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**Regulatory Comments**

# NCRC Comment to the FDIC

# Regarding the Proposed Legacy Loans Program

**April 9, 2009**

**National Community Reinvestment Coalition**

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April 9, 2009

Mr. Robert E. Feldman
Executive Secretary
Attention: Comments – Legacy Loans Program
Federal Deposit Insurance Corporation
550 17th Street, Northwest
Washington, DC 20429

Dear Mr. Feldman:

The National Community Reinvestment Coalition (NCRC) maintains that the Treasury Department and the FDIC should combine the Obama Administration's Home Affordable Modifications Program (HAMP) and the Legacy Loans Program (LLP). HAMP is a voluntary program that provides monetary incentives to lenders, servicers, and borrowers to encourage financial institutions to modify mortgages and make them affordable to borrowers experiencing difficulties paying their mortgages. LLP facilitates the sale of troubled assets (including mortgage loans) from banks to investors. The federal government would provide FDIC guarantees on loans that a private sector buyer would use to finance the purchase of troubled assets. The government would also share in the investment of the troubled assets. The government and the private-sector buyer would each have a 50 percent equity share in the troubled assets.

Since the government is providing a considerable amount of financing to move troubled assets off the books of banks, the government should require modification of the troubled assets as a quid pro quo. If the government does not require modification, the chances of subsequent modifications into sustainable mortgages decline significantly. The experience to-date suggests that modifications are easier and more effective when conducted by banks holding their loans in portfolios than when servicers manage loans for investors. It is unclear exactly what the institutional arrangement will be when loans under the LLP program are sold to investors. If the institutional arrangement resembles servicers managing loans for investors, modifications may be difficult to execute at all or to execute in a manner sustainable to borrowers.

The federal government should consider using HAMP and LLP funding to facilitate modifications as troubled loans are being sold to investors. Under HAMP, the federal government will provide up to $4,500 to servicers, $5,000 to borrowers, and $1,500 to lenders in order to facilitate medications. It would seem that the government could apply this funding of more than $10,000 to facilitate modifications when troubled loans are sold to investors in LLP. If more funds are needed, the government could reduce its 50 percent equity share of sold loans and use the diverted funding to subsidize loan modifications.

If HAMP and LLP do not achieve anticipated modification volumes, NCRC recommends that the federal government consider NCRC's Homeowners Emergency Loan Program (HELP Now) proposal (see attached). The HELP Now proposal has similarities to a combination of HAMP and LLP in that HELP Now incorporates various strategies to purchase distressed loans at steep discounts. A significant difference, however, between HELP Now and LLP is that HELP Now institutes mandatory purchases of troubled assets through the federal government's power of eminent domain. HELP Now's mandatory approach is stronger than the voluntary efforts in place for banks and other financial institutions to purchase troubled assets. A mandatory approach is necessary to stem the rising tide of foreclosures and begin the long-term process of economic recovery.

Since one of the major objectives of LLP is to help banks revive their lending activities, NCRC believes that the federal regulatory agencies must increase the frequency and rigor of their Community Reinvestment Act (CRA) exams. Frequent and vigorous CRA exams would ensure that banks involved in LLP lend in a safe and sound manner. Troubling evidence suggests, however, that CRA exams have become less frequent, especially for the largest banks. For example, the Office of the Comptroller of the Currency (OCC) conducted a CRA exam for Bank of America in 2006, a full five years after its 2001 exam. Wells Fargo, NA had a CRA exam in 2004, a full six years after its 1998 exam. Therefore, NCRC recommends that CRA exams occur every two years in order to promote responsible lending. NCRC also recommends that the federal regulatory agencies hire more CRA examiners if needed to strengthen the oversight of banks and to conduct exams in a timely manner.

While this request for comments did not explicitly seek recommendations on the Legacy Securities Program (LSP), NCRC recommends that both LSP and LLP be combined with HAMP to facilitate broad-based modifications of distressed loans. In addition, NCRC believes that the non-bank sellers of legacy securities should be required and/or strongly encouraged to engage in CRA-related community development lending and investment activities. One of the main intentions of LSP is to provide institutions that sell legacy securities with increased capacity to encourage them to lend and invest again.

Encouraging CRA community development lending and investing in low- and moderate-income neighborhoods hardest hit by the foreclosure crisis is consistent with LSP's objectives of restarting credit and investment markets. Moreover, non-bank financial institutions should be encouraged and expected to engage in community development lending and investing at a level commensurate with banks holding similar assets. The federal banking regulatory agencies should be consulted to provide information on the ratios of community development lending and investment activities to the amount of bank assets so that target levels of community development financing can be developed for the non-bank financial institutions that participate in LSP.

A secondary market is emerging for small business loans and community development loans. LSP represents an excellent opportunity to further develop this secondary market by directing institutions that sell legacy securities to engage in community development investments, particularly the purchases of small business loans and community development loans.

Finally, NCRC believes that tying LLP and LSP more closely with HAMP and CRA will maximize the intentions of LLP and LSP to end the current foreclosure crisis, restart the lending and investment markets, and revitalize low- and moderate-income neighborhoods and communities. LLP and LSP transactions are an optimal time to execute loan modifications, particularly since all the various streams of HAMP and LLP/LSP funding can come together for maximum effectiveness. If the government does not conduct meaningful loan modifications as part of the LLP or LSP transaction, loan modifications are likely to be much more difficult to achieve after those transactions.

