Testimony of Matthew J. Mason, UAW-GM Legal Services Plan Before the United States House of Representatives, Committee on the Judiciary

"H.R. 200, "Helping Families Save Their Homes in Bankruptcy Act of 2009" and H.R. 225, "Emergency Homeownership and Equity Protection Act"

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My name is Matthew J. Mason and I am an Assistant Director of the UAW-GM Legal Services Plan located in Detroit, Michigan.

I wish to thank the Chairman, Mr. Conyers, the ranking member, Mr. Smith and all of the members of the Committee for allowing me to testify today on behalf of the UAW-GM Legal Services Plan concerning the two bills pending before this committee, H.R. 200, "Helping Families Save Their Homes in Bankruptcy Act of 2009" and H.R. 225, "Emergency Homeownership and Equity Protection Act." These bills address what is one of the most pressing issues of my legal career, the unrelenting pace of mortgage foreclosures and the failure of any voluntary system of modifications to arrest this crisis which is now in its third year nationally and what seems like forever in Michigan. This statement reflects my views on this current crisis and does not and is not intended in any way to reflect the views of the General Motors Corporation or any of its subsidiaries or the International Union, UAW.

I have been a practicing attorney and administrator for almost 35 years. I have been active in the practice of bankruptcy law for over 30 years and previously testified before this Committee in 1998 on what became the far reaching amendments to the bankruptcy code that took effect in 2005.

The UAW-GM Legal Services Plan and its sister Plans, provide legal services to over 700,000 eligible UAW members on a wide variety of subjects. We have 65 offices in 20 states that handle all types of non fee generating civil matters. In the housing area, we handle buys and sells, loan modifications, work out agreements, deeds in lieu of foreclosure as well as provide foreclosure defense for active workers and retirees alike. We also provide legal services for bankruptcy, but only as a last resort.

I also currently serve as a member of the Board of Directors of the National Association of Consumer Bankruptcy Attorneys (NACBA), an organization of over 3300 consumer bankruptcy attorneys located in all fifty states and Puerto Rico.

I believe that these bills deserve your support, if for no other reason, than the simple fact that both bills allow bankruptcy judges the power in Chapter 13 to modify mortgages on personal residences. This power is necessary to break the unabated flood of mortgage foreclosures and end the barriers to meaningful, voluntary modifications outside of bankruptcy.

I. The Voluntary Loan Modification Programs Are Not Working

In preparation for NACBA's 16th Annual Conference in May 2008 I surveyed both our legal plan attorneys and the members of NACBA to determine what was actually happening inside and outside of bankruptcy concerning loan modifications.

In early 2008 pressure had been mounting on mortgage companies to rewrite the loans not only to reflect economic reality but also to keep from adding to the volumes of foreclosed homes already on the market.

By May of 2008 our legal plan attorneys reported that in most cases lenders were offering forbearance agreements, with no changes in term, interest rate, principal reductions or changing the term of the loan. The terms of the forbearance agreements also varied greatly, from adding a few payments to the end of the loan to allowing an arrears to be paid over a period of time, perhaps as much as a year.

They also reported some very modest success in obtaining a meaningful modification, typically where a variable rate mortgage was converted to a 30 year fixed, arrears either waived or added to the end of the terms and a modest reduction in the principal balance.

However counterbalancing those cases were modification proposals that were unreasonable, such as one where the lender wanted upfront money before they would even process a loan modification. ($6000 in 5 days.)

I also surveyed the NACBA membership who reported similar results, though not even as encouraging. Specifically, they reported in early 2008 that:

1. About 60% of the attorneys assisted with loan modification for clients, whether in or outside of bankruptcy.

2. The vast majority of responders (68%) said that they obtained modifications in less than 10% of the cases.

3. When they referred clients to mortgage counselors, virtually all of the clients came back. Again the vast majority responded (78%) that less than 10% of those clients received a modification through a mortgage counselor.

