

July 2009

TROUBLED ASSET RELIEF PROGRAM

Treasury Actions Needed to Make the Home Affordable Modification Program More Transparent and Accountable





Highlights of [GAO-09-837](#), a report to congressional committees

Why GAO Did This Study

GAO's sixth report on the Troubled Asset Relief Program (TARP) focuses on the Department of the Treasury's (Treasury) efforts to establish its Home Affordable Modification Program (HAMP). This 60-day report examines (1) the design of HAMP's program features with respect to maximizing assistance to struggling homeowners, (2) the analytical basis for Treasury's estimate of the number of loans that are likely to be successfully modified using TARP funds under HAMP, and (3) the status of Treasury's efforts to implement operational procedures and internal controls for HAMP. For this work, GAO reviewed documentation from Treasury and its financial agents and met with officials from Treasury, its financial agents, and other organizations.

What GAO Recommends

GAO recommends that the Secretary of the Treasury; (1) consider methods for monitoring compliance with and the effectiveness of its counseling requirement; (2) reevaluate the basis and design for HPDP; (3) regularly update assumptions and projections underlying the estimated number of borrowers likely to be helped by HAMP; (4) staff vacant positions within HPO, and evaluate its staffing levels and competencies; (5) finalize a comprehensive system of internal control over HAMP; and (6) systematically assess servicer's capacity to meet HAMP's requirements during program admission. Treasury stated it would consider GAO's recommendations as it moved forward.

View [GAO-09-837](#) or [key components](#). For more information, contact Mathew J. Scire at (202) 512-8678 or sciremj@gao.gov.

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What GAO Found

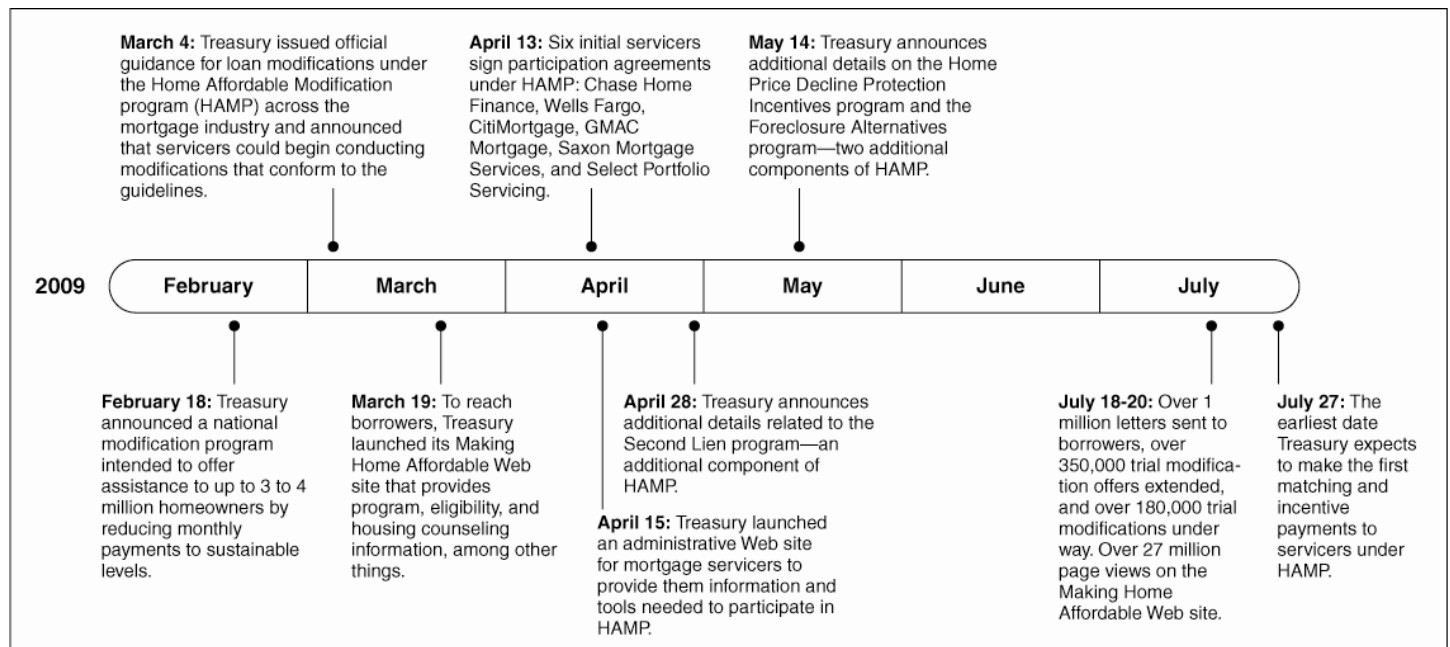
Under HAMP, Treasury will use up to \$50 billion in TARP funds to (1) modify the first-lien mortgages of homeowners in danger of foreclosure, (2) encourage the modification of mortgages in areas experiencing serious declines in property values, (3) reduce or pay off second-lien mortgages for homeowners with loans modified under HAMP, (4) arrange deeds-in-lieu or short sales as alternatives to foreclosure; and (5) provide incentive payments to encourage refinancing under the HOPE for Homeowners program. The first-lien mortgage modification effort is the largest and most developed part of HAMP, and Treasury and its financial agents are establishing the operational infrastructure for this effort. However, one of the requirements under the first-lien program—that borrowers with high levels of household debt agree to obtain counseling—may not fully meet Treasury's goals. Specifically, Treasury does not plan to systematically monitor whether borrowers who are told they must obtain counseling actually receive it, in part, because it does not wish to deny a loan modification to borrowers that have demonstrated they are able to make modified payments. Also Treasury does not plan to assess the effectiveness of its counseling requirement in limiting redefaults. The other four HAMP subprograms had been announced but were not fully designed or operational. Treasury announced the \$10 billion Home Price Decline Protection (HPDP) program, which is intended to encourage investors to modify mortgages in areas experiencing steep declines in home prices. But, Treasury officials told us that they had not yet developed estimates of the number of modifications that would result from the HPDP, and said that in some cases, the HPDP payments would go to some loan modifications that would likely have been made without this incentive. Because none of the expenditures under HPDP would be recouped, it is crucial that Treasury ensure that funds are spent only when needed to encourage modifications that would not be made without this incentive.

Treasury's estimate of the number of borrowers who would likely be helped under its HAMP loan modification program reflects uncertainty created by data gaps and the need to make numerous assumptions, and this projection may be overstated. In addition, Treasury has not specified its plans for systematically updating key assumptions and calculations. Treasury announced that up to 3 to 4 million borrowers who were at risk of default and foreclosure could be offered a loan modification under HAMP. But Treasury's projection of a participation rate of 65 percent of the target group—borrowers who were at least 60 days delinquent in their loans or in imminent danger of default—which is based roughly on a 90 percent servicer representation rate and a 70 percent borrower response rate, may be high. The loan modification program most similar to HAMP—FDIC's IndyMac Bank program—has a peak borrower response rate of only 50 percent. Additionally, servicer participation in HAMP has not yet reached the 90 percent coverage rate projected by Treasury, and borrowers cannot participate unless their servicers do. Also, not all homeowners offered a loan modification will remain current on their modified mortgages—further reducing the number of homeowners that may

avoid foreclosure through the HAMP program. Lastly, Treasury did not provide detailed information and documentation essential to adequately support its assumptions. The lack of adequate documentation and specification of the assumptions makes it difficult to assess the reliability of Treasury's estimates and, going forward, may hinder efforts to evaluate how well the program is meeting its objectives.

