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**HOME FORECLOSURES: WILL VOLUNTARY MORTGAGE
MODIFICATION HELP FAMILIES SAVE THEIR HOMES?**

**BEFORE THE
SUBCOMMITTEE ON ADMINISTRATIVE AND COMMERCIAL LAW
HOUSE OF REPRESENTATIVES JUDICIARY COMMITTEE**

JULY 9, 2009

Mr. Chairman, members of the subcommittee, I would like to thank you for the invitation to appear this afternoon to describe our experience with voluntary mortgage modifications particularly since the Making Homes Affordable plan (“MHAP”) came into effect on March 4 of this year.

My name is Irwin Trauss, I am an attorney. I supervise the Consumer Housing Unit of Philadelphia Legal Assistance (PLA), an LSC funded program in Philadelphia, Pennsylvania. I have had this position at PLA for the past 13 years. For the previous 20 years I worked for Community Legal Services (CLS) in Philadelphia in a similar capacity. For almost thirty three years I have primarily represented low income homeowners faced with the loss of their homes through mortgage foreclosure, litigating as necessary in state, federal and bankruptcy court. In addition, I have overall responsibility for the operation of the Save Your Home Philly Hotline which over the past 15 months, as part of the Philadelphia Court of Common Pleas Mortgage Foreclosure Diversion Pilot Program, has handled about 10,000 calls from Philadelphia homeowners facing the loss of their homes to foreclosure.¹ Since April of 2008 every person faced with the imminent loss of his or her home through foreclosure has been referred by the

¹ Since May of 2008, the Hotline has received an average of between 600 and 700 calls a month. Paralegals who work under the supervision of attorneys whom I supervise take the calls. The paralegals on the Hotline triage the calls. They explain the diversion program; make appointments for the callers with housing counselors; and provide information and advice to housing counselors. In appropriate cases they refer the homeowners to the legal services attorneys at PLA or CLS for representation. In a small number of cases they make referrals to private attorneys. The Hotline staff also monitors the operation of the Diversion Program and provides feedback to the Court on behalf of homeowners for whom the Diversion Program has not worked as intended. I and attorneys I supervise, or attorneys from CLS with whom we work closely, help train the volunteer attorneys and the housing counselors. At least one attorney from my unit is present in court every day on which conciliation conferences are scheduled to take place to mentor pro bono attorneys and as a resource for the housing counselors. Finally, I and the attorneys and substantive paralegals in my unit undertake extended representation, which can include litigation, in about 200 new cases a year.

Court to the Hotline. As a result we have an intimate sense of what is happening with foreclosures in Philadelphia.

I understand I have been invited to testify to provide the perspective of someone who day in and day out represents homeowners attempting to stay in their homes. From that perspective, the answer to the question that underlies this hearing is that voluntary modifications will not help families save their homes in the numbers required to significantly stem the tide of foreclosures. Voluntary modifications will only help at the margins. Substantive changes in the law, such as the proposed amendments to the Bankruptcy Code that require loans to be modified to make them affordable, are needed to prevent foreclosures in the numbers necessary to prevent the further erosion of our communities. Unless homeowners have leverage to force favorable results, lenders will continue to avoid the meaningful modifications that are necessary to keep folks in their homes.

While Making Homes Affordable (MHAP) has made a significant difference in a small percentage of the cases that we have seen in Philadelphia, it has not resulted in a significantly greater willingness on the part of servicers to enter into modifications that meaningfully reduce monthly payments. It has also not resulted in a willingness of lenders to reduce the principal due or even to reduce the amount of principal subject to interest.

I say this based not only on my personal experience, but based on the information I glean in my role as the supervisor of the Hotline and from my involvement in the creation and operation of the Diversion Program.

The Hotline is run by Philadelphia Legal Assistance with funding primarily from the Philadelphia Office of Housing and Community Development. The Hotline is an instrumental part of the Philadelphia Court of Common Pleas Mortgage Foreclosure Diversion Pilot Program

- a program designed to reduce the number of homes lost to foreclosure by requiring lenders to meet with homeowners to explore alternatives before a judgment can be entered and before a sheriff sale of the property can take place. You may have heard of this program as it has received a great deal of media attention and has been touted as a solution to the foreclosure epidemic².

Under the Philadelphia Diversion Program, in each foreclosure case a conciliation date is scheduled. The court provides notice to the homeowner of the date along with a notice to contact the Hotline. As part of the program the homeowners are referred to housing counselors who help them put together affordable proposals that will enable them to stay in their homes. The proposals are submitted to the mortgage servicer and to the attorney representing the servicer, who are supposed to respond with a counter proposal. If there is a gap between the proposal and the counter proposal, the homeowner can appear on the date set for the conciliation conference and take advantage of available volunteer “judges pro tem” appointed by the Court to assist the parties in reaching an affordable sustainable agreement by bridging the gap between the respective proposals. Under the program the housing counselor is expected to accompany the homeowner to the conciliation conference and pro bono attorneys are supposed to be available to represent the homeowners at the conferences.

At bottom, though, this process is voluntary and a resolution cannot be imposed upon an unwilling mortgagee. It has been my experience that, absent external pressure, i.e. absent

² Legislation has been introduced in the Senate (Residential Diversion and Mortgage Loan Modification Act of 2008) to encourage duplication of the program nationwide. I believe this legislation, while well intended, is a distraction from the more pressing need for changes in substantive law that would require mortgage holders to modify mortgages when necessary to make them affordable

some leverage that can be applied by the homeowners or on the homeowners' behalf, lenders are not ordinarily willing to significantly compromise the mortgages to make them affordable over the long run. They usually do so when they are forced to, either by an aggressive advocate, by the prospect of litigation, by litigation that frustrates their attempts to foreclose or by pressure applied directly or indirectly, often discretely, by the Court or the judges pro tem through the Diversion Program.