4. Modifications on average took more than 4 weeks, and many of them took in excess of six weeks.

5. In about 30% of the cases where a modification was available, the lender required that the bankruptcy be dismissed.

6. In cases where the lender required dismissal of the bankruptcy, it caused almost 75% of those clients to reject the modification.

7. Many modifications involved interest rate reductions, 75% of which were reduced by 4% or less.

8. Interest rates for ARM's were typically frozen for the life of the loan.

9. In the few cases where principal was reduced, in 85% of the cases the reduction was for $30,000 or less.

By the summer of 2008 even those limited successes seemed to evaporate. Our legal plan attorneys reported that meaningful modifications seemed to grind to a halt. The initial problem with not being able to reach lenders continued. By the end of 2008 our bankruptcy filing rate increased and our percentage of Chapter 13 cases where we could save the home decreased.

In the last few days I re-surveyed the NACBA membership and my staff to see what experience they were having with loan modifications in late 2008 and early 2009.

The results are unchanged if not worse. My staff reported that effective modifications, typically involving a long term rate reduction and decrease in principal were nonexistent. In a few instances they were able to accomplish those modifications but only after initiating some kind of litigation proceeding, such as an objection to a claim, a forced modification in bankruptcy or an adversary proceeding alleging some kind of fraud in the transaction.

The survey of NACBA attorneys produced a similar picture of fewer modifications being offered with poorer terms. For modifications obtained from October 1, 2008 to the present, they reported:

1. Less than ten percent (10%) of their clients who need a modification obtained one.

2. Even after the clients were referred to loan counselors, still less than ten percent (10%) received loan modifications.

3. The approval rates for modification have actually decreased from early 2008. 64.7 % of the respondents reported that approval rates for modification dropped since October 1, 2008.

4. The time to complete a modification has increased. 56.7% of the respondents reported that it took in excess of six weeks to get a modification approved as compared to 38. 6 % who responded to the same question in April, 2008.

5. A higher percentage of lenders are now requiring borrowers to dismiss their bankruptcy petitions before giving a modification. (42.2% in 2009 and 28.4% in 2008) In both cases, the overwhelming majority still reported that the requirement to dismiss the bankruptcy resulted in the client rejecting the modification and surrendering the home. (88.9% in 2009 and 73.9% in 2008).

6. Most modifications still involved interest rate reductions, but even there, the size of the rate reduction decreased. Relatively few borrowers received a decrease in excess of 2% and almost no borrowers received a rate decrease of 4% or more.

7. The length of time interest rates were frozen decreased. Now more attorneys reported that the rate was frozen for three years or less, not the life of the loan. In 2008 the overwhelming majority (87%) reported that the rate was frozen for the term of the loan. In 2009 that decreased to 42%.

8. The respondents still reported very few reductions in the principal balance of loans and then only in relatively small amounts, under $30,000.

In a couple of instances the lenders were taking an even harder line. In one case a large lender in the FDIC program offered to reduce the borrower's payments for a few years, provided he prove monthly income of at least double what he actually has (and which he had on the date of loan origination) while proposing to increase his mortgage balance by more than $84,000.

II. New Mortage Foreclosures Continue To Be A Serious Problem In 2009.

In his recent article, *Rewriting Contracts, Wholesale Data on Voluntary Mortgage Modifications from 2007 and 2008 Remittance Reports, (Working Draft)*, Alan M. White, Assistant Professor Valpariso School of Law, Professor White undertook an empirical review of loan modification data taken from subprime lender reports to its investors. In the article he concluded that the foreclosure crisis continued unabated thorough June, 2008.

Professor White found that the number of mortgage defaults and foreclosures increased steadily in the 2007-2008 time frame. In July 2007 the average delinquency rate in the mortgagte pools he studied was 19%. In addition 1.4% of all loans entered into foreclosure that month. That translated into a 16.8% annual rate of new foreclosures as a percentage of that portfolio.

