404	1.537	18.6
Signature Bank	12/12/2008	3/10/2010	11,320,751	11,458,577	0.988	32.4
Texas Capital Bancshares, Inc.	1/16/2009	3/11/2010	6,709,061	8,316,604	0.807	30.1
Umpqua Holdings Corp.	11/14/2008	3/31/2010	4,500,000	5,162,400	0.872	6.6
City National Corporation	11/21/2008	4/7/2010	18,500,000	24,376,448	0.759	8.5
First Litchfield Financial Corporation	12/12/2008	4/7/2010	1,488,046	1,863,158	0.799	15.9
PNC Financial Services Group Inc.	12/31/2008	4/29/2010	324,195,686	346,800,388	0.935	8.7
Comerica Inc.	11/14/2008	5/4/2010	183,673,472	276,426,071	0.664	10.8
Valley National Bancorp	11/14/2008	5/18/2010	5,571,592	5,955,884	0.935	8.3
Wells Fargo Bank	10/28/2008	5/20/2010	849,014,998	1,064,247,725	0.798	7.8
First Financial Bancorp	12/23/2008	6/2/2010	3,116,284	3,051,431	1.021	8.2
Sterling Bancshares, Inc./Sterling Bank	12/12/2008	6/9/2010	3,007,891	5,287,665	0.569	10.8
SVB Financial Group	12/12/2008	6/16/2010	6,820,000	7,884,633	0.865	7.7
Discover Financial Services	3/13/2009	7/7/2010	172,000,000	166,182,652	1.035	17.1
Bar Harbor Bancshares	1/16/2009	7/28/2010	250,000	518,511	0.482	6.2
Citizens & Northern Corporation	1/16/2009	8/4/2010	400,000	468,164	0.854	5.9
Columbia Banking System, Inc.	11/21/2008	8/11/2010	3,301,647	3,291,329	1.003	7.3
Hartford Financial Services Group, Inc.	6/26/2009	9/21/2010	713,687,430	472,221,996	1.511	30.3
Lincoln National Corporation	7/10/2009	9/16/2010	216,620,887	181,431,183	1.194	27.1
Fulton Financial Corporation	12/23/2008	9/8/2010	10,800,000	15,616,013	0.692	6.7
The Bancorp, Inc./The Bancorp Bank	12/12/2008	9/8/2010	4,753,985	9,947,683	0.478	12.8
South Financial Group, Inc./Carolina First Bank	12/5/2008	9/30/2010	400,000	1,164,486	0.343	(34.2)
TIB Financial Corp/TIB Bank	12/5/2008	9/30/2010	40,000	235,757	0.170	(38.0)
Total			**$8,148,332,166**	**$7,999,280,713**	**1.019**	**8.4**

[496] Investment date for Bank of America in CPP.
[497] Investment date for Merrill Lynch in CPP.
[498] Investment date for Bank of America in TIP.

FIGURE 51: VALUATION OF CURRENT HOLDINGS OF WARRANTS (AS OF DECEMBER 2, 2010)

[Dollars in millions]

Financial Institutions with Warrants Outstanding	Warrant Valuation		
	Low Estimate	High Estimate	Best Estimate
Citigroup, Inc.[499]	$74.68	$1,383.79	$229.25
SunTrust Banks, Inc.	13.52	322.84	103.76
Regions Financial Corporation	4.61	157.75	87.58
Fifth Third Bancorp	92.59	373.07	177.87
KeyCorp	20.60	152.96	68.87
AIG	401.00	1,977.51	744.11
All Other Banks	555.16	1,868.68	1,102.97
Total	**$1,162.16**	**$6,236.60**	**$2,514.41**

[499] Includes warrants issued under CPP, AGP, and TIP.

2. Federal Financial Stability Efforts

a. Federal Reserve and FDIC Programs

In addition to the direct expenditures Treasury has undertaken through the TARP, the federal government has engaged in a much broader program directed at stabilizing the U.S. financial system. Many of these initiatives explicitly augment funds allocated by Treasury under specific TARP initiatives, such as FDIC and Federal Reserve asset guarantees for Citigroup, or operate in tandem with Treasury programs. Other programs, like the Federal Reserve's extension of credit through its Section 13(3) facilities and special purpose vehicles (SPVs) and the FDIC's Temporary Liquidity Guarantee Program (TLGP), operate independently of the TARP.

b. Total Financial Stability Resources

Beginning in its April 2009 report, the Panel broadly classified the resources that the federal government has devoted to stabilizing the economy through myriad new programs and initiatives such as outlays, loans, or guarantees. With the reductions in funding for certain TARP programs, the Panel calculates the total value of these resources to be over $2.5 trillion. However, this would translate into the ultimate "cost" of the stabilization effort only if: (1) assets do not appreciate; (2) no dividends are received, no warrants are exercised, and no TARP funds are repaid; (3) all loans default and are written off; and (4) all guarantees are exercised and subsequently written off.

With respect to the FDIC and Federal Reserve programs, the risk of loss varies significantly across the programs considered here, as do the mechanisms providing protection for the taxpayer against such risk. As discussed in the Panel's November 2009 report, the FDIC assesses a premium of up to 100 basis points on TLGP debt guarantees.[500] In contrast, the Federal Reserve's liquidity programs are generally available only to borrowers with good credit, and the loans are over-collateralized and with recourse to other assets of the borrower. If the assets securing a Federal Reserve loan realize a decline in value greater than the "haircut," the Federal Reserve is able to demand more collateral from the borrower. Similarly, should a borrower default on a recourse loan, the Federal Reserve can turn to the borrower's other assets to make the Federal Reserve whole. In this way, the risk to the taxpayer on recourse loans only materializes if the borrower enters bankruptcy.

c. Mortgage Purchase Programs

On September 7, 2008, Treasury announced the GSE Mortgage Backed Securities Purchase Program. The Housing and Economic Recovery Act of 2008 provided Treasury with the authority to purchase MBS guaranteed by GSEs through December 31, 2009. Treasury purchased approximately $225 billion in GSE MBS by the

[500] Congressional Oversight Panel, *November Oversight Report: Guarantees and Contingent Payments in TARP and Related Programs,* at 36 (Nov. 6, 2009) (online at cop.senate.gov/documents/cop-110609-report.pdf).

time its authority expired.[501] As of November 2010, there was approximately $149.7 billion in MBS still outstanding under this program.[502]

In March 2009, the Federal Reserve authorized purchases of $1.25 trillion MBS guaranteed by Fannie Mae, Freddie Mac, and Ginnie Mae, and $200 billion of agency debt securities from Fannie Mae, Freddie Mac, and the Federal Home Loan Banks.[503] The intended purchase amount for agency debt securities was subsequently decreased to $175 billion.[504] All purchasing activity was completed on March 31, 2010. As of December 1, 2010, the Federal Reserve held $1.02 trillion of agency MBS and $148 billion of agency debt.[505]

d. Federal Reserve Treasury Securities Purchases [506]

On November 3, 2010, the Federal Open Market Committee (FOMC) announced that it has directed FRBNY to begin purchasing an additional $600 billion in longer-term Treasury securities. In addition, FRBNY will reinvest $250 billion to $300 billion in principal payments from agency debt and agency MBS in Treasury securities.[507] The additional purchases and reinvestments will be conducted through the end of the second quarter of 2011, meaning the pace of purchases will be approximately $110 billion per month. In order to facilitate these purchases, FRBNY will temporarily lift its System Open Market Account per-issue limit, which prohibits the Federal Reserve's holdings of an individual security from surpassing 35 percent of the outstanding amount.[508] As of December 1, 2010, the Federal Reserve held $917 billion in Treasury securities.[509]

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[501] U.S. Department of the Treasury, *FY2011 Budget in Brief,* at 138 (Feb. 2010) (online at www.treasury.gov/about/budget-performance/budget-in-brief/Documents/FY%202011%20BIB%20(2).pdf).

[502] U.S. Department of the Treasury, *MBS Purchase Program: Portfolio by Month* (online at www.financialstability.gov/docs/November%202010%20Portfolio%20by%20month.pdf) (accessed Dec. 3, 2010). Treasury has received $65.7 billion in principal repayments and $14.3 billion in interest payments from these securities. *See* U.S. Department of the Treasury, *MBS Purchase Program Principal and Interest Received* (online at www.financialstability.gov/docs/November%202010%20MBS%20Principal%20and%20Interest%20Monthly%20Breakout.pdf) (accessed Dec. 3, 2010).

[503] Board of Governors of the Federal Reserve System, *Federal Reserve System Monthly Report on Credit and Liquidity Programs and the Balance Sheet,* at 5 (Nov. 2010) (online at federalreserve.gov/monetarypolicy/files/monthlyclbsreport201011.pdf).

[504] *Id.* at 5.

[505] Board of Governors of the Federal Reserve System, *Factors Affecting Reserve Balances (H.4.1)* (Dec. 2, 2010) (online at www.federalreserve.gov/releases/h41/20101202/) (hereinafter "Factors Affecting Reserve Balances (H.4.1)").

[506] Board of Governors of the Federal Reserve System, *Press Release—FOMC Statement* (Nov. 3, 2010) (online at www.federalreserve.gov/newsevents/press/monetary/20101103a.htm); Federal Reserve Bank of New York, *Statement Regarding Purchases of Treasury Securities* (Nov. 3, 2010) (online at www.federalreserve.gov/newsevents/press/monetary/monetary20101103a1.pdf).