The implementation of MHAP has resulted in some delays in foreclosures that have been helpful to homeowners, but it has not meaningfully affected this dynamic. It is clear that with or without MHAP homeowners represented by knowledgeable advocates backed up by counsel prepared to litigate get resolutions that are simply not available to a homeowner who is not so represented.

In the Diversion Program when servicers, through their attorneys, make loan modification proposals, it is not unusual for the proposal to contain provisions that may deprive the homeowner of rights they are entitled to under applicable law and that increase the overall obligation, at the same time the proposal might lower the monthly payment. For example, I have seen servicers repeatedly offer modifications of FHA loans with interest rates that are in excess of the maximum rate permitted by the FHA for a modification. And I have seen new loan balances that include fees and costs in excess of the amount permitted by the mortgage document itself and by the FHA regulations.

The arrival of MHAP has not significantly affected the way the mortgage servicers and their counsel operate. It is but one more program with which servicers and their attorneys have to be forced to comply. And with which they will refuse to comply if it suits their purpose to do so.

For example, though the Servicer Participation Agreement (SPA) Bank of America (BoA) has signed with FNMA requires it to participate in the Home Affordable Modification Program (HAMP), callers to the Hotline report that Bank of America refuses to send them HAMP applications when their loans are not owned by FNMA and FHLMC. Hotline paralegals, calling on behalf of clients, have been told repeatedly by BoA loss mitigation employees that only GSE-owned loans are eligible for HAMP. Bank of America is openly violating the terms of the contract it signed with FNMA, foreclosing on homeowners entitled to the benefits of HAMP as if the program did not exist.

Mortgage servicers such as Saxon Mortgage, after an initial moratorium on the foreclosure sale of homes brought about by its signing the SPA, simply reject homeowners for consideration under HAMP, for no reason that is in any way connected with the program requirements, with no notice of any kind to the homeowner or to her counsel. I recently had a case in which Saxon's attorney advised me that my client would not be considered under HAMP because she "did not meet the debt to income ratios of the program." My request for further explanation, of which "ratios" the attorney was referring to, went unanswered. Because HAMP is not transparent, particularly in the application of the Net Present Value Test (NPV), and appears to require no notice to a homeowner who is turned down, it is difficult if not impossible to challenge a lender's refusal to agree to a modification. The forum in which the challenge can be mounted is not clear and it is certainly not clear that a foreclosure sale can be prevented while the challenge is brought.

It is not unusual for the homeowner to get no notice that the servicer has concluded that HAMP is unavailable other than to learn that the house is back on the sheriff sale list, which is what happened in my case.

The whimsical nature of the lender's decision to refuse to engage in a HAMP modification is also brought home by a recent case handled by an attorney whom I supervise, which involved Wells Fargo. The homeowner's request to be considered under HAMP was denied because according to Wells Fargo "[h]er debt to income ratio for the mortgage alone is over 70%. Her monthly mortgage payment cannot be lowered to bring it within HAMP guidelines and still payoff the mortgage debt." There was no suggestion that the NPV test was implicated or that the NPV test was even done. The reason given for the denial was nonsensical in light of the HAMP requirement that anyone with a mortgage payment exceeding 31% of gross income is eligible for consideration for a reduction of the mortgage payment to 31% and for the subsequent application of the NPV test. Nonetheless, Wells Fargo only relented from its position that HAMP was unavailable and the house would be sold, when it was embarrassed into doing so when we brought its position to the attention of a representative of FNMA during a fortuitous fact finding trip he was making to Philadelphia. Wells Fargo reversed itself, decided the client is eligible for HAMP, postponed the sheriff sale and is redoing its calculations. Had the homeowner been without counsel, as most are, her home would have gone to foreclosure sale earlier this week.

Arbitrarily, servicers exclude whole classes of homeowners from consideration under HAMP.³ Thus many servicers refuse to consider modifying the loans of folks who have

³HAMP by its express terms excludes a large class of folks who are most in need of help. It does little for a person at 200% of poverty whose mortgage payments may be less than 31% of her income, but are still unaffordable because the remaining 69% of income is insufficient to cover the cost of food, clothing, transportation, utilities and other minimum basic necessities of life. HAMP also is of little help to someone who is back to work after building up a large arrearage because of a disruption in income resulting from illness or unemployment, but because of the resumption in income cannot meet the 31% of income test.

inherited their homes or obtained them as the result of property settlements resulting from divorce. The servicers take this position because in such a case the owner of the property is not a party to the underlying note, even if she has been paying it for years. HAMP permits no such exclusion.

Absent significant leverage on the part of homeowners to force a change in behavior, the majority of servicers will continue to find ways to avoid meaningful modifications despite HAMP. The only way to change their behavior to the extent required to make meaningful modifications common is to provide the homeowner with leverage over the servicer, such as the threat of a bankruptcy judge imposing a modification. The availability of such an option for homeowners would likely complement voluntary programs such as HAMP and the Diversion Program and substantially increase the chances that meaningful long-lasting modifications will result.

In closing I'd like to thank you again for the invitation to share my experience with you. I would be happy in the future to provide any information which might be of assistance to this subcommittee in its attempt to pass legislation that will stem the steadily rising tide of foreclosures that is causing so much harm to our nation.