Treasury has taken a number of important steps toward implementing operational procedures and internal controls for HAMP but has not finalized all of the associated processes and is not systematically evaluating servicers' capacity during program admission. Treasury officials have developed and continue to refine key operational procedures and internal controls, including establishing an organizational structure for overseeing HAMP, delegating implementation authorities and responsibilities to its financial agents, and drafting work flows for processes such as those associated with the payment of incentives. As of July 20, 2009, about 180,000 borrowers have entered into trial modifications but HAMP incentive payments will not be made until July 27 at the earliest—pending successful completion of the 90-day trial periods (see timeline below of major HAMP events). While Treasury has delegated some administrative and oversight responsibilities to its financial agents, such as program administration and compliance responsibilities, it has retained authority for overall HAMP implementation, led by the Homeownership Preservation Office (HPO) with support from other Treasury offices. However, HPO continues to have a large number of unfilled positions. Treasury has also begun to develop performance measures for HAMP, but many of the specifics of these measures, such as how success will be defined, have yet to be determined. In addition, Treasury and its financial agents do not have systematic processes or controls in place to consistently evaluate the capacity of servicers to fulfill specific HAMP requirements during the program admittance process. Yet concerns have been raised by Treasury, the Congressional Oversight Panel, and federal banking regulators about servicers' capacity to fulfill program requirements and implement HAMP. Because servicers are not fully evaluated during the admittance process, Treasury is unable to adequately identify, assess, and address any potential risks that may prevent them from fulfilling program requirements. But, unlike other TARP programs, such as the Capital Purchase Program, HAMP expenditures—which are projected to be up to \$50 billion—are not investments that will be partially or fully repaid, but rather, expenditures that, once made, will not be recouped. For this reason, a system of effective internal control over program expenditures is of critical importance.

Timeline of Major HAMP Events from February 18, 2009, through July 27, 2009



Source: Treasury, OFS.

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Abbreviations

COP	Congressional Oversight Panel
FDIC	Federal Deposit Insurance Corporation
FHA	Federal Housing Administration
FHFA	Federal Housing Finance Agency
FSOB	Financial Stability Oversight Board
GSE	government-sponsored enterprise
HAMP	Home Affordable Modification Program
HERA	Housing and Economic Recovery Act of 2008
HPDP	Home Price Decline Protection
HPO	Homeownership Preservation Office
HUD	Department of Housing and Urban Development
LTV	loan-to-value
MHA	Making Home Affordable
NPV	net present value
OCC	Office of the Comptroller of the Currency
OFS	Office of Financial Stability
OTS	Office of Thrift Supervision
SIGTARP	Office of the Special Inspector General for TARP
TARP	Troubled Asset Relief Program
VA	Department of Veterans Affairs

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United States Government Accountability Office
Washington, DC 20548

July 23, 2009

Congressional Committees

Dramatic increases in home mortgage defaults and foreclosures have imposed significant costs on borrowers, lenders, mortgage investors and neighborhoods; and have been a key contributor to the current financial crisis. On October 3, 2008, the President signed into law the Emergency Economic Stabilization Act (the act), which authorized the Department of the Treasury (Treasury) to establish the \$700 billion Troubled Asset Relief Program (TARP).¹ Treasury's initial focus in implementing TARP was to attempt to stabilize the financial markets and increase lending to businesses and consumers. However, the authorities granted to Treasury under the act also are to be used to, among other things, preserve homeownership and protect home values—two of the act's stated purposes—and to maximize assistance for homeowners with respect to foreclosure mitigation efforts. On February 18, 2009, Treasury announced a framework for a program that would, among other things, help at-risk homeowners avoid potential foreclosure by using up to \$50 billion of TARP funds to reduce their monthly mortgage payments.

Under the Home Affordable Modification Program (HAMP), Treasury's Office of Financial Stability (OFS) will share the cost of reducing monthly payments on first-lien mortgages with mortgage holders/investors and provide financial incentives to servicers, borrowers, and mortgage holders/investors for loans modified under the program. HAMP also includes other subprograms, such as one that would provide incentives to modify or pay off second-lien loans of borrowers whose first mortgages were modified under HAMP. However, some observers have questioned the number of homeowners that HAMP, as it is currently structured, will help, and Treasury's own estimates do not resolve this issue. Additionally, we have noted in prior reports that developing a comprehensive system of internal controls for TARP has been an ongoing challenge, in part because

¹Pub. L. No. 110-343, 122 Stat. 3765 (2008), codified at 12 U.S.C. §§ 5201 et seq. The act originally authorized Treasury to purchase or guarantee up to \$700 billion in troubled assets. The Helping Families Save Their Homes Act of 2009, Pub. L. No. 111-22, Div. A, 123 Stat. 1632 (2009), amended the act to reduce the maximum allowable amount of outstanding troubled assets under the act by almost \$1.3 billion, from \$700 billion to \$698.741 billion.

of the rapid evolution of TARP and its activities, which includes HAMP.² As a result, Treasury runs the risk of implementing a homeownership preservation program that does not yet have proper controls to protect taxpayers' interests and ensure that HAMP objectives are met.

The act requires that GAO report at least every 60 days on the activities and performance of TARP.³ This 60-day report (1) reviews the design of HAMP's program features with respect to maximizing assistance to struggling homeowners, (2) examines the analytical basis for Treasury's estimate of the number of loans that are likely to be successfully modified using TARP funds under HAMP, and (3) evaluates Treasury's progress in implementing operational procedures and internal controls for HAMP.

Scope and Methodology

To review the design of HAMP's first-lien modification features with respect to maximizing assistance to struggling homeowners, we reviewed the act and program guidance provided by Treasury on the HAMP Web site and interviewed officials at Treasury and Fannie Mae. To describe the steps Treasury has taken to implement the program and to discuss HAMP features, we reviewed publicly available documents—including official program guidelines—and discussed these with Treasury officials. Because Treasury told us that features of the Federal Deposit Insurance Corporation's (FDIC) loan modification program at IndyMac Federal Bank formed the basis for some of the HAMP features, we reviewed documents provided by FDIC and discussed these with FDIC officials. We also interviewed NeighborWorks officials to understand how its housing counseling network has been providing counseling to HAMP borrowers with high total household debt and its plans to track these borrowers. To evaluate the initial framework of the Home Price Decline Protection (HPDP) subprogram, we reviewed Treasury documents describing HPDP and its methods for determining incentive payments and interviewed

²See GAO, *Troubled Asset Relief Program: Additional Actions Needed to Better Ensure Integrity, Accountability, and Transparency*, [GAO-09-161](#) (Washington, D.C.: Dec. 2, 2008); *Troubled Asset Relief Program: Status of Efforts to Address Transparency and Accountability Issues*, [GAO-09-296](#) (Washington, D.C.: Jan. 30, 2009).

³[GAO-09-161](#); [GAO-09-296](#); and GAO, *Troubled Asset Relief Program: March 2009 Status of Efforts to Address Transparency and Accountability Issues*, [GAO-09-504](#) (Washington, D.C.: Mar. 31, 2009); *Auto Industry: Summary of Government Efforts and Automakers' Restructuring to Date*, [GAO-09-553](#) (Washington, D.C.: Apr. 23, 2009); and *Troubled Asset Relief Program: June 2009 Status of Efforts to Address Transparency and Accountability Issues*, [GAO-09-658](#) (Washington, D.C.: June 17, 2009) for our past 60-day reports.

officials responsible for its design. To describe HAMP's second-lien and foreclosure alternatives subprograms, we reviewed publicly available documents and discussed these proposed HAMP subprograms with Treasury officials. To examine how Treasury's HAMP helps homeowners with negative equity—a factor that could have a major impact on delinquencies and foreclosures, especially if home price declines continue—we reviewed Treasury documents that described guidelines for loans and borrowers eligible to participate in the program with particular attention to negative equity and interviewed the officials. We also observed a demonstration of the HAMP net present value (NPV) test model by Fannie Mae and Federal Housing Finance Agency (FHFA) staff, a model used by participating servicers to determine whether to modify a loan. We also reviewed literature on factors likely to affect mortgage delinquencies and home foreclosures and analyzed data on home foreclosures, negative equity, and unemployment rates across states in the United States from various sources, including the Mortgage Bankers Association's National Delinquency Survey data on home foreclosures, First America CoreLogic's data on negative equity, and the Department of Labor's Bureau of Labor Statistics data on unemployment rates.

To examine the analytical basis for Treasury's estimate of the number of loans that are likely to be successfully modified for at-risk borrowers using TARP funds, we reviewed documents from Treasury that described the loan characteristics of the mortgage market, Treasury's guidelines for loans and borrowers eligible to participate in the program, assumptions about participation by homeowners and servicers, and calculations of loans that were likely to be modified. These calculations used the NPV test model developed by an interagency working group made up of officials from FDIC, Fannie Mae, Freddie Mac, FHFA, and Treasury. We also reviewed documentation from other federal agencies that were involved in HAMP or that had experience with loan modifications—FDIC, Fannie Mae, Freddie Mac, and FHFA. We observed a demonstration by Fannie Mae, the program administrator, on the NPV test model using the HAMP Web site designed for participating servicers.⁴ We interviewed officials from Treasury, FHFA, Fannie Mae, and Freddie Mac who were responsible for the design of the loan modification program and the default and NPV models that support the design and operations of the program. We also consulted publications by private entities about loan characteristics of the

⁴Administrative Website for Servicers, Home Affordable Modification Program, <https://www.hmpadmin.com/portal/index.html>

mortgage market, including the Mortgage Bankers Association's *National Delinquency Survey* data on delinquencies and foreclosures and mortgage market analyses by Credit Suisse.