Thank you for providing us the opportunity to comment. If you have any questions, please contact me at 202-628-8866 or Josh Silver, Vice President of Research and Policy, at 202-464-2708.

Sincerely,

John Taylor
President and CEO

NCRC is an association of more than 600 community-based organizations that promotes access to basic banking services, including credit and savings, to create and sustain affordable housing, job development, and vibrant communities for America's working families.

NATIONAL COMMUNITY REINVESTMENT COALITION NCRC

## Homeowners Emergency Loan Program (HELP Now)

Two years into the financial crisis, there is no substantial proposal to address mounting foreclosures that have dragged the economy into a potentially deep and protracted recession. The National Community Reinvestment Coalition (NCRC), a non-profit consumer group of more than 600 members across the country, proposes a market-driven solution to the mortgage and foreclosure crisis that puts homeowners first, stabilizes neighborhoods, and rebuilds communities, while posing minimal risk to taxpayer funds.

NCRC first proposed the Homeowners Emergency Loan Program (HELP Now) in January 2008 to stem rising foreclosures and their devastating contagion effects. A year later, with millions of foreclosures destabilizing the national economy, driving unemployment, and undermining consumer confidence, NCRC deems it critical to address this crisis with broad-scale programs that meaningfully modify high-cost loans to encourage long-term borrower affordability.

- With the HELP Now proposal, loans are purchased from investors by the government at discounted rates; loans are then resold to the private market and then modified. The HELP Now program allows the private market to remedy the problem it created in the first place.

- HELP Now targets mortgage loans to homeowners who are employed and have not experienced a reduction in income. In other words, this program helps borrowers who are otherwise able to repay their mortgages at reasonable rates, but are unable to repay mortgages that they found themselves trapped in that were high-cost and likely to go into default from the onset.

- HELP Now creates a three-year program and not a new agency. Broad-based loan modification can be accomplished through two separate approaches:

    - Reverse Auction: The Treasury Department would purchase loans in reverse auction that would start at approximately 80% of fair market value, falling to as low as 50%, and /or loans held in securitized pools at a steep discount (equal to roughly the current market value).

    - Compel the Sale of Troubled Assets: 1) Employ the power of eminent domain to purchase whole loans or loans held in securitized pools when it serves a public purpose; 2) use Real Estate Mortgage Investment Conduit tax rules that justify the creation of a government-sponsored whole loan purchase program; 3) utilize the Constitutional provisions in the “Commerce Clause” and the “Spending Clause” to alter and rewrite Mortgage Backed Securities and other secondary market structures to accomplish meaningful loan modifications; and 4) use Troubled Asset Relief Program (TARP) language that authorizes the government to purchase troubled assets. (It is recommended that the Treasury Department remove the TARP provision that dictates that a servicer is not permitted to cancel a contract entered into with an investor.)

Discounting the purchase of these loans would strike a balance between assisting homeowners and ensuring that lenders, servicers, and securitizers are not rewarded for financing and servicing unfair, deceptive, and reckless price-inflated loans. The government's purchase of these assets through eminent domain laws will avoid any threat of litigation against servicers by investors—a commonly cited reason that loans are not being modified at a greater pace. The discounted loan price should be sufficient to writedown the loan balance of millions of loans at the least direct cost to the federal government so that they can be permanently refinanced or modified to ensure their long-term sustainability.

  - For example, a mortgage loan may have an outstanding balance of $200,000, but after paying fair market value, the loan would be reduced to $140,000 (assuming a 30% discount). That discount of $60,000 would be applied to reduce the loan interest rate and (where necessary) principal balance to create a sustainable affordable loan product <u>without any government investment or guarantee</u>. The government would be immediately reimbursed for the entire amount of its purchase and have no other obligation to the investor, lender, or borrower. Modified loans would immediately be resold to Fannie Mae or Freddie Mac.

- In having the private sector refinance or modify these loans, the government would issue mandatory underwriting criteria that ensured such loans were fair and based on the borrower's ability to repay.

- If the discount procured is insufficient to allow the private banks to refinance, the Treasury Department can make a furthur discount to modify or refinance through the US Department of Housing and Urban Development or the Federal Housing Administration's Hope for Homeowners program. The government is then able to recapture a share of its equity investment when the property is sold or refinanced through a soft second and/or lien placed against the property.

- HELP Now is different from other plans offered in several ways:

  - Solving the problem through widespread loan modifications avoids the technical challenges associated with refinancing all loans.

  - HELP Now does not require refinancing with the Federal Housing Administration and does not put the government "on the hook" for 100% of the risk. No new massive government entity will need to be created, but rather HELP Now utilizes the private sector to modify and secure these loans. The government will remain responsible for only a small portion of these loans.

  - Under HELP Now the government could purchase loans in limited amounts (e.g., $50 billion per taking), and once refinanced by the private sector, use these funds to purchase additional loans. The government's investment would be a revolving fund, in which the government is made whole through the private sector. This minimizes the government's risk exposure at any period in time.

  - The government leverages its TARP investments by requiring participation in the HELP Now program and is nearly paid out in full immediately upon the refinancing or modification of the loan by the private sector.

  - This program requires a soft second for the remaining difference between the discounted purchase price and the current market value of the loan. This is recaptured upon sale of the property, ensuring that the government is not saddled with the bill.

  - Multiple strategies can be employed to compel participation, including eminent domain law and others.