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Subcommittee on Housing, Transportation, and Community Development

Hearing: Helping Responsible Homeowners Save Money Through Refinancing

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Good morning Chairman Menendez, Ranking Member DeMint, and Members of the Subcommittee. Thank you for inviting me to testify at today's hearing on efforts to help homeowners refinance their mortgages through responsible streamlined refinance policies.

I am President of the Center for Responsible Lending (CRL), a nonprofit, nonpartisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is an affiliate of Self-Help, a nonprofit community development financial institution. For thirty years, Self-Help has focused on creating asset-building opportunities for low-income, rural, women-headed, and minority families, primarily through financing safe, affordable home loans. In total, Self-Help has provided over $6 billion of financing to almost 70,000 low-wealth families, small businesses and nonprofit organizations in North Carolina and across America.

In my comments today, I will highlight the following points:

- First, time is still of the essence to improve the housing market and prevent foreclosures, because the foreclosure crisis is far from being over. Research completed by CRL shows that the foreclosure crisis is around the halfway point for borrowers with loans originated during 2004-2008.

- Second, foreclosure prevention efforts, including initiatives to help homeowners refinance their mortgage, are necessary and still needed. Access to the Home Affordable Refinance Program (HARP) is particularly important for underwater homeowners and those homeowners still in a mortgage with harmful features – including hybrid adjustable rate mortgages (ARMs) and mortgages with high interest rates. Opening up the refinance market to millions of American families paying above market interest rates and currently prevented from refinancing is a common-sense step that will prevent foreclosures, improve homeowners' financial situation and help the economy.

- Third, while the improvements made in HARP 2 are significant, more should still be done to increase refinancing access to underwater borrowers and homeowners with mortgages that have harmful features. This includes taking steps to increase lender competition, further streamline the refinance process and coordinate HARP outreach with other foreclosure prevention programs. Additionally, CRL supports Congressional action to expand refinancing opportunities through FHA for borrowers with mortgages that are not owned or guaranteed by the GSEs or FHA.

1. The U.S. is not yet halfway through the foreclosure crisis

I'd like to begin my comments today by putting the current status of the housing market in context. Last year, the Center for Responsible Lending published research showing that the nation is not yet halfway through the foreclosure crisis. CRL's research, which is detailed in our *Lost Ground* report, shows that for mortgages made during the height of the lending boom that occurred between 2004 and 2008, 8.3% of these loans were at least 60 days delinquent or in the foreclosure process as of February 2011. This represents another 3.6 million households that could possibly lose their homes. This is on top of the 6.4% of mortgages – totaling 2.7 million households – identified in CRL's study that have already gone through foreclosure. Because our research focused only on 2004-2008 originations, these estimates are likely to be on the conservative side. For example, Moody's has reported the completion of 5 million foreclosures or short sales.

In addition to highlighting the scope of the ongoing foreclosure crisis, CRL's research also makes important findings about who is likely to be affected by foreclosure. Our *Lost Ground* research confirms that higher foreclosure rates and serious delinquency rates are linked to mortgages with one of the following characteristics: having been originated by a mortgage broker, containing hybrid or option ARMs, having prepayment penalties, and featuring high interest rates (subprime loans). Homeowners with mortgages that have one of these features are much more likely to be seriously delinquent and at risk of foreclosure than homeowners in a 30-year fixed-rate mortgage without a prepayment penalty.

CRL's analysis in *Lost Ground* also confirms that foreclosures and mortgage delinquencies continue to have a disproportionate impact on African-American and Latino borrowers. This disparity persists when comparing borrowers with higher incomes. CRL's research also demonstrates that African-American and Latino borrowers were much more likely to receive mortgages with harmful features as described above. For example, African-American and Latino borrowers with FICO scores above 660 were three times as likely to have a high interest rate mortgage than white borrowers in the same credit range.