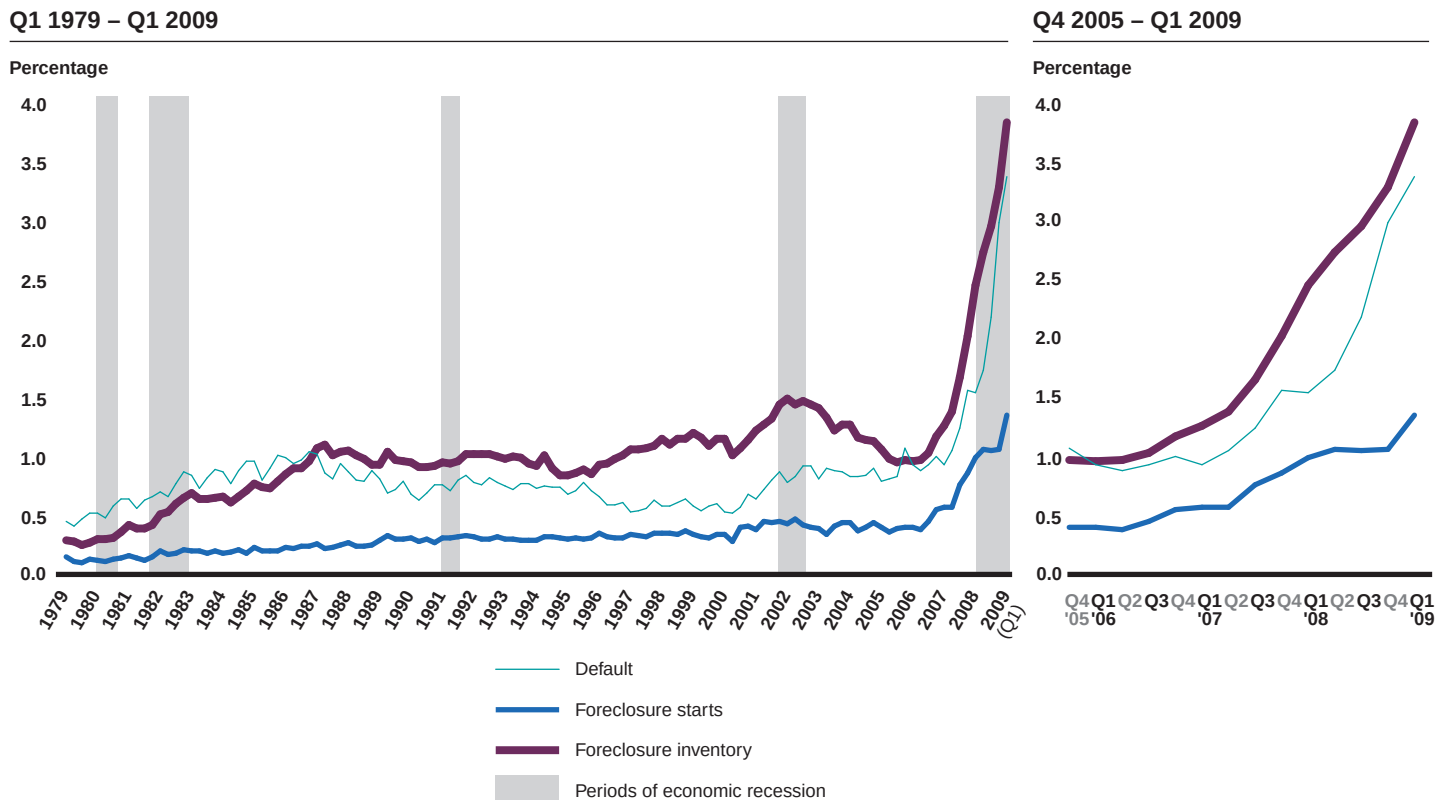
To evaluate the status of Treasury's efforts to implement operational procedures and internal controls for HAMP, we reviewed the financial agent agreements and the servicer participation agreements to understand their roles and responsibilities. In addition, we reviewed documents from these entities that outlined the organizational structure of HAMP and described internal controls, including organizational charts, flow charts depicting operational processes, narrative descriptions of risks and related controls, and other support documentation. To determine the extent to which Treasury and its financial agents had taken steps to insure that servicers were prepared for and had the capacity to conduct HAMP loan modifications at the time of program admittance, we reviewed a summary of the results of the readiness reviews conducted, discussed the readiness review process and the reviews done to date with Treasury officials, and reviewed HAMP servicer registration procedures. We also interviewed officials at Treasury, Fannie Mae, and Freddie Mac who were responsible for designing the operational procedures and internal controls for HAMP. To understand servicers' capacity to fulfill data collection and reporting requirements, we reviewed a summary of Treasury's meeting with 13 servicers and the results of a survey of servicers on these HAMP requirements. We also conducted interviews with participating servicers who entered into HAMP participation agreements to discuss program requirements. These servicers were Saxon Mortgage, Citi Mortgage, Home Loan Services, Green Tree Servicing, Carrington Mortgage Services, and Ocwen Servicing. We also reviewed the HAMP-related Web sites, press releases, and reports published by the regulatory agencies, in part to identify the data collection and reporting requirement guidelines that were in place.

We conducted this performance audit from May 2009 through July 2009 in San Francisco, California, Boston, Massachusetts, and Washington, D.C., in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on the audit objectives.

Background

As shown in figure 1, national default and foreclosure rates have increased dramatically between the third quarter of 2006 and the first quarter of 2009, rising to their highest level in 30 years. Loans in nonpayment status for 90 days or more are commonly considered to be in default, and for these loans, foreclosure can be a real possibility. Foreclosure is a legal process initiated by a mortgage lender against a homeowner after a certain number of payments have been missed. The foreclosure process has several possible outcomes, but generally means that the homeowner loses the property, typically because it is sold to repay the outstanding debt or repossessed by the lender. The foreclosure process is usually governed by state law and varies widely by state. Foreclosure processes generally fall into one of two categories—judicial foreclosures, which proceed through courts, and nonjudicial foreclosures, which do not involve court proceedings. The legal fees, foregone interest, property taxes, repayment of former homeowners' delinquent obligations, and selling expenses can make foreclosure extremely costly to lenders.

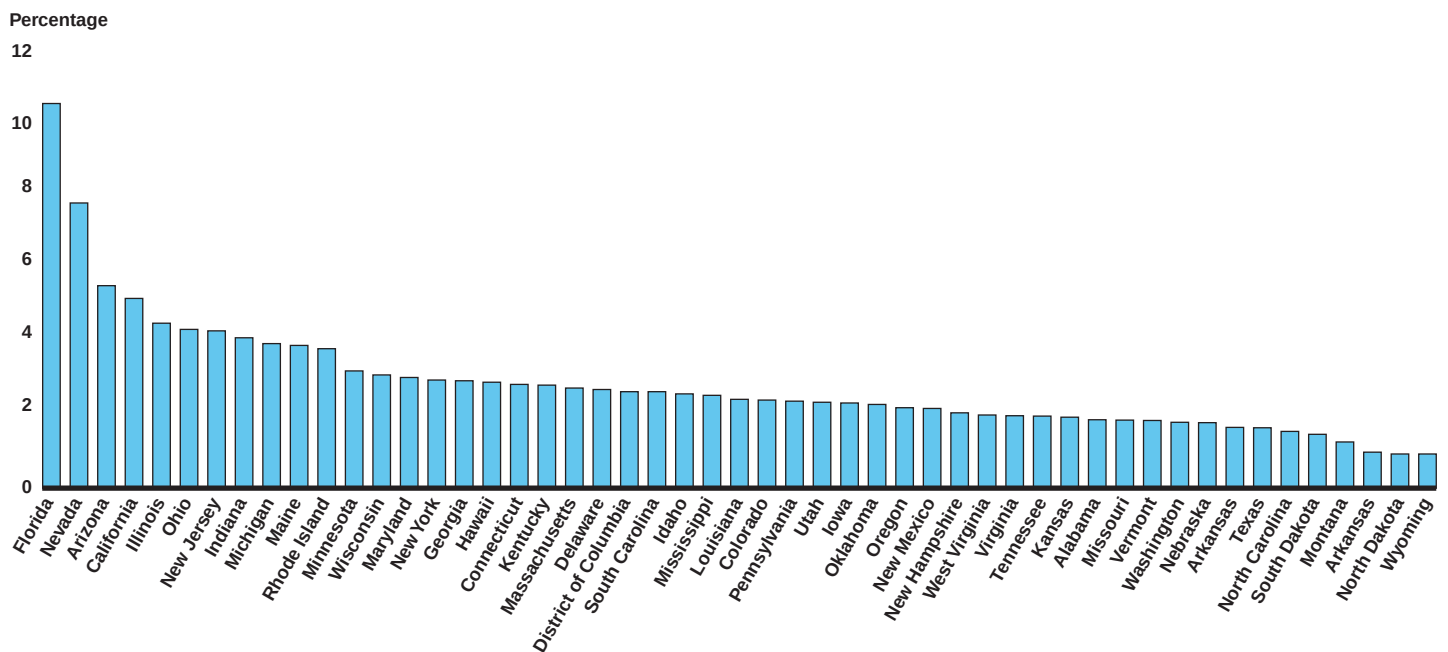
Figure 1: Default and Foreclosure Inventory Rates through the First Quarter of 2009



