

Boston College Law School

Digital Commons @ Boston College Law School

Boston College Law School Faculty Papers

1-10-2015

What Loss Mitigation Taught Us About Housing Finance Reform

Patricia A. McCoy

Boston College Law School, patricia.mccoy@bc.edu

Follow this and additional works at: <https://lawdigitalcommons.bc.edu/lfsp>



Part of the [Administrative Law Commons](#), [Banking and Finance Law Commons](#), and the [Housing Law Commons](#)

Recommended Citation

Patricia A. McCoy. "What Loss Mitigation Taught Us About Housing Finance Reform." *Housing Perspectives* (2015).

This Article is brought to you for free and open access by Digital Commons @ Boston College Law School. It has been accepted for inclusion in Boston College Law School Faculty Papers by an authorized administrator of Digital Commons @ Boston College Law School. For more information, please contact abraham.bauer@bc.edu.



Housing Perspectives

Research, trends, and perspective from The Harvard Joint Center for Housing Studies

Tuesday, January 13, 2015

What Loss Mitigation Taught Us About Housing Finance Reform



by Patricia McCoy
Guest Blogger

From time to time, Housing Perspectives features posts by guest bloggers. Today's post was written by Patricia McCoy, Liberty Mutual Insurance Professor, Boston College Law School, and former Assistant Director for Mortgage Markets, Consumer Financial Protection Bureau.

Since 2007, the federal government and servicers have groped toward striking the right balance between cost-effective loss mitigation and unavoidable foreclosures for homeowners with delinquent home mortgages. Among other things, this painful experience resulted in a cornucopia of data about the right way and wrong way to do loss mitigation. Nevertheless, none of the leading housing finance reform proposals has incorporated these lessons. Take, for example, the Johnson-Crapo bill, which was the leading reform contender and made it to the Senate floor. That bill would vaguely require servicers to establish "loss mitigation options that seek to enhance value" but says nothing about the best way to do so. That oversight is unfortunate because it sets us up to repeat the mistakes of the past.

First, some history. Eight years ago, the federal government became focused on foreclosure prevention as mortgage delinquency rates began to spike. The George W. Bush Administration sought to achieve that goal through moral suasion and voluntary compliance by servicers under the aegis of **HOPE NOW**. Later, the Obama Administration turned up the heat by offering a carrot and a stick: a carrot consisting of the **HAMP Program**, which paid servicers to grant loan modifications when doing so would increase recovery, and a stick through rulemakings and enforcement. One of the results was a rich trove of data on what makes loss mitigation work and why.

So what did we learn? I address this question in some detail in a chapter in the Joint Center's latest book, *Homeownership Built to Last*, but here are a few quick takeaways:

1. Standardized decision tree, or "waterfall," such as that employed by HAMP to lower monthly payments, is key to minimizing default rates (by cutting the interest rate or, if necessary, reducing principal).
2. Foreclosure prevention is more successful the sooner it is granted after a homeowner's first delinquency – ideally within two to three months.
3. The federal government should offer meaningful relief to people who are temporarily unemployed and need help making their mortgage payments until they get back on their feet.

These three techniques are a win-win for distressed homeowners and for investors by avoiding needless foreclosures while maximizing investor recovery.

But there's one final lesson that is directly relevant to housing finance reform. We can't implement lessons one through three unless we remove servicer barriers to effective foreclosure prevention. In 2007 and 2008, the private-label mortgage-backed securities market collapsed and that market remains moribund today. In the aftermath, servicers rushed to foreclosure in too many cases, saying that pooling and servicing agreements with investors (PSAs) tied their hands. Investors disputed those claims, complaining that the PSAs did not in fact bind servicers' hands and that foreclosure prevention would have enhanced recovery in many of those cases.

After that sour experience, investors will not be eager to rush back to the private-label market unless loss mitigation rules give them stronger protections. It is important, going forward, that

About

 **Harvard Joint Center for Housing Studies**

Drawing from the ongoing research and analysis of the Harvard Joint Center for Housing Studies, Housing Perspectives provides timely insight into current trends and key issues in housing. We dig deeper into the housing headlines to discuss critical issues and trends in housing, community development, global urbanism, and sustainability. Posts are written by staff of the Joint Center, drawing from their wide-ranging knowledge and experience studying housing. We hope you will follow Housing Perspectives, and we welcome your comments.

[View my complete profile](#)

Receive our newest blog posts in your inbox.