[507] On August 10, 2010, the Federal Reserve began reinvesting principal payments on agency debt and agency MBS holdings in longer-term Treasury securities in order to keep the amount of their securities holdings in their System Open Market Account portfolio at their then-current level. Board of Governors of the Federal Reserve System, *FOMC Statement* (Aug. 10, 2010) (online at www.federalreserve.gov/newsevents/press/monetary/20100810a.htm).

[508] Federal Reserve Bank of New York, *FAQs: Purchases of Longer-term Treasury Securities* (Nov. 3, 2010) (online at www.newyorkfed.org/markets/lttreas_faq.html).

[509] Factors Affecting Reserve Balances (H.4.1), *supra* note 505.

FIGURE 52: FEDERAL GOVERNMENT FINANCIAL STABILITY EFFORT (AS OF DECEMBER 1, 2010) [xxxiii]

[Dollars in billions]

Program	Treasury (TARP)	Federal Reserve	FDIC	Total
Total	**$475**	**$1,345.3**	**$690.9**	**$2,511.2**
Outlays [xxxiv]	218.7	1,196.9	188.9	1,604.6
Loans	23.4	148.4	0	171.8
Guarantees [xxxv]	4.3	0	502	506.3
Repaid and Unavailable TARP Funds	228.6	0	0	228.6
AIG [xxxvi]	**69.8**	**82.6**	**0**	**152.4**
Outlays	[xxxvii] 69.8	[xxxviii] 26.1	0	95.9
Loans	0	[xxxix] 56.5	0	56.5
Guarantees	0	0	0	0
Citigroup	**11.6**	**0**	**0**	**11.6**
Outlays	[xl] 11.6	0	0	11.6
Loans	0	0	0	0
Guarantees	0	0	0	0
Capital Purchase Program (Other)	**37.8**	**0**	**0**	**37.8**
Outlays	[xli] 37.8	0	0	37.8
Loans	0	0	0	0
Guarantees	0	0	0	0
Capital Assistance Program	**N/A**	**0**	**0**	[xlii] **N/A**
TALF	**4.3**	**38.7**	**0**	**43.0**
Outlays	0	0	0	0
Loans	0	[xliv] 38.7	0	38.7
Guarantees	[xliii] 4.3	0	0	4.3
PPIP (Loans) [xlv]	**0**	**0**	**0**	**0**
Outlays	0	0	0	0
Loans	0	0	0	0
Guarantees	0	0	0	0
PPIP (Securities)	[xlvi] **22.4**	**0**	**0**	**22.4**
Outlays	7.5	0	0	7.5
Loans	14.9	0	0	14.9
Guarantees	0	0	0	0
Making Home Affordable Program/Foreclosure Mitigation	**45.6**	**0**	**0**	**45.6**
Outlays	[xlvii] 45.6	0	0	45.6
Loans	0	0	0	0
Guarantees	0	0	0	0
Automotive Industry Financing Program	[xlvii] **53.6**	**0**	**0**	**53.6**
Outlays	45.5	0	0	45.5
Loans	8.1	0	0	8.1
Guarantees	0	0	0	0
Automotive Supplier Support Program	**0.4**	**0**	**0**	**0.4**
Outlays	0	0	0	0
Loans	[xlix] 0.4	0	0	0.4
Guarantees	0	0	0	0
SBA 7(a) Securities Purchase	[l] **0.36**	**0**	**0**	**0.36**
Outlays	0.36	0	0	0.36
Loans	0	0	0	0
Guarantees	0	0	0	0
Community Development Capital Initiative	[li] **0.57**	**0**	**0**	**0.57**
Outlays	0	0	0	0
Loans	0.57	0	0	0.57
Guarantees	0	0	0	0
Temporary Liquidity Guarantee Program	**0**	**0**	**502.0**	**502.0**
Outlays	0	0	0	0
Loans	0	0	0	0
Guarantees	0	0	[lii] 502.0	502.0
Deposit Insurance Fund	**0**	**0**	**188.9**	**188.9**
Outlays	0	0	[liii] 188.9	188.9

FIGURE 52: FEDERAL GOVERNMENT FINANCIAL STABILITY EFFORT (AS OF DECEMBER 1, 2010) [xxxiii]—Continued

[Dollars in billions]

Program	Treasury (TARP)	Federal Reserve	FDIC	Total
Loans	0	0	0	0
Guarantees	0	0	0	0
Other Federal Reserve Credit Expansion	**0**	**1,224.0**	**0**	**1,224.0**
Outlays	0	[liv] 1,170.8	0	1,170.8
Loans	0	[lv] 53.2	0	53.2
Guarantees	0	0	0	0

[xxxiii] Unless otherwise noted, all data in this figure are as of November 26, 2010.

[xxxiv] The term ''outlays'' is used here to describe the use of Treasury funds under the TARP, which are broadly classifiable as purchases of debt or equity securities (e.g., debentures, preferred stock, exercised warrants, etc.). These values were calculated using (1) Treasury's actual reported expenditures, and (2) Treasury's anticipated funding levels as estimated by a variety of sources, including Treasury statements and GAO estimates. Anticipated funding levels are set at Treasury's discretion, have changed from initial announcements, and are subject to further change. Outlays used here represent investment and asset purchases—as well as commitments to make investments and asset purchases—and are not the same as budget outlays, which under section 123 of EESA are recorded on a ''credit reform'' basis.

[xxxv] Although many of the guarantees may never be exercised or will be exercised only partially, the guarantee figures included here represent the federal government's greatest possible financial exposure.

[xxxvi] U.S. Department of the Treasury, *Treasury Update on AIG Investment Valuation* (Nov. 1, 2010) (online at financialstability.gov/latest/pr_11012010.html). AIG values exclude accrued dividends on preferred interests in the AIA and ALICO SPVs and accrued interest payable to FRBNY on the Maiden Lane LLCs.

[xxxvii] This number includes investments under the AIGIP/SSFI Program: a $40 billion investment made on November 25, 2008, and a $30 billion investment made on April 17, 2009 (less a reduction of $165 million representing bonuses paid to AIG Financial Products employees). As of November 1, 2010, AIG had utilized $47.5 billion of the available $69.8 billion under the AIGIP/SSFI. U.S. Department of the Treasury, *Treasury Update on AIG Investment Valuation* (Nov. 1, 2010) (online at www.financialstability.gov/latest/pr_11012010.html); U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 13 (Nov. 30, 2010) (online at financialstability.gov/docs/ transactionreports/11-30-10%20Transactions %20Report%20as%20of%2011-26-10.pdf).

[xxxviii] As part of the restructuring of the U.S. government's investment in AIG announced on March 2, 2009, the amount available to AIG through the Revolving Credit Facility was reduced by $25 billion in exchange for preferred equity interests in two special purpose vehicles, AIA Aurora LLC and ALICO Holdings LLC. Board of Governors of the Federal Reserve System, *Federal Reserve System Monthly Report on Credit and Liquidity Programs and the Balance Sheet,* at 18 (Nov. 2010) (online at www.federalreserve.gov/monetarypolicy/ files/monthlyclbsreport201011.pdf). These SPVs were established to hold the common stock of two AIG subsidiaries: American International Assurance Company Ltd. (AIA) and American Life Insurance Company (ALICO). As of December 1, 2010, the book value of the Federal Reserve Bank of New York's holdings in AIA Aurora LLC and ALICO Holdings LLC was $26.1 billion in preferred equity ($16.7 billion in AIA and $9.4 billion in ALICO). Federal Reserve Bank of New York, *Factors Affecting Reserve Balances (H.4.1)* (Dec. 2, 2010) (online at www.federalreserve.gov/releases/h41/20101202/).

[xxxix] This number represents the full $29.2 billion made available to AIG through its Revolving Credit Facility (RCF) with FRBNY ($21.3 billion had been drawn down as of December 1, 2010) and the outstanding principal of the loans extended to the Maiden Lane II and III SPVs to buy AIG assets (as of December 1, 2010, $13.3 billion and $13.9 billion, respectively). Federal Reserve Bank of New York, *Factors Affecting Reserve Balances (H.4.1)* (Dec. 2, 2010) (online at www.federalreserve.gov/releases/ h41/20101202/); Board of Governors of the Federal Reserve System, *Federal Reserve System Monthly Report on Credit and Liquidity Programs and the Balance Sheet* (Nov. 2010) (online at www.federalreserve.gov/monetarypolicy/ files/monthlyclbsreport201011.pdf). The amounts outstanding under the Maiden Lane II and III facilities do not reflect the accrued interest payable to FRBNY. Income from the purchased assets is used to pay down the loans to the SPVs, reducing the taxpayers' exposure to losses over time. Board of Governors of the Federal Reserve System, *Federal Reserve System Monthly Report on Credit and Liquidity Programs and the Balance Sheet,* at 15 (Nov. 2010) (online at www.federalreserve.gov/monetarypolicy/ files/monthlyclbsreport201011.pdf).