Source: GAO analysis of MBA data, National Bureau of Economic Research.

The increase in foreclosures has affected homeowners in all states, but some states have been affected more than others. As illustrated in figure 2, the Sunbelt states—Arizona, California, Florida, and Nevada—have particularly large inventories of homes in foreclosure.

Figure 2: Foreclosure Inventory Rates by State, as of March 31, 2009



Source: GAO analysis of Mortgage Bankers Association data.

Options to Avoid Foreclosure

Defaults and foreclosures have imposed significant costs on borrowers, lenders, and mortgage investors and have contributed to increased volatility in the U.S. and global financial markets. Options to avoid foreclosure include forbearance plans, short sales, deeds-in-lieu of foreclosure, and loan modifications. With forbearance plans and loan modifications, the borrower retains ownership of the property. With short sales and deeds-in-lieu, the borrower does not.

- With a forbearance plan, a lender agrees not to exercise the legal right of foreclosure if the borrower agrees to a payment plan that will resolve the borrower's deficiency for a set period of time. The plan may incorporate features such as reduced or suspended payments that allow the homeowner to recover from a serious event, such as illness, that has caused the homeowner to miss several loan payments. Usually, the lender

will require the borrower to make up the difference at a later time.

- Loan modification involves making temporary or permanent changes to the terms of the existing loan agreement. There are several ways to make these changes, including allowing the borrower to skip payments and adding the skipped payments to the amount of the loan (capitalizing arrearages), reducing the interest rate charged, extending the loan term, and reducing the total amount of the loan (forgiving principal).
- In a short sale, a house is sold through a real estate agent or other means rather than through foreclosure, even if the proceeds of the sale are less than what the owner still owes on the mortgage. Lenders may agree to accept the proceeds of a short sale and may waive any deficiency.
- Under a deed-in-lieu of foreclosure, the homeowner voluntarily conveys the interest in the home to the lender to satisfy a loan that is in default as an alternative to foreclosure proceedings. Lenders may opt to accept ownership of the property in place of the money owed on the mortgage and may waive any deficiency. Deeds-in-lieu will generally not be accepted by a mortgage holder if there are other liens on the property, as foreclosure may be necessary for the mortgage holder to gain clear title.

Role of the Secondary Market in Foreclosures

As we noted in December 2008, any program that aims to modify loans or present other alternatives to foreclosure faces challenges, particularly when the loans have been bundled into securities that are sold to investors.⁵ Most mortgages are bundled into residential mortgage-backed securities that are bought and sold by investors. These securities may be issued by government-sponsored enterprises (GSE), such as Fannie Mae and Freddie Mac, and private companies.⁶ Privately issued mortgage-backed securities, known as private-label securities, are typically backed by mortgage loans that do not conform to GSE purchase requirements because they are too large or do not meet GSE underwriting criteria. The originator/lender of a pool of securitized assets usually continues to

⁵GAO, *Troubled Asset Relief Program: Status of Efforts to Address Defaults and Foreclosures on Home Mortgages*, [GAO-09-231T](#) (Washington D.C.: Dec. 4, 2008).

⁶The GSEs—Fannie Mae and Freddie Mac—are private, federally chartered companies created by Congress to, among other things, provide liquidity to home mortgage markets by purchasing mortgage loans, thus enabling lenders to make additional loans. To be eligible for purchase by the GSEs, loans (and borrowers receiving the loans) must meet specified requirements. In September 2008, Fannie Mae and Freddie Mac were placed into federal government conservatorship.

service the securitized portfolio, including providing customer service and payment processing for borrowers and collection actions, in accordance with the pooling and servicing agreement. The decision to modify loans held in a mortgage-backed security typically resides with the servicer. However, one of the challenges that servicers face in modifying these loans is making transparent to investors the analysis supporting the value of modification over foreclosure. Additionally, the pooling and servicing agreements may place some restrictions on the servicer's ability to make large-scale modifications of the underlying mortgages without the investors' approval.⁷ In addition, many homeowners may have second liens on their homes that may be controlled by a different loan servicer, potentially complicating loan-modification efforts.

Treasury's Making Home Affordable Program

As we reported in December 2008, Treasury established an Office of Homeownership Preservation within OFS to address the issues of preserving homeownership and protecting home values.⁸ On February 18, 2009, Treasury announced the broad outline of a three-pronged effort to help homeowners avoid foreclosure and provided additional program descriptions on March 4, 2009, April 28, 2009, and May 14, 2009. First, one of the efforts—the Home Affordable Refinance Program—would provide a refinancing vehicle for homeowners that had (1) Fannie Mae and Freddie Mac held or guaranteed mortgages, (2) interest rates above the prevailing market rates, and (3) loan-to-value ratios between 80 and 105.⁹ Treasury estimated the number of borrowers in that current loan-to-value range for whom a refinanced mortgage would be potentially beneficial, based on the prevailing interest rates in February, at 4 to 5 million homeowners. No TARP funds would be used to refinance these loans. Second, Treasury would increase its funding commitment in preferred stock purchase agreements to Fannie Mae and Freddie Mac, authorized by the Housing and Economic Recovery Act (HERA) of 2008, from \$100 billion each to \$200 billion each to help support low mortgage rates by strengthening

⁷A pooling and servicing agreement is a contractual agreement for the pooling (i.e., collection) of a large amount of individual mortgage loans and the servicing of those loans by a servicer. A mortgage pooling and servicing agreement describes how pooled loans will be serviced and dictates how proceeds and losses will be distributed to mortgage holders/investors, and may set forth loss-mitigation options available to the servicer and the extent of the servicer's authority to use these options.

⁸GAO-09-161.

⁹On July 1, 2009, the Department of Housing and Urban Development (HUD) announced that the maximum loan-to-value rate had been increased to 125 percent.

confidence in the two GSEs. Treasury indicated that the increased funding commitment would be made under HERA and would not require the use of TARP funds. The third effort, HAMP, is designed to commit \$75 billion of GSE and TARP funds to offer relief through loan modification for up to 3 to 4 million borrowers struggling to pay their mortgages. According to Treasury officials, up to \$50 billion of TARP funds will be used primarily to encourage the modification of mortgages that financial institutions own and hold in their portfolios (whole loans) and mortgages held in private-label securitization trusts.¹⁰ Fannie Mae and Freddie Mac are expected to provide up to an additional \$25 billion to encourage servicers and borrowers to modify loans owned or guaranteed by the two GSEs. Treasury has taken various key steps to implement HAMP. Fannie Mae and Freddie Mac are in the process of implementing the HAMP guidelines for borrowers with loans that they own or guarantee.¹¹

As outlined in the March 4, 2009, program guidelines, HAMP's eligibility requirements stipulate that

- the property must be owner-occupied and the borrower's primary residence (the program excludes vacant and investor-owned properties);
- the property must be a single-family (1-4 unit) property with a maximum unpaid principal balance on the unmodified first-lien mortgage that is equal to or less than \$729,750 for a 1-unit property;¹²
- the loans must have been originated on or before January 1, 2009; and

¹⁰Loans held in private-label securitization trusts include loans not insured or guaranteed by Fannie Mae, Freddie Mac, HUD's Federal Housing Administration (FHA), the Department of Veterans Affairs (VA), and rural housing loans. The \$50 billion dollars will also be used for activities other than loan modification as discussed in later sections of this report.

