January 13, 2009

The Honorable Christopher Dodd, Chairman
Committee on Banking, Housing, and Urban Affairs
U.S Senate
Washington, DC 20510

The Honorable Richard Shelby, Ranking Member
Committee on Banking, Housing, and Urban Affairs
U.S. Senate
Washington, DC 20510

Dear Chairman Dodd and Ranking Member Shelby:

The Troubled Asset Relief Program (TARP) must include a foreclosure prevention program that requires those who receive funding to engage in streamlined loan modification efforts. This TARP program must be implemented quickly, whether through an agreement with the Obama Administration on core principles or through legislation consistent with the concepts in Title II of Chairman Frank's H.R. 384. The following core principles, aimed at achieving sustainable, broad-based loan modifications, are reflected in Chairman Frank's bill and are critical to any effort made through TARP to stem foreclosures:

- **Implement a quid pro quo policy for TARP funding**. Financial institutions that own mortgages or a mortgage servicing operation should not be eligible for TARP funds without agreeing to a foreclosure prevention program. There is already precedent for this very action when Citigroup recently agreed to expedite modifications as a condition of its second receipt of TARP funds. Subsequent TARP expenditures, however, including the recent $6 billion to GMAC, which owns GMAC Residential Capital LLC, one of the nation's largest mortgage servicers, have lacked the foreclosure prevention condition, leaving a patchwork approach, inconsistent standards, and varying expectations. The Citigroup condition, which serves as a simple and effective template, required that Citi would abide by the protocols established by the FDIC in its work on the IndyMac mortgage portfolio, which represents an economically rational approach to loss mitigation. The FDIC has developed a loan modification spreadsheet protocol which provides a win/win solution: new loan terms which will return more to the investor than a foreclosure and which are affordable—and thus sustainable—for the homeowner. Given this good product, Treasury should ensure that *no recipient of TARP funds may foreclose on any principal residence unless the FDIC loan modification protocol does not produce a loan modification, or the homeowner has defaulted on such a loan modification.*

- **Provide incentives to servicers to modify loans.** The current compensation structure for servicers creates a perverse incentive for foreclosure rather than engaging in foreclosure prevention. Servicers are often not paid for modifications, but are reimbursed for foreclosure costs. Moreover, it often is easier and faster for a servicer to recover amounts advanced to the investor on behalf of the borrower when the servicer proceeds to foreclosure, rather than when the servicer provides a loan modification. As a result, servicers face financial disincentives to engage in loan modifications, even if investors fare better if foreclosure were avoided. Direct payments to servicers for substantive loan modifications should be made competitive with those for foreclosures and short sales. Treasury already has the authority to do this under the existing TARP legislation and through its conservatorship of the GSEs, and as such, these incentives should be incorporated into the agreement with the Administration.

We are pleased that Title II of H.R. 384 signals Chairman Frank's belief that $40-100 billion of TARP funding should be set aside for foreclosure relief programs and that Treasury should develop and fund a plan by April 1, preferably at the behest of the FDIC. To date, TARP funds have been utilized exclusively for the benefit of the financial sector with virtually no conditions placed on the funding other than interest and preferred shares, and minor limits on executive compensation. American taxpayers, homeowners, and the economy would be much better served if this funding were leveraged to achieve industry changes that are absolutely essential to fixing the foreclosure mess and bringing our economy out of a tailspin.

In addition to working quickly with the Administration to ensure that financial institutions receiving TARP funding—both already disbursed and yet to be disbursed—aggressively modify loans, Congress must also act quickly to remove some key obstacles to effective loan modifications. Therefore, we ask you to work with the Administration to achieve the following other programmatic objectives:

- **Provide for meaningful protection for servicers when they modify loans.** One obstacle to servicers in modifying loans is that they fear lawsuits by investors adversely affected by their decision. Congress should protect servicers who avoid foreclosures by acting reasonably in modifying or selling any loan under the Treasury program. Unless Congress provides adequate liability protections, servicers will remain unwilling to modify troubled loans in the face of potential investor litigation.

- **Provide that continued Real Estate Mortgage Investment Conduit (REMIC) status be contingent on modifying PSAs to allow for economically rational modifications**. Currently, some pooling and servicing agreements (PSAs) place restrictions on loan modifications. Congress should provide that for trusts to retain their status (and future tax benefits) as REMICs, their PSAs must not restrict modifications that would benefit the investors as a whole.