The maximum amount available through the RCF decreased from $34.4 billion to $29.3 billion between March and September 2010, as a result of the sale of several subsidiaries. The reduced ceiling also reflects a $3.95 billion repayment to the RCF from proceeds earned from a debt offering by the International Lease Finance Corporation (ILFC), an AIG subsidiary. The balance on the AIG Revolving Credit Facility increased $0.3 billion between September 29 and October 27, 2010, primarily due to recapitalized interest and fees as principal repayments. Board of Governors of the Federal Reserve System, *Federal Reserve System Monthly Report on Credit and Liquidity Programs and the Balance Sheet,* at 17, 19–20 (Nov. 2010) (online at www.federalreserve.gov/monetarypolicy/files/monthlyclbsreport201011.pdf).

[xl] This figure represents Treasury's $25 billion investment in Citigroup, minus $13.4 billion applied as a repayment for CPP funding. The amount repaid comes from the $16.4 billion in gross proceeds Treasury received from the sale of 4.1 billion Citigroup common shares. *See* endnote ii, *supra,* for further details of the sales of Citigroup common stock to date. U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 1, 13 (Nov. 30, 2010) (online at financialstability.gov/docs/ transaction-reports/11-30-10%20 Transactions%20Report%20as%20of%2011-26-10.pdf).

[xli] This figure represents the $204.9 billion Treasury disbursed under the CPP, minus the $25 billion investment in Citigroup identified above, $139.5 billion in repayments (excluding the amount repaid for the Citigroup investment) that are in ''repaid and unavailable'' TARP funds, and losses under the program. This figure does not account for future repayments of CPP investments and dividend payments from CPP investments. U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 13 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

[xlii] On November 9, 2009, Treasury announced the closing of the CAP and that only one institution, GMAC (now Ally Financial), was in need of further capital from Treasury. GMAC, however, received further funding through the AIFP. Therefore, the Panel considers CAP unused. U.S. Department of the Treasury, *Treasury Announcement Regarding the Capital Assistance Program* (Nov. 9, 2009) (online at www.financialstability.gov/latest/tg_11092009.html).

[xliii] This figure represents the $4.3 billion adjusted allocation to the TALF SPV. However, as of October 27, 2010, TALF LLC had drawn only $105 million of the available $4.3 billion. Board of Governors of the Federal Reserve System, *Factors Affecting Reserve Balances (H.4.1)* (Oct. 28, 2010) (online at www.federalreserve.gov/releases/h41/20101028/); U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 21 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf). On June 30, 2010, the Federal Reserve ceased issuing loans collateralized by newly issued CMBS. As of this date, investors had requested a total of $73.3 billion in TALF loans ($13.2 billion in CMBS and $60.1 billion in non-CMBS) and $71 billion in TALF loans had been settled ($12 billion in CMBS and $59 billion in non-CMBS). Earlier, it ended its issues of loans collateralized by other TALF-eligible newly issued and legacy ABS (non-CMBS) on March 31, 2010. Federal Reserve Bank of New York, *Term Asset-Backed Securities Loan Facility: Terms and Conditions* (online at www.newyorkfed.org/markets/talf_terms.html) (accessed Dec. 10, 2010); Federal Reserve Bank of New York, *Term Asset-Backed Securities Loan Facility: CMBS* (online at www.newyorkfed.org/markets/cmbs_operations.html) (accessed Dec. 10, 2010); Federal Reserve Bank of New York, *Term Asset-Backed Securities Loan Facility: CMBS* (online at www.newyorkfed.org/markets/CMBS_recent_operations.html) (accessed Dec. 10, 2010); Federal Reserve Bank of New York, *Term Asset-Backed Securities Loan Facility: non-CMBS* (online at www.newyorkfed.org/markets/talf_operations.html) (accessed Dec. 10, 2010); Federal Reserve Bank of New York, *Term Asset-Backed Securities Loan Facility: non-CMBS* (online at www.newyorkfed.org/markets/TALF_recent_operations.html) (accessed Dec. 10, 2010).

[xliv] This number is derived from the unofficial 1:10 ratio of the value of Treasury loan guarantees to the value of Federal Reserve loans under the TALF. U.S. Department of the Treasury, *Fact Sheet: Financial Stability Plan,* at 4 (Feb.10, 2009) (online at financialstability.gov/docs/fact-sheet.pdf) (describing the initial $20 billion Treasury contribution tied to $200 billion in Federal Reserve loans and announcing potential expansion to a $100 billion Treasury contribution tied to $1 trillion in Federal Reserve loans). Since only $43 billion in TALF loans remained outstanding when the program closed, Treasury is currently responsible for reimbursing the Federal Reserve Board only up to $4.3 billion in losses from these loans. Thus, the Federal Reserve's maximum potential exposure under the TALF is $38.7 billion. *See* Board of Governors of the Federal Reserve System, *Federal Reserve Announces Agreement with Treasury Regarding Reduction of Credit Protection Provided for the Term Asset-Backed Securities Loan Facility (TALF)* (July 20, 2010) (online at www.federalreserve.gov/newsevents/press/monetary/20100720a.htm); Board of Governors of the Federal Reserve System, *Factors Affecting Reserve Balances (H.4.1)* (Oct. 28, 2010) (online at www.federalreserve.gov/releases/h41/20101028/).

[xlv] No TARP resources were expended under the PPIP Legacy Loans Program, a TARP program that was announced in March 2009 but never launched. Since no TARP funds were allocated for the program by the time the TARP expired in October 2010, this or a similar program cannot be implemented unless another source of funding is available.

[xlvi] This figure represents Treasury's final adjusted investment amount in the Legacy Securities Public-Private Investment Program (PPIP). As of November 26, 2010, Treasury reported commitments of $14.9 billion in loans and $7.5 billion in membership interest associated with PPIP. *See* U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 23 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf). On January 4, 2010, Treasury and one of the nine fund managers, UST/TCW Senior Mortgage Securities Fund, L.P. (TCW), entered into a ''Winding-Up and Liquidation Agreement.'' U.S. Department of the Treasury, *Winding Up and Liquidation Agreement Between the United States Department of the Treasury and UST/TCW Senior Mortgage Securities Fund, L.P.* (Jan. 4, 2010) (online at financialstability.gov/docs/TCW%20Winding%20Up%20Agmt%20(Execution%20Copy)%20Redacted.pdf). Treasury's final investment amount in TCW totaled $356 million. Following the liquidation of the fund, Treasury's initial $3.3 billion obligation to TCW was reallocated among the eight remaining funds on March 22, 2010. *See* U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 23 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

On October 20, 2010, Treasury released its fourth quarterly report on PPIP. The report indicates that as of September 30, 2010, all eight investment funds have realized an internal rate of return since inception (net of any management fees or expenses owed to Treasury) above 19 percent. The highest performing fund, thus far, is AG GECC PPIF Master Fund, L.P., which has a net internal rate of return of 52 percent. U.S. Department of the Treasury, *Legacy Securities Public-Private Investment Program,* at 7 (Oct. 20, 2010) (online at financialstability.gov/docs/External%20Report%20-%2009-10%20vFinal.pdf).

[xlvii] As of November 26, 2010, the total cap for HAMP was $29.9 billion. The total amount of TARP funds committed to HAMP is $29.9 billion. However, as of December 2, 2010, only $728.9 million in non-GSE payments have been disbursed under HAMP. U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 45 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf); U.S. Department of the Treasury, *Troubled Assets Relief Program Monthly 105(a) Report—October 2010,* at 4 (Nov. 10, 2010) (online at financialstability.gov/docs/October%20105(a)%20Report.pdf); Data provided by Treasury (Dec. 3, 2010).

[xlviii] A substantial portion of the total $81.3 billion in debt instruments extended under the AIFP has since been converted to common equity and preferred shares in restructured companies. $8.1 billion has been retained as first-lien debt (with $1 billion committed to Old GM and $7.1 billion to Chrysler). This figure ($53.6 billion) represents Treasury's current obligation under the AIFP after repayments and losses. U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 18 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

[xlix] This figure represents Treasury's total adjusted investment amount in the ASSP. U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 19 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

[l] U.S. Department of the Treasury, *Troubled Asset Relief Program: Two Year Retrospective,* at 43 (Oct. 2010) (online at www.financialstability.gov/docs/TARP%20Two%20Year%20Retrospective_10%2005%2010_transmittal%20letter.pdf).

[li] U.S. Department of the Treasury, *Troubled Asset Relief Program Transactions Report for the Period Ending November 26, 2010,* at 17 (Nov. 30, 2010) (online at financialstability.gov/docs/transaction-reports/11-30-10%20Transactions%20Report%20as%20of%2011-26-10.pdf).

[lii] This figure represents the current maximum aggregate debt guarantees that could be made under the program, which is a function of the number and size of individual financial institutions participating. $286.8 billion of debt subject to the guarantee is currently outstanding, which represents approximately 57.1 percent of the current cap. Federal Deposit Insurance Corporation, *Monthly Reports Related to the Temporary Liquidity Guarantee Program: Debt Issuance Under Guarantee Program* (Oct. 31, 2010) (online at www.fdic.gov/regulations/resources/tlgp/total_issuance10-10.html). The FDIC has collected $10.4 billion in fees and surcharges from this program since its inception in the fourth quarter of 2008. Federal Deposit Insurance Corporation, *Monthly Reports Related to the Temporary Liquidity Guarantee Program: Fees Under Temporary Liquidity Guarantee Debt Program* (Oct. 31, 2010) (online at www.fdic.gov/regulations/resources/tlgp/fees.html).