¹¹Any funds provided by Treasury to the GSEs under the funding commitments, while not under TARP, will be funded, like TARP, through the issuance of public debt. Any losses incurred by the GSEs in relation to the additional \$25 billion they provide would be financed by Treasury (through issuance of public debt) through the funding commitments to the extent that the GSEs have liabilities that exceed assets.

¹²Unpaid principal balance limits (prior to modification) are \$729,750 for a 1-unit building; \$934,200 for a 2-unit building; \$1,129,250 for a 3-unit building; and \$1,403,400 for a 4-unit building.

-
- the first-lien mortgage payment must be more than 31 percent of the homeowner's gross monthly income.¹³

The cutoff date for borrowers to be accepted into the program is December 31, 2012.

Treasury has delegated significant responsibilities to its financial agents to administer the program, which we discuss in greater detail later in this report. Fannie Mae has signed an agreement with Treasury to act as the program administrator and record keeper for HAMP and is responsible for developing and administering program operations. Freddie Mac has signed an agreement with Treasury to act as the compliance agent for HAMP, and its responsibilities include conducting information technology testing, security reviews, and audits. Finally, Bank of New York-Mellon, in the role of custodian for TARP, is responsible for remitting mortgage payment reductions and program incentive payments to participating servicers.

As we described in our January 2009 report, the act created other oversight entities in addition to our oversight responsibilities, including the Congressional Oversight Panel (COP), the Office of the Special Inspector General for TARP (SIGTARP), and the Financial Stability Oversight Board (FSOB). We are coordinating our work with COP, SIGTARP, and FSOB and are meeting with officials from these entities to share information and effectively make use of our combined resources. COP issued a report in March 2009 that focused on foreclosures, and Treasury's efforts related to its Homeowner Affordability and Stability Plan.¹⁴ As of June 30, 2009, SIGTARP and FSOB had not issued any reports specifically looking at Treasury's planned use of TARP funds to preserve homeownership and protect property values, although this area may be the topic of future efforts.

¹³The mortgage, or front-end, debt-to-income ratio under the HAMP first-lien component is the percentage of a borrower's income comprising mortgage principal, interest, taxes, insurance, and association dues.

¹⁴Congressional Oversight Panel, *The Foreclosure Crisis: Working Towards a Solution* (Washington, D.C., Mar. 6, 2009).

Treasury Has Not Fully Developed All HAMP Subprograms, and the Initial Design of At Least Two Aspects of HAMP Limits Its Potential to Help Homeowners

In keeping with the act's purposes, Treasury has developed HAMP with the objective of preserving homeownership and protecting home values.¹⁵ According to Treasury, HAMP's primary goal is to reduce struggling borrowers' mortgage payments to an affordable level, thereby preventing unnecessary foreclosures and helping to stabilize home prices in neighborhoods hardest hit by foreclosures. HAMP was announced on February 18, 2009, and since that time, in addition to HAMP's main first-lien modification program, four major subprograms have been announced. Together these five programs use the \$50 billion Treasury targeted for HAMP to

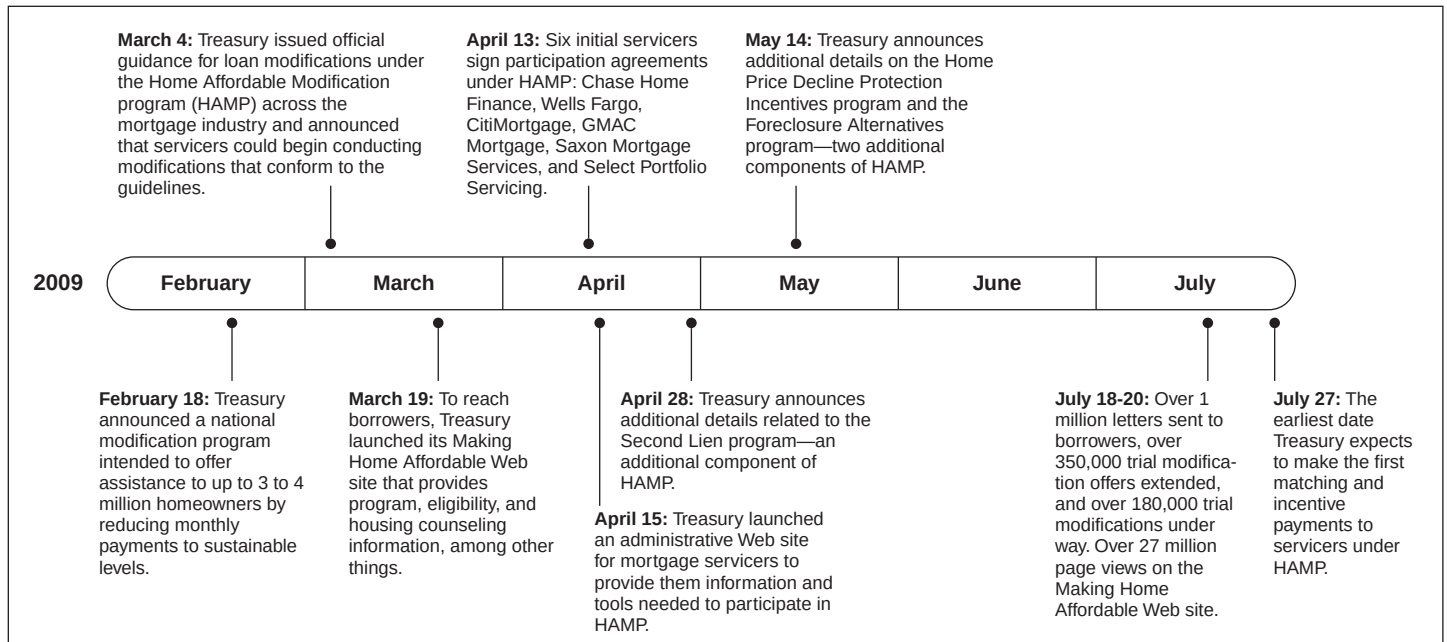
- modify first-lien mortgage loans;
- provide additional incentives to mortgage holders/investors to modify, rather than foreclose on, loans in areas where home price declines have been most severe;
- modify or eliminate second-lien loans (such as home equity lines of credit);
- offer alternatives to foreclosure for homeowners that do not qualify for a first-lien loan modification under HAMP; and
- provide incentive payments under the HOPE for Homeowners mortgage refinance program under the Federal Housing Administration (see fig. 3).¹⁶

¹⁵As noted above, the act authorized Treasury to purchase troubled assets from financial institutions. The act defines troubled assets to include both certain residential or commercial mortgages and securities based on such mortgages, and any other financial instrument that the Secretary determines needs to be purchased to promote financial market stability. Sections 101 and 3(9) of the Emergency Economic Stabilization Act. Under HAMP, Treasury, acting through its financial agent, enters into contracts with servicers that are financial institutions to purchase financial instruments under which the servicers commit to modify mortgages and to receive and make payments in accordance with specified criteria. To participate in HAMP, the servicer is required to enter into a Commitment to Purchase Financial Instrument and Servicer Participation Agreement with Fannie Mae, acting as Treasury's financial agent. We are planning to analyze these agreements in future work.

¹⁶The HOPE for Homeowners program was created by Congress under the Housing and Economic Recovery Act of 2008. The program, which was put in place in October 2008, is administered by the Federal Housing Administration under HUD and is designed to help those at risk of default and foreclosure refinance into more affordable, sustainable loans.

Treasury has made the most progress in implementing the first-lien modification program, and most of its features appear to be consistent with goals articulated by Congress and Treasury. However, one of the first-lien modification requirements—that borrowers with high levels of household debt obtain housing counseling in order to avoid possible redefault, which borrowers agree to when they enter into a trial loan modification—lacks an appropriate mechanism that would help ensure the requirement’s success. Specifically, Treasury does not plan to systematically track borrowers who are told they must obtain counseling to determine whether they do so or to analyze the effectiveness of the counseling. In addition, Treasury developed the HPDP subprogram with the purpose of increasing the number of modifications completed under HAMP. However, as it is currently described, some of the HPDP incentive payments appear to be unnecessary because Treasury may make payments for modifications that would have been made without this program. Treasury has targeted up to \$10 billion for the HPDP program.

