Congressional Oversight Panel Examines "Robo-Signed" Foreclosures and Other Mortgage Irregularities

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For Immediate Release

WASHINGTON, D.C. - The Congressional Oversight Panel today released its November oversight report, "Examining the Consequences of Mortgage Irregularities for Financial Stability and Foreclosure Mitigation." The Panel reviewed allegations that companies servicing $6.4 trillion in American mortgages may in some cases have bypassed legally required steps to foreclose on a home. The implications of these irregularities remain unclear, but it is possible that "robo-signing" may have concealed deeper problems in the mortgage market that could potentially threaten financial stability and undermine foreclosure prevention efforts.

In the best-case scenario, concerns about mortgage documentation irregularities may prove overblown. In this view, which has been embraced by the financial industry, a handful of employees failed to follow procedures in signing foreclosure-related affidavits, but the facts underlying the affidavits are demonstrably accurate. Foreclosures could proceed as soon as the invalid affidavits are replaced with properly executed paperwork.

The worst-case scenario is considerably grimmer. In this view, which has been articulated by academics and homeowner advocates, the "robo-signing" of affidavits served to cover up the fact that loan servicers cannot demonstrate the facts required to conduct a lawful foreclosure. The risk stems from the possibility that the rapid growth of mortgage securitization in recent years may have outpaced the ability of the legal and financial system to track mortgage loan ownership. In essence, banks may be unable to prove that they own the mortgage loans they claim to own.

If documentation problems prove to be pervasive and throw into doubt the ownership of pooled mortgages, the consequences could be severe. Borrowers may be unable to determine whether they are sending their monthly payments to the right people. Judges may block any effort to foreclose, even in cases where borrowers have failed to make regular payments. Multiple banks may attempt to foreclose upon the same property. Borrowers who have already suffered foreclosure may seek to regain title to their homes and force any new owners to move out. Would-be buyers and sellers could find themselves in limbo, unable to know with any certainty whether they can safely buy or sell a home.

Further wide-scale disruptions in the housing market, if they arose, could cause significant harm to financial institutions. For example, if a Wall Street bank were to discover that, due to shoddily executed paperwork, it still owns millions of defaulted mortgages that it thought it sold off years ago, it could face billions of dollars in unexpected losses. To put in perspective the potential problem, the mortgage-backed securities market totals approximately $7.6 trillion, so irregularities that affect even a small percentage of this market could have dramatic effects on bank balance sheets -

potentially posing risks to the very financial stability that the Troubled Asset Relief Program was designed to protect. The Panel urges Treasury and bank regulators to undertake new "stress tests" to gauge the ability of major financial institutions to cope with a potential documentation-related crisis.

Documentation irregularities could also disrupt Treasury's foreclosure prevention efforts. Some servicers dealing with Treasury may not be able to document a legal right to initiate foreclosures, which may call into question their ability to grant modifications or to demand payments from homeowners. The servicers' use of "robo-signing" may also have affected determinations about individual loans; servicers may have been more willing to foreclose if they were not bearing the full costs of a properly executed foreclosure. The Panel recommends that Treasury immediately undertake more active efforts to monitor the impact of documentation irregularities on its foreclosure mitigation programs.

Documentation irregularities could compound other threats to the mortgage market. In particular, allegations have surfaced that banks may have misrepresented the quality of many loans sold for securitization. Banks found to have provided misrepresentations could be required to repurchase any affected mortgages. Because millions of these mortgages are in default or foreclosure, the result could be extensive capital losses if such repurchase risk is not adequately reserved.

The Panel emphasizes that mortgage lenders and securitization servicers should not undertake to foreclose on any homeowner unless they are able to do so in full compliance with applicable laws and their contractual agreements with the homeowner.

The full report is available at cop.senate.gov.

The Congressional Oversight Panel was created to oversee the expenditure of the Troubled Asset Relief Program (TARP) funds authorized by Congress in the Emergency Economic Stabilization Act of 2008 (EESA) and to provide recommendations on regulatory reform. The Panel members are Senator Ted Kaufman (D-DE); J. Mark McWatters; Richard H. Neiman, Superintendent of Banks for the State of New York; Damon Silvers, Policy Director and Special Counsel for the AFL-CIO;and Kenneth Troske, William B. Sturgill Professor of Economics at the University of Kentucky.