[liii] This figure represents the FDIC's provision for losses to its deposit insurance fund attributable to bank failures in the third and fourth quarters of 2008; the first, second, third, and fourth quarters of 2009; and the first and second quarters of 2010. Federal Deposit Insurance Corporation, *Chief Financial Officer's (CFO) Report to the Board: DIF Income Statement—Second Quarter 2010* (Sept. 23, 2010) (online at www.fdic.gov/about/strategic/corporate/cfo_report_2ndqtr_10/income.html). For earlier reports, *see* Federal Deposit Insurance Corporation, *Chief Financial Officer's (CFO) Report to the Board* (Sept. 23, 2010) (online at www.fdic.gov/about/strategic/corporate/index.html). This figure includes the FDIC's estimates of its future losses under loss-sharing agreements that it has entered into with banks acquiring assets of insolvent banks during these eight quarters. Under a loss-sharing agreement, as a condition of an acquiring bank's agreement to purchase the assets of an insolvent bank, the FDIC typically agrees to cover 80 percent of an acquiring bank's future losses on an initial portion of these assets and 95 percent of losses on another portion of assets. *See, e.g.,* Federal Deposit Insurance Corporation, *Purchase and Assumption Agreement—Whole Bank, All Deposits—Among FDIC, Receiver of Guaranty Bank, Austin, Texas, Federal Deposit Insurance Corporation and Compass Bank,* at 65–66 (Aug. 21, 2009) (online at www.fdic.gov/bank/individual/failed/guaranty-tx_p_and_a_w_addendum.pdf).

[liv] Outlays are comprised of the Federal Reserve Mortgage Related Facilities. The Federal Reserve balance sheet accounts for these facilities under federal agency debt securities and mortgage-backed securities held by the Federal Reserve. Board of Governors of the Federal Reserve System, *Factors Affecting Reserve Balances (H.4.1)* (Dec. 2, 2010) (online at www.federalreserve.gov/releases/h41/20101202/) (accessed Dec. 3, 2010). Although the Federal Reserve does not employ the outlays, loans, and guarantees classification, its accounting clearly separates its mortgage-related purchasing programs from its liquidity programs. *See, e.g.,* Board of Governors of the Federal Reserve System, *Factors Affecting Reserve Balances (H.4.1),* at 2 (Dec. 2, 2010) (online at www.federalreserve.gov/releases/h41/20101202) (accessed Dec. 3, 2010).

[lv] Federal Reserve Liquidity Facilities classified in this table as loans include primary credit, secondary credit, central bank liquidity swaps, Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility, loans outstanding to Commercial Paper Funding Facility LLC, seasonal credit, term auction credit, the Term Asset-Backed Securities Loan Facility, and loans outstanding to Bear Stearns (Maiden Lane LLC). Board of Governors of the Federal Reserve System, *Factors Affecting Reserve Balances (H.4.1)* (Dec. 2, 2010) (online at www.federalreserve.gov/releases/h41/20101202/) (accessed Dec. 3, 2010). For further information, please see the data that the Federal Reserve recently disclosed on these programs pursuant to its obligations under the Dodd-Frank Wall Street Reform and Consumer Protection Act. Board of Governors of the Federal Reserve System, *Credit and Liquidity Programs and the Balance Sheet: Overview* (May 11, 2010) (online at www.federalreserve.gov/monetarypolicy/bst.htm); Board of Governors of the Federal Reserve System, *Credit and Liquidity Programs and the Balance Sheet: Reports and Disclosures* (Aug. 24, 2010) (online at www.federalreserve.gov/monetarypolicy/bst_reports.htm); Board of Governors of the Federal Reserve System, *Usage of Federal Reserve Credit and Liquidity Facilities* (Dec. 3, 2010) (online at www.federalreserve.gov/newsevents/reform_transaction.htm).

SECTION FIVE: OVERSIGHT ACTIVITIES

The Congressional Oversight Panel was established as part of the Emergency Economic Stabilization Act (EESA) and formed on November 26, 2008. Since then, the Panel has produced 25 oversight reports, as well as a special report on regulatory reform, issued on January 29, 2009, and a special report on farm credit, issued on July 21, 2009.

Upcoming Reports and Hearings

The Panel will release its next oversight report in January. The report will provide an update on government support for the domestic automotive industry via the TARP's Automotive Industry Financing Program. This will be the Panel's third report focusing on the AIFP, following its September 2009 and March 2010 oversight reports.[510]

The Panel will hold a hearing with Secretary Geithner in Washington on December 16, 2010. The Panel will ask the Secretary for a general update on the TARP, for information regarding the future plans for TARP investments following expiration of the program's authority on October 3, 2010, and for specific information pertaining to the topics of the Panel's recently published and forthcoming oversight reports. This will be the Secretary's fifth appearance before the Panel; his most recent appearance was on June 22, 2010.

[510] *See* Congressional Oversight Panel, *September Oversight Report: The Use of TARP Funds in Support and Reorganization of the Domestic Automotive Industry* (Sept. 9, 2009) (online at cop.senate.gov/documents/cop-090909-report.pdf); Congressional Oversight Panel, *March Oversight Report: The Unique Treatment of GMAC Under TARP* (Mar. 11, 2010) (online at cop.senate.gov/documents/cop-031110-report.pdf).

SECTION SIX: ABOUT THE CONGRESSIONAL OVERSIGHT PANEL

In response to the escalating financial crisis, on October 3, 2008, Congress provided Treasury with the authority to spend $700 billion to stabilize the U.S. economy, preserve home ownership, and promote economic growth. Congress created the Office of Financial Stability (OFS) within Treasury to implement the TARP. At the same time, Congress created the Congressional Oversight Panel to "review the current state of financial markets and the regulatory system." The Panel is empowered to hold hearings, review official data, and write reports on actions taken by Treasury and financial institutions and their effect on the economy. Through regular reports, the Panel must oversee Treasury's actions, assess the impact of spending to stabilize the economy, evaluate market transparency, ensure effective foreclosure mitigation efforts, and guarantee that Treasury's actions are in the best interests of the American people. In addition, Congress instructed the Panel to produce a special report on regulatory reform that analyzes "the current state of the regulatory system and its effectiveness at overseeing the participants in the financial system and protecting consumers." The Panel issued this report in January 2009. Congress subsequently expanded the Panel's mandate by directing it to produce a special report on the availability of credit in the agricultural sector. The report was issued on July 21, 2009.

On November 14, 2008, Senate Majority Leader Harry Reid and the Speaker of the House Nancy Pelosi appointed Richard H. Neiman, Superintendent of Banks for the State of New York, Damon Silvers, Director of Policy and Special Counsel of the American Federation of Labor and Congress of Industrial Organizations (AFL–CIO), and Elizabeth Warren, Leo Gottlieb Professor of Law at Harvard Law School, to the Panel. With the appointment on November 19, 2008, of Congressman Jeb Hensarling to the Panel by House Minority Leader John Boehner, the Panel had a quorum and met for the first time on November 26, 2008, electing Professor Warren as its chair. On December 16, 2008, Senate Minority Leader Mitch McConnell named Senator John E. Sununu to the Panel. Effective August 10, 2009, Senator Sununu resigned from the Panel, and on August 20, 2009, Senator McConnell announced the appointment of Paul Atkins, former Commissioner of the U.S. Securities and Exchange Commission, to fill the vacant seat. Effective December 9, 2009, Congressman Jeb Hensarling resigned from the Panel and House Minority Leader John Boehner announced the appointment of J. Mark McWatters to fill the vacant seat. Senate Minority Leader Mitch McConnell appointed Kenneth Troske, Sturgill Professor of Economics at the University of Kentucky, to fill the vacancy created by the resignation of Paul Atkins on May 21, 2010. Effective September 17, 2010, Elizabeth Warren resigned from the Panel, and on September 30, 2010, Senate Majority Leader Harry Reid announced the appointment of Senator Ted Kaufman to fill the vacant seat. On October 4, 2010, the Panel elected Senator Kaufman as its chair.

APPENDIX I: LETTER FROM SPECIAL MASTER PATRICIA GEOGHEGAN TO CHAIRMAN TED KAUFMAN RE: FOLLOW UP TO EXECUTIVE COMPENSATION HEARING, DATED NOVEMBER 18, 2010

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

November 18, 2010

Honorable Ted Kaufman
Chairman
Congressional Oversight Panel
732 North Capitol Street, NW
Room C-320
Washington, DC 20401

Re: Data Request

Dear Senator Kaufman:

Thank you for your interest in the work of the Office of the Special Master for TARP Executive Compensation. We have responded to each of your five data requests below to the best of our ability. Supporting details are provided in Attachments A through D as indicated below.

Turnover: How many employees left TARP exceptional assistance firms after the American Recovery and Reinvestment Act was passed? After the Interim Final Rule was passed in June 2009? After the Special Master issued his 2009 determinations? How does this data compare to expected turnover under "normal" conditions? In total, how many employees have left exceptional assistance firms as a result of the TARP's executive compensation restrictions?