Figure 3: Timeline of Major HAMP Events from February 18, 2009, through July 27, 2009



Source: Treasury, OFS.

Breakdown of Costs for HAMP Initiatives Has Yet to Be Determined

As shown in table 1, Treasury expects to use about \$32.5 billion in TARP funds to encourage modifications on first-lien mortgages of up to 2 to 2.6 million borrowers by sharing the costs of reducing borrowers' monthly payments with mortgage holders/investors, and by providing incentive payments for successful modifications to borrowers, servicers, and mortgage holders/investors.¹⁷ Also, using part of the \$50 billion in TARP funds, Treasury plans to provide up to \$10 billion in incentive payments to mortgage holders/investors for modifications in areas experiencing home price declines to partially offset potential losses should the modified loan redefault once prices have dropped. To reduce payments or pay off second lien loans of 1 to 1.5 million borrowers, Treasury has announced a Second-lien Modification Program using a yet to be determined amount of the TARP funds targeted for HAMP. For borrowers unable to qualify for a first-lien modification under HAMP, Treasury will provide TARP funding to encourage servicers to use alternatives to foreclosure, including short sales and deeds-in-lieu of foreclosure. Finally, Treasury announced that it would use part of the TARP funds allocated for HAMP to provide incentive payments to servicers that help refinance mortgages and lenders that originate refinanced mortgages under the HOPE for Homeowners program.

The number of borrowers Treasury expects to reach through the HPDP, foreclosure alternatives, and HOPE for Homeowners incentive payments subprograms has yet to be determined. In addition, funding levels for second-lien modifications, foreclosure alternatives, and HOPE for Homeowners incentive payments subprograms have yet to be determined. According to Treasury officials, these specifications have not yet been made because they wish to retain flexibility under HAMP to target TARP funds to those subprograms that attract the largest numbers of borrowers, servicers, and mortgage holders/investors.

¹⁷HAMP is designed to commit a combined total of \$75 billion in GSE and TARP funds to offer assistance to up to 3 to 4 million borrowers. The estimate of 2-2.6 million first-lien modifications is approximately two-thirds of the estimated total 3 to 4 million first-lien modifications to be offered assistance under the combined program.

Table 1: Projected Cost and Number of Borrowers Targeted for Assistance Using TARP Funds under HAMP, as of July 14, 2009

HAMP subprograms (TARP funds only)	Estimated number of borrowers assisted	Initial subprogram funding level	Obligated
First-lien Modification	Up to 2 to 2.6 million	About \$32.5 billion	\$18.7 billion
Home Price Decline Protection	To be determined ^a	Up to \$10 billion	None
Second-Lien Modification	Up to 1 to 1.5 million	To be determined	None
Foreclosure Alternatives	To be determined	To be determined	None
HOPE for Homeowners Incentive Payments	To be determined	To be determined	None
Total initial HAMP funding level		Up to \$50 billion	

Source: Treasury, OFS.

^aAll modified first-lien loans are eligible for HPDP payments.

Treasury Has Focused Most of Its Efforts on the First-Lien Modification Program

The first-lien modification program is the largest and most developed of HAMP's five parts and will use TARP funds to share the cost of modifying first-lien mortgages over a set period (5 years or until the loan is paid off, whichever occurs first) with mortgage holders/investors in order to reduce to affordable levels the monthly loan payments of homeowners in danger of foreclosure.¹⁸ The first-lien program targets borrowers in default (defined as 60 days or more delinquent on their mortgage payments) or in imminent danger of default (borrowers that are current on their mortgages but facing hardships such as job losses or interest rate increases on their adjustable rate mortgages) for first-lien modifications. Initial HAMP guidelines for completing first-lien modifications were released on March 4, 2009, and updated guidance was issued on April 6, 2009.¹⁹ The guidelines set out the requirements for eligibility, loan underwriting, loan modification, and servicer compliance and reporting. Treasury has launched a Web site that describes first-lien modification opportunities under HAMP and provides self-assessment tools and calculators borrowers can use to determine if they might be eligible.²⁰ Through the

¹⁸Mortgage holders/investors can include servicers/lenders that own whole mortgages within their portfolio, as well as individuals or institutions that invest in pools of securitized mortgages.

¹⁹HAMP Supplemental Directive 09-01, Introduction of the Home Affordable Modification Program (Apr. 6, 2009).

²⁰Making Home Affordable, Help for America's Homeowners, <http://makinghomeaffordable.gov/>.

Web site, borrowers are directed to free housing counseling, homeowner events in their communities, and a hotline. According to Treasury, as of July 18, 2009, this Web site had been viewed over 27 million times.

Treasury has also established an additional Web site to communicate with potential and participating servicers. Servicers can use the Web site to register to participate in HAMP, obtain official HAMP guidance, and submit program data once they begin conducting HAMP trial first-lien modifications.²¹ As of July 14, 2009, 27 servicers had executed HAMP servicer participation agreements with Fannie Mae, the HAMP administrator. The servicer participation agreements for HAMP specify the loan modification and other foreclosure prevention services to be performed, the payment structure for the first-lien subprogram, and other requirements, including those concerning audits, reporting, and data collection and retention. The agreements specify actions Fannie Mae may take if a servicer defaults under the agreement, such as by failing to perform or comply with any of its material obligations. In the event of a servicer default, Fannie Mae has the authority, with Treasury's approval, to reduce the amounts payable to the servicer, require repayment of previous payments made under HAMP under certain circumstances, require the servicer to submit to additional oversight, or terminate the servicer's participation agreement. According to Treasury, participating servicers report that as of July 20, 2009 they had extended over 354,115 trial modification offers to borrowers and 180,305 trial modifications had begun.²²

To control total obligations for HAMP first-lien modifications, Treasury has set initial funding limits, or caps, for the potential total amount that will be obligated to each participating servicer. The caps include the maximum amount allotted to help reduce borrowers' mortgage payments and to pay the associated incentive payments to borrowers, servicers, and

²¹ Administrative Web site for Servicers, Home Affordable Modification Program, <https://www.hmpadmin.com/portal/index.html>.

²² This information has been reported to Treasury's financial agent by participating servicers. Treasury has not validated the number of trial modification offers extended or the number of trial modifications begun.

mortgage holders/investors.²³ Almost \$19 billion of the TARP funds had been obligated to these servicers as of July 14, 2009 (see app. I for a list of the servicers that had signed TARP agreements as of July 14, 2009.)

The first-lien modification program has three main features. First, a cost-sharing arrangement with mortgage holders/investors is designed to help reduce first-lien mortgage payments to 31 percent of the homeowner's gross household income. Mortgage holders/investors will be required to take the first loss in reducing the borrower's monthly payments to no more than 38 percent of the borrower's income. Treasury will then use TARP funds to match further reductions on a dollar-for-dollar basis, down to the target of 31 percent. For eligible loans with monthly mortgage payments that are already below 38 percent, Treasury will match servicers' reductions. This modified monthly payment is fixed, as long as the loan remains in good standing with the program for a maximum of 5 years or until the loan is paid off, whichever is earlier. Treasury estimated that HAMP would cut participating borrowers' existing monthly payments by one-third, on average.²⁴

A second major feature of the program is the required use of standardized loan modification procedures, including the application of a net present value (NPV) test on all loans that are 60 days or more delinquent and for those borrowers who are current but in imminent danger of default. The NPV test compares the "net present value" of expected cash flows from a

²³ According to Treasury, the initial cap allocations were based on publicly available data, or data submitted by the servicers once admitted to the program, and reflect Treasury's estimated cost to be paid by each servicer for modifications. For initial caps, set with publicly available information, the caps have been updated using more complete data on the servicer's mortgage portfolio. All servicer caps will be reassessed on a quarterly basis using data on the actual number of modifications made by the servicer under the program.