Email Address * indicates required

 [Follow by RSS](#)

Blog Archive

- ▼ 2015 (9)
 - ▶ February (4)
 - ▼ January (5)
 - [New Report: U.S. Home Improvement Industry Outpace...](#)
 - [What Effect Will Lower FHA Mortgage Insurance Prem...](#)
 - [Growth Slowing in Home Remodeling in 2015 \(+ New R...](#)
 - [What Loss Mitigation Taught Us About Housing Finan...](#)
 - [11+ Million Undocumented Immigrants in the U.S. Co...](#)
- ▶ 2014 (44)
- ▶ 2013 (45)
- ▶ 2012 (17)

Search This Blog

PSAs in future deals give servicers no excuse to deny loan modifications that will increase investor recovery vis-à-vis foreclosure. Since PSAs are privately negotiated, the only real way to assure that is to prescribe standard loss mitigation protocols and require PSAs to follow those protocols in any housing finance reform law that Congress enacts. The protocols should require servicers to evaluate loan modification requests by distressed borrowers using a standardized waterfall that is designed to reduce monthly payments to an affordable target level. Under that waterfall, servicers should attempt to attain the target payment level first through interest rate reductions and then, if need be, through principal reductions. The statutory protocols should also set time limits for loan modification decisions to help encourage early intervention. With these protocols in place, we can help avoid the experience in recent years where useless foreclosures pushed down home prices and delayed the economic recovery.

Posted by [Harvard Joint Center for Housing Studies](#) at 9:28 AM



Labels: [foreclosure](#), [GSEs](#), [HAMP](#), [homeownership](#), [mortgage finance](#), [policy](#)

No comments:

Post a Comment

Comment as:

Notify me

[Newer Post](#)

[Home](#)

[Older Post](#)

Subscribe to: [Post Comments \(Atom\)](#)

Labels

[accessible](#) [housing](#) [design](#) [ACS](#)
[affordability](#) [aging in place](#) [AHS](#) [baby boom](#) [bacteria](#) [boomerang](#) [Boston](#) [bubble](#) [C-30](#)
[census](#) [children](#) [cities](#) [climate change](#) [community development](#) [construction](#) [CPS](#)
[debt](#) [demographics](#) [disabled](#)
[distressed properties](#) [DIY](#) [Dunlop](#) [echo boom](#) [education](#) [elderly](#) [employment](#) [energy efficiency](#) [environment](#) [equity](#) [fannie mae](#) [FHA](#) [foreclosure](#) [freddie mac](#) [gateway cities](#) [GDP](#) [geographic mobility](#) [GIS](#) [GSEs](#) [HAMP](#) [headship rate](#) [healthy housing](#) [Hispanic](#) [homebuilding](#) [homeowner](#) [counseling](#) [homeownership](#)
[household growth](#) [housing assistance](#) [housing demand](#) [HUD](#) [hvs](#) [immigration](#) [inadequate housing](#) [indoor air quality](#) [interest rates](#) [international investors](#) [LIHTC](#) [LIRA](#) [low income](#) [LTV](#) [marriage](#) [metros](#) [microbes](#) [microbiomes](#) [millennials](#) [minority](#) [mortgage finance](#) [mortgage insurance](#) [mortgage interest deduction](#) [multifamily](#) [New Residential Construction](#) [Surveys](#) [nonprofit](#) [overcount](#) [pathogens](#) [policy](#) [population growth](#) [price-to-income ratio](#) [public housing](#) [recession](#) [recovery](#) [remodeling](#) [rent](#) [rental](#) [reverse mortgage](#) [RFI](#) [SCF](#) [seniors](#) [shared equity](#) [slums](#) [sprawl](#) [state of the nation's housing](#) [student loan](#) [substandard housing](#) [sustainability](#) [sustainable urban development](#) [undercount](#) [urban growth](#) [urban planning](#) [urban poverty](#) [voucher](#) [workforce housing](#)

Tweets by [@Harvard_JCHS](#)

Blogs We Read

[Zillow Blog - Real Estate Market Stats, Celebrity Real Estate, and Zillow News](#)

1 hour ago

[Latest Posts | The Atlantic Cities](#)

1 hour ago

[NHC Open House Blog](#)

3 hours ago

[Urban Institute MetroTrends](#)

3 hours ago

[Redfin Real Estate Blog](#)

5 hours ago

[NHI Rooflines](#)

1 day ago

[S&P HousingViews](#)

1 day ago

[Eye on Housing](#)

3 weeks ago

[NeighborWorks News](#)

4 months ago

[Economic Commentary \(Federal Reserve Bank of Cleveland\)](#)

[Lincoln Institute of Land Policy](#)

[The Stoop \(Furman Center for Real Estate and Urban Policy\)](#)

[Real Estate Research \(Federal Reserve Bank of Atlanta\)](#)

[The Demand Institute](#)

The opinions expressed in Housing Perspectives do not necessarily represent the views of Harvard University, the Policy Advisory Board of the Joint Center for Housing Studies, or any other sponsoring agency. The Joint Center welcomes comments to our Housing Perspectives blog. Any opinions expressed in posted comments, or in guest blogs, are those of the authors and not those of the Joint Center for Housing Studies of Harvard University or of any of the persons or organizations providing support to the Joint Center for Housing Studies. Comments are generally not edited but are reviewed for appropriateness, and normally post within a day. The Joint Center reserves the right to delete or decline to post comments that are off-topic, illegal, or otherwise objectionable or injurious. Commenters are fully responsible for the content they submit, and indemnify Harvard University and the Joint Center for Housing Studies against any losses, damages, or costs resulting from any claim relating to material they have posted. We require commenters to sign their comments with their real names. All comments and postings are the property of the Joint Center and may be used by the Joint Center at its discretion.

Simple template. Powered by [Blogger](#).