- Turnover is reflected in the number of employees that depart an organization for a variety of reasons, including retirement, termination for cause, mutual termination, better opportunity and additional compensation. The Office of the Special Master did not collect information on the reasons for the departures or on departure rates in the past, which would be required in order to determine whether the turnover rates during this time period were considered "normal."
- Each exceptional assistance participant was required to submit the list of the five Senior Executive Officers and next twenty highest paid employees for 2009 and 2010. Each list is based on compensation from the prior year and includes only those employees employed as of January 1 of the given year. On August 14, 2009 the companies were required to deliver to the Office of the Special Master their submissions for the Special Master's 2009 determinations, including their proposals for compensation for those executives in the Top 25 still with the company as of that date. A second list of the Top 25 was submitted January 15, 2010 in preparation for the 2010 determinations. We know, based on the lists provided by the companies, that 40 of the Top 25 employees of the seven exceptional assistance participants resigned, retired or were fired between January 1 and August 14, 2009, and that 17 additional employees from the 2009 Top 25 group at the five remaining exceptional assistance companies left between the 2009

determinations and the 2010 submissions. Attachment A shows, for each exceptional assistance company, how many of the Top 25 as of January 1, 2009 were still employed on October 22, 2009. It also shows, for each of the five remaining exceptional assistance companies, how many of that group were still employed on March 23, 2010.

- The aggregate retention rate (percentage of the Top 25 remaining with the firm) for the seven companies between January 1, 2009 and October 22, 2009 is 77%. Consistent with the fact sheet released with the 2010 Top 25 determinations on March 23, 2010 and Special Master Feinberg's final report dated September 10, 2010, the aggregate retention rate for the remaining five exceptional assistance companies for the period between the Special Master's October 2009 determinations and the March 2010 determinations is 84%. See Attachment A for further details.

Individual compensation comparison: How did the Special Master's 2009 determinations for individual employees compare to their 2007 and 2008 salaries? The Special Master's determination letters provide this information in the aggregate, but not at an individual level. Individual names are not necessary, so long as some basis for comparison (such as employee identification numbers) is provided.

- The Office of the Special Master collected information on the pay levels for the Top 25 employees for the two years prior to 2009. In response to your request we have constructed a table for each 2009 exceptional assistance TARP recipient showing the percentage change in cash base salary and total direct compensation (cash base salary and short- and long-term bonuses in both cash and equity; for the 2009 figures, total direct compensation also includes stock salary) between 2007 and 2008 as compared to 2009. See Attachment B. Note: In keeping with the suggestion contained in your request, the chart in Attachment B contains different employee IDs and the order is changed from the published exhibits in the determination letters (which can be found in Attachments C and D) to prevent the inadvertent disclosure of confidential, non-public compensation information with respect to individuals. We have included all covered employees who were with the company for all three years.

2009 total compensation: What was the total compensation that covered employees received between January 1, 2009 and December 31, 2009? How much did each employee receive during the period between June 15, 2009 and the Special Master's determinations in October 2009?

- The 2009 total direct compensation including cash base salary, stock salary and long-term restricted stock for each of the Top 25 is reflected in Exhibit I of each of the 2009 determination letters, and is attached here as part of Attachment C for your convenience. As you will note, in many cases the total direct compensation column is not the sum of the other components for 2009. This is because the determination letters were released late in the year and some employees had different base salary levels prior to the determinations. This is explained in more detail on the exhibit. These numbers are in effect on a modified accrual basis rather than on a cash basis. They do not reflect grandfathered payments such as deferred compensation from prior years. In addition (a) the stock salary that vested in 2009 will be paid out over three or four years and (b) payment of the actual awards of 2009 long-term restricted stock (in contrast with the target amounts reflected in the exhibits) will be deferred for a minimum of two years and will not be made until the company has repaid its TARP obligations in 25% increments.

- Though the Office of the Special Master did not collect information on compensation paid between June 15, 2009 and October 2009, the Interim Final Rule states in part, "For the period from June 15, 2009 through the date of the Special Master's final determination, the TARP recipient will be treated as complying with this section if, with respect to employees covered by paragraph (a)(3)(i) of this section, the TARP recipient continues to pay compensation to such employees in accordance with the terms of employment as of June 14, 2009 to the extent otherwise permissible under this Interim Final Rule (for example, continued salary payments but not any bonus payments) and if, with respect to employees covered by paragraph (a)(3)(ii) of this section, the TARP recipient continues to pay compensation to such employees under the compensation structure established as of June 14, 2009, and if in addition the TARP recipient promptly complies with any modifications that may be required by the Special Master's final determination."

2010 total compensation: What is the total compensation that you anticipate covered employees will receive between January 1, 2010 and December 31, 2010?

- The total direct compensation for the 2010 Top 25 is reflected in Exhibit I of the 2010 determination letters included here as part of Attachment D. It should be noted that the long-term restricted stock is listed at the maximum target level and is dependent upon the individual's and/or the company's achieving predefined performance metrics in order to be earned. As in the case of the 2009 numbers in Attachment C, as described above, these numbers are in effect on a modified accrual basis.

General Motors determinations: The Special Master's 2009 determination letter for General Motors does not provide employee ID numbers, making it difficult to compare individual employee compensation in 2009 and 2010. How did compensation for individual employees at General Motors change between 2009 and 2010?

- All exceptional assistance organizations were instructed to provide employee IDs that could not be linked back to the employee in order to protect the privacy of the employee. On the morning of the release of the 2009 determination letters, General Motors realized they had provided the Office of the Special Master the actual employee IDs used by the firm's HR department. It was for this reason that the exhibit in the General Motors determination letter did not include employee IDs.

- General Motors had significant turnover in the Top 25 due primarily to a change in accounting as the firm went through bankruptcy (for a further explanation, see the footnote to the GM chart in Attachment C). Accordingly, we have highlighted those individuals who were in the Top 25 in both 2009 and 2010 on the General Motors exhibits included in Attachments C and D so that you may compare their compensation during the two periods.

My team and I are available to discuss and answer any questions you might have about the information provided.

Very truly yours,

Patricia Geoghegan

Patricia Geoghegan
Office of the Special Master for
TARP Executive Compensation

Page 5
Re: Data Request

Attachment A
Top 25 Turnover

Name of the Exceptional Assistance Recipient	2009 Top 25 Employees Included in the 2009 Determinations Issued October 22, 2009	Top 25 Employees Included in the 2009 Top 25 and Still Employed by the Company on March 23, 2010
AIG	13	8
Bank of America	13	NA*
Chrysler	24	20
Chrysler Financial	22	17
Citigroup	21	NA*
General Motors	20	19
GMAC	22	20

*Bank of America and Citigroup both paid back their Exceptional Assistance before submissions were due for 2010.

Page 6
Re: Data Request

Attachment B
2007 and 2008 Individual Compensation Compared to 2009

American International Group, Inc.*

	Cash Base Salary		Total Direct Compensation	
Employee ID	Percentage Change 2009 over 2008	Percentage Change 2009 over 2007	Percentage Change 2009 over 2008	Percentage Change 2009 over 2007
AIG1	-89%	0%	-98%	-91%
AIG2	-87%	0%	-98%	-89%
AIG3	-47%	0%	-98%	-85%
AIG4	-85%	0%	-98%	-87%
AIG5	-56%	0%	-97%	-89%
AIG6	-78%	-73%	-95%	-93%
AIG7	-30%	-30%	-86%	-79%
AIG8	-58%	-55%	-73%	-95%
AIG9	-50%	-43%	-69%	-89%
AIG10	-57%	-52%	350%	-26%
AIG11	-55%	-38%	387%	-10%
AIG12	-48%	-33%	575%	40%

*Certain executives evaluated solely on corporate results received no incentive compensation in 2008. As a result, 2009 total target compensation was higher than their total actual compensation received in 2008.

Bank of America Corporation*

	Cash Base Salary		Total Direct Compensation	
Employee ID	Percentage Change 2009 over 2008	Percentage Change 2009 over 2007	Percentage Change 2009 over 2008	Percentage Change 2009 over 2007
BoA1	-100%	-100%	-100%	-100%
BoA2	50%	50%	-76%	-76%
BoA3	50%	44%	-55%	-63%
BoA4	50%	50%	-54%	-72%
BoA5	49%	49%	-36%	-35%
BoA6	50%	50%	-28%	-83%
BoA7	50%	50%	-5%	-73%
BoA8	-38%	-38%	488%	-33%
BoA9	-38%	-38%	650%	9%

*Certain executives evaluated solely on corporate results received no incentive compensation in 2008. As a result, 2009 total target compensation was higher than their total actual compensation received in 2008.

Chrysler*

Employee ID	Cash Base Salary		Total Direct Compensation	
	Percentage Change 2009 over 2008	Percentage Change 2009 over 2007	Percentage Change 2009 over 2008	Percentage Change 2009 over 2007
Chrysler1	1%	3%	0%	2%
Chrysler2	3%	8%	0%	6%
Chrysler3	2%	3%	27%	29%
Chrysler4	2%	2%	27%	27%
Chrysler5	2%	4%	27%	30%
Chrysler6	2%	5%	27%	31%
Chrysler7	9%	18%	31%	41%
Chrysler8	19%	23%	35%	40%
Chrysler9	10%	19%	35%	46%
Chrysler10	21%	27%	38%	45%
Chrysler11	21%	29%	39%	48%
Chrysler12	32%	35%	40%	44%
Chrysler13	10%	20%	49%	64%
Chrysler14	10%	13%	58%	62%
Chrysler15	38%	43%	60%	66%
Chrysler16	32%	36%	65%	69%
Chrysler17	43%	47%	77%	83%
Chrysler18	74%	100%	125%	158%

*Chrysler did not pay their top executives a bonus in 2007 or 2008. The result is that 2009 total target compensation was higher than their total actual compensation in 2007 and 2008.