²⁴ According to Supplemental Directive 09-01, if the modified interest rate is below the interest rate cap, this reduced rate will be in effect for the first 5 years followed by annual increases of 1 percent per year (or such lesser amount as may be needed) until the interest rate reaches the interest rate cap, at which time it will be fixed for the remaining loan term. If the resulting rate exceeds the interest rate cap, then that rate is the permanent rate. The directive defines the interest rate cap as the Freddie Mac Weekly Primary Mortgage Market Survey rate for 30-year fixed-rate conforming loans, rounded to the nearest 0.125 percent, as of the date the agreement is prepared (the March HAMP guidelines define the interest rate cap as the lesser of this survey rate or the fully indexed and fully amortizing original contractual rate).

loan with a modification and the same loan with no modification.²⁵ If the estimated cash flow with a modification is “positive” (i.e., more than the estimated cash flow of the unmodified loan), the loan servicer is required to make the loan modification. According to Treasury, the NPV test increases mortgage holder/investor confidence and the consistency of borrower treatment under the program by providing a transparent and externally derived objective standard for all loan servicers to follow. In addition, the first-lien modification guidelines set forth the sequential modification process (the modification “waterfall”) that servicers are to follow to reduce payments. Specifically, to reach the target affordability level of 31 percent, interest rates must first be reduced to as little as 2 percent. If the debt-to-income ratio is still over 31 percent at the 2 percent interest rate, servicers must then extend the amortization period of the loan up to 40 years. Finally, if the debt-to-income ratio is still over 31 percent, the servicer must forbear—defer—principal until the payment is reduced to the 31 percent target.²⁶ Servicers may also forgive mortgage principal to achieve the target monthly payment ratio of 31 percent of the borrower’s income on a stand-alone basis or before any other step in the standard waterfall process set forth above.

A third major feature of the first-lien modification program is its incentive payment structure. Treasury will use HAMP funds to provide both one-time and ongoing, so-called pay-for-success incentives to loan servicers, mortgage holders/investors, and borrowers to increase the likelihood that the program will produce successful modifications over the long term and help cover the costs of modifying a loan (see table 2). In addition to the cost-sharing payment to reduce borrowers’ monthly payments to be paid to mortgage holders/investors, Treasury will make the following HAMP incentive payments:

- Servicer incentive payments include one-time payments of \$1,000 for each completed modification under HAMP.

²⁵The NPV test compares the expected cash flow from the loan if a modification were to be made using program guidelines against the expected cash flow from the loan if no modification were to be made and the loan remained in default or became current again.

²⁶The principal forbearance amount cannot accrue interest under the guidelines or be amortized over the loan term. Rather, the amount of principal forbearance will result in a balloon payment fully due and payable upon the borrower’s transfer of the property, payoff of the interest bearing unpaid principal balance, or maturity of the mortgage loan.

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- Servicers also receive an additional current borrower bonus incentive payment of \$500 when a loan is modified for a borrower whose loan is current. Mortgage holders/investors will also receive this type of incentive as a one-time payment of \$1,500 for each modification agreement executed with a borrower who is current on entering HAMP.²⁷
 - Borrowers who remain current on their mortgage payments are eligible for up to \$1,000 in annual, ongoing “pay-for-performance” incentives for 5 years to be used to pay down the mortgage principal.²⁸
 - Servicers are also eligible for up to \$1,000 in annual, ongoing, so-called pay-for-success incentive payments that accrue when monthly mortgage payments are made on time for 3 years after borrower’s monthly mortgage payment is modified.

According to Treasury, modifying the loans of borrowers facing a hardship that could make default imminent while they are current on their mortgage payments may reduce the likelihood that these borrowers will default on the modified loan. All HAMP matching and incentive payments are contingent on the successful completion of a trial period. All HAMP payments listed in table 2, except for the cost-reduction share payment and the one-time servicer incentive payment, are contingent on a reduction of at least 6 percent in the borrower’s monthly mortgage payment.²⁹

²⁷ According to program guidelines, servicers must determine whether a borrower is at imminent risk of default based on their own servicing standards. Potentially eligible hardships leading to imminent default may include, among others, job loss, income reduction, or an interest rate reset that makes mortgage payments unaffordable.

²⁸ The Internal Revenue Service has ruled that if a homeowner benefits from pay-for-performance success payments under HAMP, the payments are excludable from income under a specified exclusion. Rev. Rul. 2009-19, 2009 FED 46,412.

²⁹ Compensation for mortgage payment reduction matching and incentives may not be remitted until the completion of a successful trial modification period.

Table 2: Summary of HAMP Payments Using TARP Funds on First-Lien Modifications

Payment type	Payment beneficiary	Description	Payment period	Amount
Monthly payment reduction cost share	Mortgage holder/investor	Monthly one-to-one matching payments made to achieve 31 percent debt-to-income ratio for borrower.	Paid monthly by Treasury for up to 5 years beginning in the first month of the official modification.	Mortgage holder/investor first reduces the mortgage payment to 38 percent of the borrower's monthly income if the premodification payment is higher than that amount. Between 38 and 31 percent of the borrower's monthly income Treasury matches reductions down to 31 percent on a dollar-for-dollar basis.
Servicer incentive	Servicer	One-time payment for loans that successfully complete trial modification period.	Paid one time by Treasury in the first month of the official modification.	\$1,000
Current borrower one-time bonus	Servicer and mortgage holder/investor	To encourage modifications for nondelinquent borrowers.	Paid one time by Treasury in the first month of the official modification.	\$500 (servicer) \$1,500 (mortgage holder/investor)
Borrower Pay-for-performance success	Borrower	Annual payment for ongoing timely borrower loan modification payments. Success payments pay down borrower unpaid principal balance.	Paid by Treasury 12 months after the trial modification start date and annually thereafter for a total of 5 years.	Up to \$1,000 per year for 5 years
Servicer pay for success	Servicer	Annual incentive payment for ongoing borrower participation and timely payments in HAMP.	Paid by Treasury 12 months after the trial modification start date and annually thereafter for a total of 3 years.	Up to \$1,000 per year for 3 years

Source: Treasury, OFS.

A number of other HAMP first-lien loan modification features are intended to help reduce monthly payments and prevent foreclosures while protecting taxpayer funds. For example, to avoid helping borrowers with mortgages on investment properties, eligibility requirements limit HAMP to borrowers with owner-occupied properties. To qualify for the program, borrowers' incomes must also be verified. According to Treasury, accurately measuring income is critical to making sure the program is helping borrowers who truly need the assistance to remain in their homes and to preventing fraud. Furthermore, as we have reported in the past, particularly between the years 2000 and 2006, an increased number of private-label securitized loans were underwritten using limited or no

documentation of borrower income or assets.³⁰ For certain loans prospectively eligible for HAMP modification, servicers may have limited past data on the borrower's income or assets.

Borrowers must also demonstrate their ability to pay the modified amount by successfully completing a trial period of at least 90 days before the loan is considered modified and any government payments are made under HAMP. According to Treasury, this feature was instituted to ensure that loan modifications are affordable and sustainable, thereby reducing the amount of taxpayer funds that would be used for unsuccessful modifications. Further, servicers are required to screen all current borrowers who contact them with an economic hardship to see if there is a danger of imminent default. Treasury has not specified how servicers should screen borrowers for imminent default. Rather, according to HAMP guidelines, the servicer must make a determination as to whether a payment default is imminent based on the servicer's own standards for imminent default. One participating servicer told us that clarification from Treasury would be helpful on this point. In the process of making its imminent default determination, the servicer must evaluate and verify the borrower's financial condition in light of any financial hardship and investigate the condition of and circumstances affecting the property securing the mortgage loan. If the servicer determines that default is imminent, it must document in its servicing system the basis for its determination and evaluate the borrower for a HAMP modification using the NPV test. According to Treasury, loan modifications are more likely to succeed if they are made before a borrower misses a payment because, among other reasons, delinquent borrowers are often difficult to contact.

³⁰ GAO, *Information on Recent Default and Foreclosure Trends for Home Mortgages and Associated Economic and Market Developments*, [GAO-08-78R](#) (Washington, D.C.: Oct. 16, 2007).

**Treasury Informs
Borrowers with High Total
Household Debt They Must
Obtain Housing
Counseling but Does Not
Plan to Track Whether
Counseling Has Occurred**

HAMP requires borrowers with high total household debt levels (postmodification debt-to-income ratios of 55 percent or higher) to agree to obtain housing counseling, which according to Treasury, will help reduce redefaults.³¹ We have previously reported that it is important for any loan modification program to be designed to limit the likelihood of redefault.³² While HAMP requires high debt-to-income borrowers to agree to obtain this counseling, it does not require documentation that they actually received the counseling. Specifically, HAMP first-lien modification guidelines instruct servicers to send a counseling letter to borrowers with high total debt levels informing them that they must work with a counselor approved by the Department of Housing and Urban Development (HUD) on a plan to reduce their total indebtedness.³³ Borrowers are made aware of this requirement before entering the trial period in the cover letter to the trial period plan, and the trial period plan itself requires borrowers to certify that they will obtain counseling if the lender requires them to do so.