By June 2008 he found that the delinquency rate had nearly doubled to 34% and new foreclosures were occuring at an annual rate of 27%.

In an article from January 15, 2009 the Associated Press just reported that mortgage foreclosure rates doubled in 2008 compared to 2007

" WASHINGTON - More than 2.3 million American homeowners faced foreclosure proceedings last year, an 81 percent increase from 2007, with the worst yet to come as consumers grapple with layoffs, shrinking investment portfolios and falling home prices.

Nationwide, more than 860,000 properties were actually repossessed by lenders, more than double the 2007 level, according to RealtyTrac, a foreclosure listing firm based in Irvine, Calif., which compiled the figures."

Our experience locally supports those findings. For example, for the first six months of 2007 there had been 28,075 foreclosures in Detroit and Wayne County Michigan, a 26% increase over the last six months of 2006, and over 90% of them in the City of Detroit. There were over 14,000 properties listed for sale on foreclosure.com just in Wayne County Michigan.

Now in January, 2009 Wayne County still has almost 12,000 homes listed on for sale on a single website, foreclosure.com. Nationally over 2.2 million homes are listed for sale on this same site as homes in some stage of foreclosure.

In reviewing our local Detroit Legal News we found that on January 20, 2009 there were 551 homes slated for foreclosure sale, all of them in Wayne County. On a daily basis now homes were added to the list at an alarming rate.

In just six days, from January 12, 2009 through January 19, 2009 there were, on average, 126 homes each day listed for foreclosure sale for the first time

Professor White also sees no bottoming out of the foreclosure crisis at least as of June, 2008. As credit for refinancing dried up and borrowers have become less credit worthy because of job losses, cuts in wages and hours, the mortgage foreclosure rates increased into June 2008.

III. The Modifications Offered Do Not Solve The Problem

Professor White also noted that the modifications currently being offered do not solve the fundamental problem, that is lower the payment to an affordable rate as well as reduce the principal balance to reflect the market value of the home.

Most of the modifications involved recasting arrears, which is adding delinquent payments to the balance of the loan or a modest, temporary reduction in the

interest rate. Very few loans had principal balances reduced. Furthermore in 23% of the reported modifications, the monthly payment even increased. Page 20-21.

Professor White concluded that, at best, the current modification programs were only putting off the day of reckoning. He stated at page 27:

"More importantly, homeowners have not been relieved of the devalued debt, either through completed foreclosures sales or loan concessions. Many are still stuck in a "sweat box" struggling to pay above-market interest rates on above-market loans."

Therefore it would not be surprising to see even those borrowers who are listed as having "modified" their loan, default in the future, placing that home in the new foreclosure start category.

Finally Professor White noted in his research that there was no consistency among servicers in their approach to loan modifications. Our experience bears that out as well.

For example, in Saginaw, Michigan a foreclosure case was commenced for a client who was behind on their mortgage. We were told by the foreclosing attorneys that we had to deal with the servicer directly. We called the mortgage company and asked for loss mitigation. They said they would send a loan modification application but that it would take 30 days or more to process. We asked for an adjournment of the mortgage sale to allow time to process the modification. Three (3) times we called the person with the authority to adjourn and each time we got the voice mail message that the voice mail box was full. We faxed a request for an adjournment but received no response. We filed the loan modification application but have not received a response. In the meantime the loan is proceeding through the foreclosure process.

In Dearborn, Michigan we applied for a modification to stop another sale. We were able to reach that company but they only offered to suspend payments for three (3) months and then add those three months to the existing arrears. The effect would have just been to increase the total amount due. There was no offer to reduce the interest rate, principal or amount of monthly payments.

Even when we try loss mitigation such as deeding the property back to the lender we have run into great difficulties. In one case out of Indiana we initially asked for a loan modification which was denied. We then offered to provide the lender with a deed in lieu of foreclosure. Now eighteen months later the mortgage company has yet to complete the documents to accept the deed in lieu of foreclosure, even though no payments are being made.