Chrysler Financial*		
	Cash Base Salary	**Total Direct Compensation**
Employee ID	Percentage Change 2009 over 2008	Percentage Change 2009 over 2008
ChryslerFin1	118%	-62%
ChryslerFin2	8%	-61%
ChryslerFin3	1%	-60%
ChryslerFin4	161%	-60%
ChryslerFin5	0%	-60%
ChryslerFin6	0%	-59%
ChryslerFin7	135%	-58%
ChryslerFin8	0%	-58%
ChryslerFin9	130%	-56%
ChryslerFin10	68%	-55%
ChryslerFin11	91%	-54%
ChryslerFin12	118%	-51%
ChryslerFin13	126%	-51%
ChryslerFin14	105%	-50%
ChryslerFin15	100%	-50%
ChryslerFin16	86%	-49%
ChryslerFin17	92%	-49%
ChryslerFin18	90%	-48%

*Chrysler Financial was created August 3, 2007. Consequently, there was not enough data for a full year 2007 to 2009 comparison.

Page 10
Re: Data Request

Citigroup Inc.*

Employee ID	Cash Base Salary: Percentage Change 2009 over 2008	Cash Base Salary: Percentage Change 2009 over 2007	Total Direct Compensation: Percentage Change 2009 over 2008	Total Direct Compensation: Percentage Change 2009 over 2007
Citi1	-100%	-100%	-100%	-100%
Citi2	171%	171%	-93%	-78%
Citi3	111%	111%	-76%	10%
Citi4	36%	36%	-75%	-39%
Citi5	171%	171%	-75%	-12%
Citi6	79%	78%	-41%	-65%
Citi7	111%	111%	-33%	-74%
Citi8	79%	78%	-33%	-40%
Citi9	111%	111%	-27%	251%
Citi10	111%	111%	-26%	-53%
Citi11	111%	111%	-22%	-65%
Citi12	111%	111%	-20%	-69%
Citi13	111%	111%	-20%	-79%
Citi14	90%	90%	-18%	-63%
Citi15	111%	111%	-11%	-74%
Citi16	111%	111%	-10%	-70%
Citi17	0%	122%	43%	-63%
Citi18	111%	111%	56%	-65%
Citi19	25%	25%	85%	8%

*Citigroup, like most financial services companies, had a compensation structure comprised of a very small base salary and large bonuses. The industry had, over time, taken on a practice of paying all or part of those bonuses, regardless of performance, because the base salary was not considered sufficient. We encouraged Citigroup to establish a more balanced compensation plan that going forward would provide them with a plan where incentives were paid upon successful completion of targets only. Citigroup set base salary by pay grade with all executives in the same pay grade having the same cash base salary, the net effect of this change resulted in the same increase for each executive in a particular grade.

General Motors

Employee ID	Cash Base Salary: Percentage Change 2009 over 2008	Cash Base Salary: Percentage Change 2009 over 2007	Total Direct Compensation: Percentage Change 2009 over 2008	Total Direct Compensation: Percentage Change 2009 over 2007
GM1	45%	50%	-40%	-30%
GM2	-47%	-28%	-36%	-20%
GM3	29%	40%	-30%	-28%
GM4	39%	39%	-27%	-23%
GM5	-44%	-17%	-26%	5%
GM6	62%	69%	-24%	-1%
GM7	5%	10%	-23%	4%
GM8	4%	6%	-18%	-16%
GM9	22%	23%	-15%	-26%
GM10	39%	44%	-14%	3%
GM11	43%	43%	-12%	-24%
GM12	8%	8%	-10%	-18%
GM13	69%	75%	-5%	-31%
GM14	19%	24%	-3%	-25%
GM15	8%	12%	-1%	-24%
GM16	59%	70%	6%	-9%
GM17	-30%	-30%	7%	-21%
GM18	14%	14%	13%	-3%

GMAC

Employee ID	Cash Base Salary: Percentage Change 2009 over 2008	Cash Base Salary: Percentage Change 2009 over 2007	Total Direct Compensation: Percentage Change 2009 over 2008	Total Direct Compensation: Percentage Change 2009 over 2007
GMAC1	5%	1%	-85%	-91%
GMAC2	0%	20%	-77%	-80%
GMAC3	5%	21%	-77%	-79%
GMAC4	-41%	-41%	-75%	-93%
GMAC5	25%	43%	-73%	-77%
GMAC6	4%	40%	-68%	-61%

Page 12
Re: Data Request

ATTACHMENT C
2009 Determination Exhibits

American International Group, Inc. 2009 Total Direct Compensation

Employee ID	Cash Salary (Rate going forward.)	Stock Salary (Performance based: The stock vests at grant and is redeemable in three equal, annual installments beginning on the 2nd anniversary of grant.)	Long-Term Restricted Stock (Performance based: Awarded based on achievement of objective performance goals. Vests after 3 years of service. Transferability dependent on TARP repayment.)	Total Direct Compensation (Cash salary paid to date plus two months at new run rate + stock salary + long-term restricted stock.)
1	$3,000,000	$4,000,000	$3,500,000	$10,500,000
110	$350,000	$100,000	$225,000	$675,000
137	$125,000	$0	$0	$125,000
145	$177,799	$0	$0	$177,799
150	$425,000	$0	$0	$425,000
157	$125,000	$0	$0	$125,000
163	$350,000	$3,725,000	$833,333	$4,558,333
182	$144,000	$0	$0	$144,000
188	$100,000	$0	$0	$100,000
206	$450,000	$5,600,000	$2,000,000	$7,600,000
209	$425,000	$0	$0	$425,000
255	$450,000	$0	$0	$450,000
267	$375,000	$4,358,333	$1,750,000	$6,108,333

Page 13
Re: Data Request

Bank of America Corporation 2009 Total Direct Compensation

Employee ID	Cash Salary (Rate going forward.)	Stock Salary (Performance based: The stock vests at grant and is redeemable in three equal, annual installments beginning on the 2nd anniversary of grant.)	Long-Term Restricted Stock (Performance based: Awarded based on achievement of objective performance goals. Vests after 3 years of service. Transferability dependent on TARP repayment.)	Total Direct Compensation (Cash salary paid to date plus two months at new run rate + stock salary + long-term restricted stock.)
1678	$0	$0	$0	$0
1029	$500,000	$1,750,000	$1,125,000	$3,375,000
1055	$403,847	$5,412,180	$2,851,923	$8,555,770
1108	$412,500	$1,914,583	$1,106,250	$3,318,750
1123	$300,000	$4,483,333	$2,350,000	$7,050,000
1143	$500,000	$9,900,000	$0	$9,900,000
1164	$500,000	$5,640,000	$3,001,250	$9,003,750
1227	$352,500	$4,797,917	$2,526,250	$7,578,750
1562	$500,000	$5,250,000	$0	$6,000,000
1564	$412,500	$5,114,583	$2,706,250	$8,118,750
1714	$403,847	$4,612,180	$2,451,923	$7,355,770
1787	$412,500	$2,114,583	$1,206,250	$3,618,750
1850	$500,000	$3,950,000	$0	$4,700,000

Chrysler 2009 Total Direct Compensation

Employee ID	Cash Salary (Rate going forward.)	Stock Salary (Performance based: The stock vests at grant and is redeemable in three equal, annual installments beginning on 2nd anniversary of grant.)	Long-Term Restricted Stock (Performance based: Awarded based on achievement of objective performance goals. Vests after 3 years of service. Transferability dependent on TARP repayment.)	Total Direct Compensation (Cash salary paid to date plus two months at new run rate + stock salary + long-term restricted stock.)
TRP001	$0	$0	$0	$0
TRP002	$500,000	$34,001	$102,002	$644,336
TRP003	$0	$0	$0	$2,150,000
TRP004	$485,000	$197,253	$0	$694,756
TRP005	$485,000	$105,000	$107,002	$626,175
TRP006	$455,000	$84,000	$102,002	$620,175
TRP007	$440,000	$29,334	$88,002	$503,169
TRP008	$435,000	$29,001	$87,002	$463,503
TRP009	$410,000	$27,334	$82,002	$490,169
TRP010	$410,000	$27,334	$82,002	$511,003
TRP011	$410,000	$27,334	$82,002	$511,003
TRP012	$405,000	$27,000	$81,001	$508,835
TRP013	$400,000	$0	$0	$391,667
TRP014	$479,300	$25,667	$77,002	$503,393
TRP015	$370,000	$0	$0	$365,833
TRP016	$335,000	$22,334	$67,002	$416,003
TRP017	$315,000	$21,000	$63,001	$394,835
TRP018	$315,000	$21,000	$63,001	$357,341
TRP019	$310,700	$20,714	$62,141	$389,388
TRP020	$310,000	$20,667	$62,002	$380,169
TRP021	$295,000	$19,667	$59,001	$369,501
TRP022	$290,000	$19,334	$58,001	$334,018
TRP023	$280,000	$18,667	$56,001	$350,501
TRP024	$280,000	$18,667	$56,001	$350,501
TRP025	$310,000	$20,667	$62,002	$359,336