The research published in *Lost Ground* is CRL's latest effort to document the harmful impact of predatory and subprime lending. In fact, this research builds on and updates CRL's 2006 study entitled *Losing Ground*, which estimated that predatory lending would lead to approximately 2.2 million foreclosures of subprime mortgages. While CRL correctly predicted a likely foreclosure crisis, the number of foreclosures has unfortunately been much larger than forecast, in part because the crisis spread beyond the subprime market and into the broader housing market.

As homeowners and communities struggle with ongoing foreclosures, we encourage Members of this Subcommittee to continue all efforts to find solutions that help families stay in their homes and prevent as many foreclosures as possible.

2. **Supporting mortgage refinancing is a needed policy tool to avoid foreclosures and help homeowners obtain less expensive and more stable mortgages.**

Interest rates are currently at historic lows, but many homeowners who stand to benefit from these low rates have not refinanced their existing, higher-rate mortgage. Making refinancing more accessible for underwater homeowners and those homeowners in mortgages with harmful features should be an essential component of preventing foreclosures.

Millions of families across the country have seen the value of their homes plummet over the last five years. According to the Fiserv Case-Shiller house price index, housing prices have fallen by one-third since the first quarter of 2006, and the statistics released yesterday show that the housing market is still struggling. In the years leading up to the housing market collapse, homeowners took out mortgages while home prices were increasing. Unsustainable lending driven by Wall Street investment bank demand for risky mortgages regardless of whether borrowers could afford the loans fueled the housing bubble. The subsequent drop in housing prices is a market price correction of the housing bubble that has harmed current homeowners through no fault of their own.

Decreased home prices have created complications for many homeowners trying to refinance their mortgage. Homeowners have lost over $7 trillion in home equity since the housing market collapse, and approximately 11 million homeowners are now estimated to be underwater on their mortgage, meaning that their mortgage balance is greater than the value of their home. As a result, many of these homeowners have been unable to refinance their mortgage because they now have a high loan-to-volume (LTV) ratio well above standard underwriting requirements.

Racial and ethnic differences in refinancing rates are a less-discussed aspect of this issue, but an important one to examine. Home Mortgage Disclosure Act (HMDA) data show that while the number of refinance applications for Asian and non-Hispanic white borrowers increased between 2008 and 2010, the number of refinance applications for African-American and Latino borrowers actually decreased. In addition, CRL analysis shows that among borrowers current on mortgage payments through February 2011, African-American and Latino borrowers remained more likely to be paying toward a high-interest (subprime) loan than Asian and non-Hispanic white borrowers. While not conclusive, these data suggest that many African-American and Latino borrowers would benefit from refinancing at today's historically low interest rates, but that there remains significant frictions in the refinance market that have prevented them from doing so.

The Federal Housing Finance Agency's announcement last year to expand HARP to all underwater borrowers was a strong step in the right direction. The initial HARP program was limited to borrowers with a maximum LTV of 125%, and the revisions made in "HARP 2" have removed this high-LTV restriction. HARP 2 program changes went into effect on December 1, 2011.

The changes in HARP 2 have the potential to help underwater borrowers and borrowers in mortgages with harmful features gain better access to refinancing opportunities. To date, the majority of borrowers entering into a HARP refinance fall between 80-105% LTV. Since its inception in 2009 through February 2012, more borrowers with an LTV between 80-105% benefited from HARP refinances (1.01 million) than underwater borrowers with an LTV above 105% (110,000). However, progress is being made with the improvements in HARP 2: more borrowers with an LTV above 105% refinanced under HARP in January and February 2012 than in any prior month.

3. **Further improvements to HARP 2 should be designed to maximize participation by underwater homeowners and those homeowners still in a mortgage with harmful features.**

While the changes implemented in HARP 2 are very positive, we believe that FHFA should take additional steps to expand access to streamlined refinances of mortgages owned or guaranteed by Fannie Mae or Freddie Mac. There is an urgent need to prevent as many foreclosures as possible, and CRL supports changes that will maximize the participation of underwater borrowers and those with mortgages that have harmful features. Expanded access to streamlined refinances – along with principal reduction in certain circumstances, principal forbearance, and mortgage modifications – is an important part of the solution.