Talking with local loan counselors confirmed my view that some large lending institutions are actually getting worse in their modification practice. They have

hired outside firms to do loss mitigation and are adding the fees of those firms onto the modification. They only offer interest rate reductions and then not much. They will still not talk to borrowers who are not yet in default. Even if they are in default, the response from the lender typically comes within days of the foreclosure sale, if at all.

IV. Modifying Mortgage Loans On Personal Residences In Bankruptcy Is The Only Proposal That Gives Homeowners Rights They Can Enforce.

Currently the various proposals for loan modifications all start with an application to the lender. The lender determines who gets the modification, what kind it is and for how long it will last. It has been our experience that the modification terms vary wildly between clients, for no apparent reason. The modification terms also do not take into account, in most instances, the value of the property and what the borrower can really afford.

As a consequence borrowers are often encouraged to abandon their homes, especially when they can rent or perhaps even buy a new home in the same neighborhood for a fraction of the cost of their existing home. However that process is slow and has enormous costs. There are costs to foreclose, costs to move and costs to maintain abandoned properties that will never be recovered. In addition neighborhoods continue to deteriorate and house values continue to fall.

Allowing a borrower to propose their own modification in bankruptcy puts a plan on the table that actually assigns a value to the collateral, and then proposes to pay the loan based on current market interest rates. The plan has to be feasible and is tailored to the borrower's income and expenses. That information is subject to verification through the six months of pay stubs that are required to be filed in every bankruptcy. Tax returns must also be filed. If there is a dispute as to the value of the house, appraisals will be typically exchanged, with the judge having the final decision.

Lenders still have the possibility of recovering some of their losses. The existing loan is split into two parts, secured and unsecured. The creditor always maintains a claim for the unsecured balance of the loan. Payments are mandated on the unsecured balance if the debtor's income or assets warrant it. Furthermore borrowers and lenders could agree to a claw back provision that could return equity to the lender if the home appreciated.

V. Bankruptcy Provides A Uniform Solution To The Foreclosure Crisis And Cuts Through All The Problems Of Lender Cooperation

Bankruptcy also provides a uniform solution to the foreclosure crisis. Your loan is not evaluated from the lender's perspective that might include the fear of being

sued by their investors. Instead it is open to any borrower who has income and can qualify. They propose a plan, it is confirmed or not and the case moves on. Currently bankruptcy courts process hundreds of thousands of Chapter 13 plans each year. The issues presented by modifications are quite familiar to them.

A Chapter 13 modification also addresses the issues of lender liability. Servicers have already been sued on the basis that their voluntary loan modification programs exceed the authority granted to them. To the extent that the threat of suit by investors has negatively impacted the scope of modification programs, bankruptcy eliminates that issue.

Professor White notes that it could take ten to fifteen years to work though the mortgage crisis using the current voluntary methods. It could even take longer, especially if the holding pattern of voluntary modification only leads to another default, starting the cycle of default and foreclosure all over again. Homes remain unsold. The economy never recovers.

However bankruptcy cuts through many of these issues. The plan is confirmed or not in a matter of months. The plan lasts from 36-60 months. The modification is not voluntary so the lender cannot be sued for overstepping its discretion. Second liens can be valued and allowed or stripped. Since the bankruptcy court is open to everyone, it provides a fair, expeditious, tested and familiar structure for families to save their homes.

Conclusion

The current voluntary programs are a failure. We continue to have difficulty, even in reaching some lenders to propose a timely modification. For whatever reason lenders are still not capable of consistently voluntarily modifying loans in such a way, that would grant to borrowers the repayment terms necessary to save their homes. Typically that would involve an interest rate reduction, a curing of the arrearage, a reduction in the principal balance, whether combined with an equity sharing arrangement or not, and moving the loan from a variable rate to a fixed rate. H.R. 200 and H.R. 225 both cut through the voluntary modification process and provide an effective mechanism to modify mortgage loans in Chapter 13 bankruptcy.