Page 15
Re: Data Request

Chrysler Financial 2009 Total Direct Compensation

Employee ID	Cash Salary (Rate going forward.)	Stock Salary (Performance based: The stock vests at grant and is redeemable in three equal, annual installments beginning on 2nd anniversary of grant.)	Long-Term Restricted Stock (Performance based: Awarded based on achievement of objective performance goals. Vests after 3 years of service. Transferability dependent on TARP repayment.)	Total Direct Compensation (Cash salary paid to date plus two months at new run rate + stock salary + long-term restricted stock.)
A216G8	$1,500,000	$0	$0	$875,000
A224F7	$216,000	$0	$0	$216,000
A272C1	$800,000	$0	$0	$466,667
A288A8	$400,000	$0	$0	$218,667
A296A7	$432,000	$0	$0	$252,500
B225F8	$1,350,000	$0	$0	$704,167
B233F7	$410,000	$0	$0	$246,753
B241E6	$415,000	$0	$0	$250,767
B249D5	$490,000	$0	$0	$265,167
C250D6	$216,000	$0	$0	$216,000
C258D5	$490,000	$0	$0	$268,587
C298A9	$400,000	$0	$0	$245,667
D203H4	$194,436	$0	$0	$194,436
E212G4	$182,496	$0	$0	$182,496
E220G3	$410,000	$0	$0	$272,083
E236E1	$500,000	$0	$0	$500,003
F245E1	$410,000	$0	$0	$246,533
F253D9	$443,000	$0	$0	$234,263
G206H7	$490,000	$0	$0	$261,667
H207H8	$175,872	$0	$0	$175,872
H231F5	$425,000	$0	$0	$237,833
H279B8	$600,000	$0	$0	$300,000

Page 16
Re: Data Request

Citigroup Inc. 2009 Total Direct Compensation

Employee ID	Cash Salary (Rate going forward.)	Stock Salary (Performance based: The stock vests at grant and is redeemable in three equal, annual installments beginning on the 2nd anniversary of grant.)	Long-Term Restricted Stock (Performance based: Awarded based on achievement of objective performance goals. Vests after 3 years of service. Transferability dependent on TARP repayment.)	Total Direct Compensation (Cash salary paid to date plus two months at new run rate + stock salary + long-term restricted stock.)
100001	$1	$0	$0	$1
100004	$475,000	$5,433,333	$2,850,000	$8,550,000
100005	$500,000	$3,400,000	$1,950,000	$5,850,000
100006	$0	$0	$0	$0
100007	$475,000	$5,629,167	$3,000,000	$9,000,000
100008	$475,000	$3,733,333	$2,000,000	$6,000,000
100009	$475,000	$3,979,167	$2,133,333	$6,400,000
100010	$475,000	$5,699,390	$3,000,000	$9,000,000
100011	$475,000	$4,683,333	$2,475,000	$7,425,000
100013	$475,000	$5,399,390	$2,850,000	$8,550,000
100014	$475,000	$5,733,333	$3,000,000	$9,000,000
100015	$475,000	$4,400,000	$2,333,333	$7,000,000
100017	$475,000	$3,200,000	$1,733,333	$5,200,000
100019	$475,000	$3,000,000	$1,633,333	$4,900,000
100020	$475,000	$2,845,833	$1,556,250	$4,668,750
100021	$475,000	$1,775,000	$1,000,000	$3,000,000
100022	$475,000	$2,520,000	$1,393,333	$4,180,000
100023	$475,000	$3,733,333	$2,000,000	$6,000,000
100025	$475,000	$250,000	$237,500	$712,500
100075	$500,000	$5,062,500	$2,666,667	$8,000,000
100107	$500,000	$2,916,666	$1,666,667	$5,000,000

Page 17
Re: Data Request

General Motors 2009 Total Direct Compensation*

Employee ID	Cash Salary (Rate going forward.)	Stock Salary (Performance based: The stock vests at grant and is redeemable in three equal annual installments beginning on 2nd anniversary of grant.)	Long-Term Restricted Stock (Performance based: Awarded based on achievement of objective performance goals. Vests after 3 years of service. Transferability dependent on TARP repayment.)	Total Direct Compensation (Cash salary paid to date plus two months at new run rate + stock salary + long-term restricted stock.)
	$950,000	$2,421,667	$1,815,000	$5,445,000
	$400,000	$88,317	$233,408	$700,225
	$450,000	$137,717	$224,908	$674,225
	$353,333	$11,567	$172,533	$517,600
1731	$750,000	$436,467	$493,858	$1,481,575
	$276,667	$96,041	$183,021	$549,062
	$500,000	$316,222	$426,994	$1,280,883
	$433,333	$312,894	$314,342	$943,025
6335	$500,000	$576,667	$630,000	$1,881,000
6610	$443,333	$194,594	$241,475	$724,425
	$326,667	$123,091	$190,296	$570,887
	$313,333	$131,357	$181,928	$545,785
	$233,333	$61,967	$145,733	$437,200
	$500,000	$353,300	$365,158	$1,095,475
	$426,667	$186,817	$277,658	$832,975
9635	$500,000	$279,778	$353,889	$1,061,667
	$306,667	$79,517	$173,008	$519,025
	$294,500	$38,967	$166,733	$500,200
	$276,667	$187,250	$204,875	$614,625
3394	$500,000	$409,222	$526,319	$1,578,958

Indicates that this employee was in the Top 25 in both 2009 and 2010. The IDs for these employees match their IDs used for 2010. IDs are not provided for all other employees, because GM provided actual employee identifying information, so Treasury does not have randomly generated IDs for these individuals.

*Under the Recovery Act, Top 25 executives are identified using SEC executive compensation disclosure rules to determine which executives had the highest annual compensation. Under SEC rules, the amount of an executive's annual compensation from equity awards is measured based on FAS 123R accounting expense recognized by the company in a given year. In 2008, previously granted performance equity awards held by GM corporate executives suffered substantial decreases in value which, under the accounting standards, caused a corresponding decrease in the annual compensation levels of the executives. Employees of a division within GM that was traditionally paid entirely or almost entirely in cash were not similarly affected by these accounting standards. As a result, these employees had annual compensation levels higher than more senior corporate executives and were thus included in the Top 25. In 2009, the accounting effect was not repeated, and the 2010 Top 25 population was composed of the more traditional corporate executives.

Page 18
Re: Data Request

GMAC 2009 Total Direct Compensation

Employee ID	Cash Salary (Rate going forward.)	Stock Salary (Performance based: The stock vests at grant and is redeemable in three equal annual installments beginning on 2nd anniversary of grant.)	Long-Term Restricted Stock (Performance based: Awarded based on achievement of objective performance goals. Vests after 3 years of service. Transferability dependent on TARP repayment.)	Total Direct Compensation (Cash salary paid to date plus two months at new run rate + stock salary + long-term restricted stock.)
582903	$850,000	$4,491,667	$2,816,667	$8,450,000
129881	$400,000	$588,333	$415,000	$1,320,000
151695	$500,000	$1,858,333	$1,088,000	$3,363,000
172265	$500,000	$2,730,000	$1,615,000	$4,845,000
197253	$500,000	$1,941,667	$1,050,000	$3,325,000
250095	$500,000	$4,437,500	$2,500,000	$7,500,000
265383	$375,000	$445,833	$400,000	$1,200,000
353403	$365,000	$646,111	$500,000	$1,500,000
391076	$450,000	$1,133,333	$725,000	$2,225,000
398005	$450,000	$625,833	$500,000	$1,530,000
501828	$450,000	$1,850,000	$1,150,000	$3,450,000
509014	$400,000	$852,278	$618,000	$1,855,000
513416	$450,000	$880,000	$665,000	$1,995,000
546145	$500,000	$1,641,667	$1,216,667	$3,650,000
555076	$480,000	$1,029,167	$750,000	$2,255,000
682168	$600,000	$3,083,333	$1,716,667	$5,150,000
699403	$380,000	$483,783	$420,000	$1,270,000
725547	$450,000	$1,220,833	$825,000	$2,475,000
805106	$500,000	$2,208,333	$1,300,000	$3,925,000
921597	$400,000	$1,149,872	$665,000	$2,070,000
936790	$400,000	$1,141,667	$725,000	$2,225,000
964006	$450,000	$2,391,667	$1,400,000	$4,200,000