Although FHFA has the authority to implement most of the suggestions detailed below, in the meantime we also believe that the Menendez-Boxer Discussion Draft would go a long way to further improving borrower access to streamlined refinances.

First, CRL supports efforts to increase competition in offering HARP refinances, which would result in better pricing and greater access to refinancing opportunities. One way to accomplish this goal is by putting servicers on par with one another regarding the waiver of representations and warranties liability. Frequently called "reps and warranties," these statements require servicers to buy back a mortgage if it later falls short of the characteristics promised when it was originated. As Laurie Goodman has highlighted in her research, servicers participating in HARP currently have reduced reps and warrants liability if they are refinancing a mortgage already in their servicing portfolio. However, servicers taking on a new mortgage to refinance maintain full reps and warranties liability. Ms. Goodman and her colleagues have persuasively argued that this differential treatment reduces competition and, therefore, increases the cost of HARP refinances.

Second, expanding HARP to all borrowers – regardless of LTV ratio – would likely have several benefits. One benefit would be further streamlining the refinance process by eliminating differences between Fannie Mae and Freddie Mac's versions of HARP. It also would allow borrowers who don't reach 80% LTV on their first mortgage but have a combined LTV above 80% when factoring in a second mortgage to qualify for HAMP refinances. This would put these borrowers on par with borrowers over 80% LTV on a first mortgage alone. Lastly, it would allow lower LTV borrowers who are unable to access this market to actually obtain a refinance and at a lower cost.

Third, the Menendez-Boxer Discussion Draft language concerning resubordination of second liens would also contribute to streamlining the refinance process for these borrowers.

In addition to the Menendez-Boxer Discussion Draft language concerning outreach to eligible borrowers, CRL encourages Fannie Mae, Freddie Mac and FHFA to make every effort to coordinate their HARP outreach efforts with other federal agencies administering housing initiatives. HARP is one part of a broader list of foreclosure prevention initiatives, including the Independent Foreclosure Review tied to the April 2011 Consent Orders between the banking regulators and mortgage servicers; the Attorneys Generals and Administration settlement involving refinancing and principal reduction; FHA refinancing initiatives; and mortgage modifications through HAMP. Coordinated outreach will help reach borrowers possibly eligible for HARP or another program.

Finally, we support the Administration's proposal to pay the closing costs of borrowers who refinance into shorter-term mortgages in order to encourage principal reduction through quicker amortization. The debt overhang facing borrowers needs to be addressed through various means, and this is an important approach.

Given capacity constraints that would be further heightened by some of these proposals, we do have concerns about opening up HARP to investment properties. While investors would benefit from lower rates and tenants are harmed when their landlords are foreclosed upon, we believe the needs facing owner-occupants are so significant that servicer capacity should continue to be focused on this group.

On top of the HARP improvements outlined above, CRL believes several additional points merit further thought and consideration. One is paying attention to whether lenders are adding overlays that limit HARP's reach to underwater borrowers. It is especially important for the refinancing market to serve underwater borrowers while also serving those borrowers with a lower LTV ratio. Additionally, in developing HARP outreach materials for eligible borrowers, we believe that refinancing costs and fees should be included in these materials in addition to the estimated monthly savings.

I want to end on a final point that also merits additional Congressional action, which is expanding streamlined refinances to borrowers in mortgages that are not owned or guaranteed by the GSEs or FHA. The Administration’s proposal to provide these borrowers with streamlined refinancing opportunities through FHA would help both underwater borrowers and those borrowers currently in mortgages with harmful features, such as subprime mortgages. Every effort should be made to reach these borrowers with responsible refinancing opportunities.

Thank you for the opportunity to present this testimony before the Subcommittee today, and I look forward to your questions.