- **Ensure income tax burdens do not undermine sustainability of loan modifications.** Under current law, when a homeowner is provided with a loan modification containing a principal write-down or a significant interest rate reduction, the IRS considers the homeowner to have received taxable cancellation of indebtedness income unless the mortgage debt is “qualified” under the terms of the Mortgage Forgiveness Debt Relief Act of 2007 or the homeowner is insolvent. In many instances, the prospect of tax liability discourages homeowners from seeking a modification, or, if such a modification is obtained, the resulting tax liability could cause the homeowner to re-default on the loan. Congress should remedy this inadvertent consequence by amending the law to remove the requirement to file Form 1099 with the IRS when canceling any mortgage-related debt and modifying the definition of “qualified mortgage debt” to include all mortgage debt, not just acquisition debt.

- **Increase foreclosure mitigation counseling to $600 million and legal assistance to $60 million.** Isolated and fearful borrowers will continue to need assistance in order to work with their servicer and will need trusted third party advice, such as that provided by nonprofit housing counseling agencies, before they will be willing to sign workout agreements. Funding should be directed to the HUD housing counseling program and include a set-aside for organizational capacity building to fund staff management, internal training, technology, and equipment as well as community outreach to reach underserved and isolated borrowers. A significant funding stream will assist nonprofit agencies as they struggle to keep capacity apace with demand for foreclosure prevention services, which are often specialized and time-intensive. In addition, $60 million of funding should be allocated to attorneys at non-profit organizations providing foreclosure mitigation legal assistance, including foreclosure defense work. Housing counselors, who play a vital role in helping at-risk homeowners, are unfortunately limited in their ability to pursue federal and state legal claims for abusive lending practices. Legal Aid and other non-profit lawyers, with their experience in representing homeowners and their legal knowledge of state and federal consumer protections, have the unique ability to change that equation and force recalcitrant servicers into creating loans that allow homeowners to remain in their homes and in their communities.

- **Provide for judicial modification of loans**. It is critical to provide a backstop to protect those homeowners whose lenders cannot or will not agree to voluntarily modify their loans, either through the TARP initiative or otherwise, when the homeowner could sustain a market rate mortgage. The best and only solution in these cases is to lift the ban on judicial modifications and allow a bankruptcy court to implement an economically rational solution that otherwise would be lost.

Last month, Credit Suisse released a report that projected 8 million foreclosures over the next four years unless current industry practices change. Alternatively, according to the same report, should the mortgage industry stop foreclosing on families with unaffordable loans and instead provide them with affordable modifications, up to 4 million of those foreclosures could be prevented. While a staggering number of foreclosures would still occur, the prospects for our nation’s economic recovery would be much improved. In the vast majority of cases, a successful modification under affordable terms represents a significantly reduced loss to investors when compared to a foreclosure in this down market.  Modifying loans to prevent foreclosures is good for investors, homeowners, the communities, and the economy. More than a year into this crisis, we know that voluntary industry efforts are simply not up to the task and a broader federal intervention is required.

Congress again has the opportunity to take long-term, streamlined, affordable loan modifications to scale by refocusing TARP on fixing the foreclosure crisis, either through a substantive agreement with the Obama Administration on principles or through legislation, and by taking other legislative measures to remove barriers to modifications. We look forward to discussing these issues further.  Should you need additional information, please contact Brenda Muñiz, ACORN, at 202.547.2500 or via email: bmuniz@acornmail.net.

Sincerely,

ACORN
Center for Responsible Lending (CRL)
Consumer Action
Consumer Federation of America
Consumers Union
Greenlining Institute
Lawyers' Committee for Civil Rights Under Law
Leadership Conference on Civil Rights (LCCR)
National Association of Consumer Advocates (NACA)
National Association of Consumer Bankruptcy Attorneys
National Community Reinvestment Coalition (NCRC)
National Consumer Law Center (on behalf of its low-income clients)
National Council of La Raza (NCLR)
National Fair Housing Alliance (NFHA)
National NeighborWorks Association
PICO National Network
National Training and Information Center
Public Citizen
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