Page 19
Re: Data Request

ATTACHMENT D
2010 Determination Exhibits

American International Group, Inc. 2010 Total Direct Compensation

Employee ID	Cash Salary	Stock Salary (Performance based: The stock vests at grant and is redeemable in three equal, annual installments beginning on the 2nd anniversary of grant.)	Long-Term Restricted Stock (Performance based: Awarded based on achievement of objective performance goals. Generally vests after 3 years of service. Transferability dependent on TARP repayment.)	Total Direct Compensation (Cash salary + stock salary + long-term restricted stock.)
1	$3,000,000	$4,000,000	$3,500,000	$10,500,000
133	$450,000	$4,062,500	$1,500,000	$6,012,500
134	$700,000	$3,050,000	$1,250,000	$5,000,000
145	$177,799	$3,322,201	$0	$3,500,000
147	$241,933	$758,067	$0	$1,000,000
157	$125,000	$3,468,750	$0	$3,593,750
163	$495,000	$4,485,000	$1,020,000	$6,000,000
182	$450,000	$3,062,500	$0	$3,512,500
186	$450,000	$1,437,500	$625,000	$2,512,500
188	$100,000	$3,500,000	$0	$3,600,000
192	$700,000	$2,000,000	$0	$2,700,000
196	$495,000	$3,731,250	$1,375,000	$5,601,250
206	$700,000	$5,000,000	$1,900,000	$7,600,000
217	$1,500,000	$2,520,000	$1,980,000	$6,000,000
236	$475,000	$2,156,250	$875,000	$3,506,250
237	$495,000	$3,656,250	$850,000	$5,001,250
243	$500,000	$1,300,000	$0	$1,800,000
261	$475,000	$4,568,750	$0	$5,043,750
267	$495,000	$5,149,000	$1,156,000	$6,800,000
534	$312,500	$0	$0	$312,500
1056	$475,000	$2,967,932	$854,000	$4,296,932
1057	$442,874	$2,117,126	$640,000	$3,200,000

Chrysler 2010 Total Direct Compensation

Employee ID	Cash Salary	Stock Salary (Performance based: The stock vests at grant and is redeemable in five equal, annual installments beginning on the 1st anniversary of grant.)	Long-Term Restricted Stock (Performance based: Awarded based on achievement of objective performance goals. Generally vests after 3 years of service. Transferability dependent on TARP repayment.)	Total Direct Compensation (Cash salary + stock salary + long-term restricted stock.)
TRP001	$0	$0	$0	$0
TRP002	$500,000	$180,000	$340,000	$1,020,000
TRP005	$485,000	$145,500	$315,250	$945,750
TRP006	$455,000	$150,150	$302,575	$907,725
TRP009	$410,000	$135,300	$272,650	$817,950
TRP010	$410,000	$61,500	$235,750	$707,250
TRP011	$400,000	$144,000	$272,000	$816,000
TRP012	$405,000	$0	$0	$405,000
TRP014	$385,000	$138,600	$261,800	$785,400
TRP016	$335,000	$110,550	$222,775	$668,325
TRP017	$315,000	$85,085	$200,030	$600,115
TRP018	$315,000	$85,050	$200,025	$600,075
TRP019	$310,704	$0	$0	$310,704
TRP020	$310,000	$115,200	$212,600	$637,800
TRP021	$295,008	$0	$0	$295,008
TRP022	$290,004	$104,400	$197,200	$591,604
TRP023	$280,008	$100,800	$190,400	$571,208
TRP024	$280,008	$0	$0	$280,008
TRP025	$310,000	$102,300	$206,150	$618,450
TRP026	$270,000	$97,200	$183,600	$550,800
TRP028	$265,008	$100,800	$182,900	$548,708
TRP029	$265,032	$95,412	$180,220	$540,664
TRP030	$265,032	$95,412	$180,220	$540,664
TRP055	$325,000	$87,750	$206,375	$619,125

Chrysler Financial 2010 Total Direct Compensation*

Employee ID	Cash Salary	**Stock Salary** (Performance based: The stock vests at grant and is redeemable in five equal, annual installments beginning on the 1st anniversary of grant.)	**Long-Term Restricted Stock** (Performance based: Awarded based on achievement of objective performance goals. Generally vests after 3 years of service. Transferability dependent on TARP repayment.)	**Total Direct Compensation** (Cash salary + stock salary + long-term restricted stock.)
A216G8	$1,650,000	$0	$0	$1,650,000
A200H1	$495,000	$0	$0	$495,000
A224F7	$237,600	$0	$0	$237,600
A232F6	$270,864	$0	$0	$270,864
A272C1	$880,000	$0	$0	$880,000
A288A8	$440,000	$0	$0	$440,000
A296A7	$475,200	$0	$0	$475,200
B225F8	$1,485,000	$0	$0	$1,485,000
B241E6	$456,500	$0	$0	$456,500
B249D5	$539,000	$0	$0	$539,000
C234F8	$451,000	$0	$0	$451,000
C258D5	$539,000	$0	$0	$539,000
C298A9	$440,000	$0	$0	$440,000
D211H3	$240,570	$0	$0	$240,570
D235F0	$451,000	$0	$0	$451,000
E204H5	$440,000	$0	$0	$440,000
E220G3	$451,000	$0	$0	$451,000
E236E1	$550,004	$0	$0	$550,004
F213G5	$265,216	$0	$0	$265,216
F245E1	$451,000	$0	$0	$451,000
F253D9	$487,300	$0	$0	$487,300
F285B5	$282,150	$0	$0	$282,150
G206H7	$539,000	$0	$0	$539,000
H231F5	$467,500	$0	$0	$467,500
H279B8	$660,000	$0	$0	$660,000

*Note that Chrysler Financial exited Exceptional Assistance in May 2010.

General Motors 2010 Total Direct Compensation

Employee ID	Cash Salary	Stock Salary (Performance based: The stock vests at grant and is redeemable in five equal, annual installments beginning on the 1st anniversary of grant.)	Long-Term Restricted Stock (Performance based: Awarded based on achievement of objective performance goals. Generally vests after 3 years of service. Transferability dependent on TARP repayment.)	Total Direct Compensation (Cash salary + stock salary + long-term restricted stock.)
7924	$1,700,000	$5,300,000	$2,000,000	$9,000,000
0012	$450,000	$433,000	$441,000	$1,324,000
0017	$495,000	$2,639,750	$0	$3,134,750
0135	$490,000	$691,400	$590,600	$1,772,000
0417	$450,000	$281,000	$350,000	$1,081,000
0542	$800,000	$1,333,250	$1,000,000	$3,133,250
1731	$495,000	$1,683,866	$0	$2,178,866
2346	$485,000	$745,883	$566,667	$1,797,550
2387	$495,000	$802,450	$600,000	$1,897,450
2983	$375,000	$308,888	$0	$683,888
2986	$700,000	$1,212,183	$866,667	$2,778,850
3317	$900,000	$3,373,700	$2,000,000	$6,273,700
3348	$600,000	$791,417	$633,333	$2,024,750
3394	$300,000	$250,000	$0	$550,000
4894	$495,000	$958,383	$666,667	$2,120,050
5360	$375,000	$467,600	$0	$842,600
5434	$580,000	$1,040,100	$280,000	$1,900,100
5697	$600,000	$1,070,233	$766,667	$2,436,900
6335	$495,000	$935,783	$666,667	$2,097,450
6447	$495,000	$702,450	$550,000	$1,747,450
6524	$495,000	$701,200	$550,000	$1,746,200
6610	$450,000	$631,000	$500,000	$1,581,000
7231	$750,000	$3,450,000	$2,000,000	$6,200,000
9635	$490,000	$607,000	$500,000	$1,597,000

Indicates that this employee was in the Top 25 in both 2009 and 2010.

Page 23
Re: Data Request

GMAC 2010 Total Direct Compensation

Employee ID	Cash Salary	Stock Salary (Performance based: The stock vests at grant and is redeemable in five equal, annual installments beginning on the 1st anniversary of grant.)	Long-Term Restricted Stock* (Performance based: Awarded based on achievement of objective performance goals. Generally vests after 3 years of service. Transferability dependent on TARP repayment.)	Total Direct Compensation (Cash salary + stock salary; excluding potential long-term restricted stock.)
280677	$0	$8,000,000		$8,000,000
151695	$500,000	$1,858,333		$2,358,333
166144	$500,000	$900,000		$1,400,000
197253	$500,000	$1,941,667		$2,441,667
250095	$500,000	$4,437,500		$4,937,500
265967	$500,000	$2,350,000		$2,850,000
339212	$500,000	$4,437,500		$4,937,500
354392	$450,000	$1,000,000		$1,450,000
391076	$450,000	$1,133,333		$1,583,333
501828	$450,000	$1,850,000		$2,300,000
509014	$400,000	$852,278		$1,252,278
513416	$450,000	$880,000		$1,330,000
546145	$500,000	$1,641,667		$2,141,667
555076	$480,000	$1,029,167		$1,509,167
567303	$400,000	$1,300,000		$1,700,000
682168	$500,000	$3,183,333		$3,683,333
707713	$400,000	$1,000,000		$1,400,000
710047	$500,000	$1,300,000		$1,800,000
725547	$450,000	$1,220,833		$1,670,833
746382	$400,000	$1,000,000		$1,400,000
805106	$500,000	$2,208,333		$2,708,333
921597	$400,000	$1,149,872		$1,549,872
936790	$400,000	$1,141,667		$1,541,667
964006	$450,000	$2,391,667		$2,841,667

*In the March 23, 2010 GMAC 2010 Top 25 determination letter, the Special Master footnoted GMAC's determination on long-term restricted stock. Though no long-term restricted stock grants were identified in Exhibit I, the Special Master allowed for GMAC's compensation committee to grant up to $12.5M of incentives to employees for achievement of objective individual performance goals. Any additional long-term restricted for incentive grants will be determined at the end of 2010 based on Company performance, subject to Special Master approval.