Treasury officials told us that they would not require proof that the borrowers had obtained housing counseling because Treasury does not want to deny a modification to borrowers that successfully complete the trial period but may not have obtained counseling. Treasury also did not want to delay modifications under the program until servicers built systems in coordination with counselors to track whether borrowers obtained counseling. Treasury officials told us that while designing HAMP, Fannie Mae, Freddie Mac, and servicers had expressed concerns about the difficulty and burden of communication between the servicer and the counseling agency to certify that borrowers had received counseling. Treasury has indicated that it will capture information on borrowers who access counselors through the Homeowners HOPE hotline listed on the

³¹The total household debt-to-income ratio is a comparison of the borrower's total monthly debt payments (such as monthly housing payments, any mortgage insurance premiums, payments on all installment debts, monthly payments on all junior liens, alimony, car lease payments, aggregate negative net rental income from all investment properties owned, and monthly mortgage payments for second homes) to the borrower's monthly gross income.

³²GAO, *Troubled Asset Relief Program: Status of Efforts to Address Defaults and Foreclosures on Home Mortgages*, [GAO-09-231T](#) (Washington, D.C.: Dec. 4, 2008).

³³HAMP Supplemental Directive 09-01. The counseling letter also informs borrowers that housing counseling is free of charge for the borrower.

Making Home Affordable Web site.³⁴ However, according to a senior administrator of that hotline, providing loan-level tracking on borrowers they counsel is a complicated issue. One national organization that has been involved in counseling HAMP high debt-to-income borrowers told us that it will soon be able to use its Web-based loan-level portal to track whether HAMP borrowers receive housing counseling.³⁵ Without knowing if borrowers who were told that they are required to obtain this counseling actually do so, or evaluating the performance of borrowers who do and do not receive counseling, Treasury will not know whether the requirement is meeting its purpose of reducing redefaults among high-debt-burdened borrowers.

Treasury Has Announced Four Additional HAMP Subprograms, but the Need for the \$10 Billion Home Price Decline Protection Subprogram Is Unclear

In addition to the first-lien modification program of HAMP, Treasury has announced a HAMP subprogram intended to partially protect mortgage holders/investors against future declining home prices and thus encourage additional loan modifications. It is also designing other HAMP subprograms intended to reduce payments on second mortgages, provide alternatives to foreclosure to homeowners who do not qualify for modifications or cannot maintain payments during the trial period or modification, and offer incentives to servicers and lenders involved in originating refinanced loans under the HOPE for Homeowners Program.

- On May 14, 2009, Treasury announced additional details on its HPDP subprogram, which is designed to use up to \$10 billion in TARP funds to encourage mortgage holders/investors to undertake more modifications by assuring them that their losses in housing markets experiencing high price declines will be partially offset. These incentives will be based on the severity of house price declines in different metropolitan area housing markets and the average house price in each of those markets. Treasury

³⁴The Homeowners HOPE hotline is operated by the Homeownership Preservation Foundation—a nonprofit organization that currently has a network of nine HUD-certified housing counseling agencies from across the United States that offer free housing counseling to callers.

³⁵NeighborWorks America is an organization chartered by Congress that has been appropriated \$410 million in federal funds to operate the National Foreclosure Mitigation Counseling Program. Consolidated Appropriations Act of 2008, Pub. L. No. 110-161, Div. I, Title III, 121 Stat. 1844, 2441 (2007) (\$180 million); Economic Recovery Act of 2008, Pub. L. No. 110-289, Div. B, Title III, § 2305, 122 Stat. 2654, 2859 (2008) (\$180 million); and Omnibus Appropriations Act of 2009, Pub. L. No. 111-8, Div. I, Title III, 123 Stat. 524, 982 (2009) (\$50 million). Counseling from a HUD-approved counselor typically includes advice on defaults, foreclosures, and credit issues.

will make HPDP payments benefiting mortgage holders/investors annually for the first 2 years after the modification of a loan located in a metropolitan area with declining house prices.³⁶ No payments would be made if prices appreciate in the two quarters preceding modification of the loan. HPDP incentive payments will be included in future versions of the NPV model for loans being considered for modification under HAMP, and will, according to Treasury, increase the likelihood that the NPV calculation will produce a result in favor of modification. Although Treasury says that this incentive will increase the number of modifications made under HAMP, it has not yet stated how many more modifications might be made. According to Treasury officials, the number of additional modifications as a result of these payments depends on interactions with other changes in the NPV model and the specific subprogram parameters. Treasury is developing these estimates as the subprogram specifications are finalized.

According to Treasury officials, a loan with a positive NPV test result—that is one that would mean a mandatory modification—without the benefit of the HPDP payments will nonetheless receive this incentive payment, but only if the property is located in a qualified metropolitan area. It is not clear why mortgage holders/investors should further benefit from modifying loans that would pass an NPV test without an HPDP incentive solely because the properties are located in a market where home prices are declining. Providing HPDP payments for modifications that would have been made without this payment reduces the funds available for other HAMP efforts. As the subprogram is currently described, it is unclear how much of the \$10 billion allocated to the HPDP incentives would be needed to increase the number of modifications made under HAMP and maximize assistance to homeowners as provided for by the act. Furthermore, because none of the expenditures under HPDP would be recouped, it is crucial that Treasury ensure that funds are spent only when they are specifically needed to encourage additional modifications that would not be made without this incentive.

- On April 28, 2009, Treasury announced the framework for reducing payments on or, in some cases, extinguishing second liens for borrowers that receive first-lien loan modifications under HAMP. Treasury estimates that approximately 50 percent of the borrowers who may receive a HAMP

³⁶ As discussed later in this report, Treasury's custodian for TARP, Bank of New York-Mellon, will remit all payments under HAMP to servicers. Servicers are then responsible for distributing payments consistent with program guidelines to borrowers' accounts and mortgage holders/investors.

first-lien modification have second liens, and between 1 million and 1.5 million borrowers, might be eligible to receive a second-lien payment modification depending on servicer participation in this subprogram. Treasury plans to release second lien modification guidelines in late July or August 2009. Servicers that sign a second lien subprogram participation agreement will be obligated to modify the second lien when a HAMP modification is performed on the associated first lien. The second-lien modification will include an interest rate reduction down to 1 percent and a reamortization of the loan to match the terms of the modified first-lien. There will be three types of incentives under this subprogram: a servicer incentive, an investor incentive, and a borrower incentive that will be applied toward paying down the principal on the first lien if the borrower is successful in making payments on the second. As an alternative to modifying the second lien, the servicer will have the option of paying it off in exchange for a lump sum payment under a preset formula. According to Treasury officials, the purpose of the second-lien subprogram is to help lower total monthly household debt payments and increase affordability of the second mortgage. As we have seen, Treasury has yet to determine the cost of the second-lien modification subprogram.

- Another planned HAMP subprogram provides alternatives for borrowers that do not qualify for a loan modification under the first-lien subprogram or cannot maintain payments during the trial period or modification but want to avoid foreclosure. Treasury states that these alternatives will be less costly to mortgage holders/investors than foreclosures because the borrower, servicer, and investor will avoid the foreclosure process entirely. According to an announcement by Treasury on May 14, 2009, participating servicers will be required to consider a short sale and, if that is unsuccessful, a deed-in-lieu of foreclosure when eligible borrowers are not able to complete a modification under HAMP. A short sale allows the borrower to sell the property at its current value even if the sale nets less than the total amount owed on the mortgage. With a deed-in-lieu under HAMP, the borrower voluntarily transfers ownership of the property to the servicer (provided the title is free and clear of additional liens). Servicers will receive compensation of \$1,000 for a short sale or deed-in-lieu, and borrowers will receive \$1,500 for relocation expenses. The Foreclosure Alternatives Program is designed to minimize the negative impact foreclosures can have on communities, including home price decline, vandalism and crime. This subprogram is still under development, and Treasury has not yet released detailed guidelines or estimated the overall cost or number of borrowers it expects to reach with these foreclosure alternatives. According to Treasury officials, detailed guidelines are expected by the end of August.

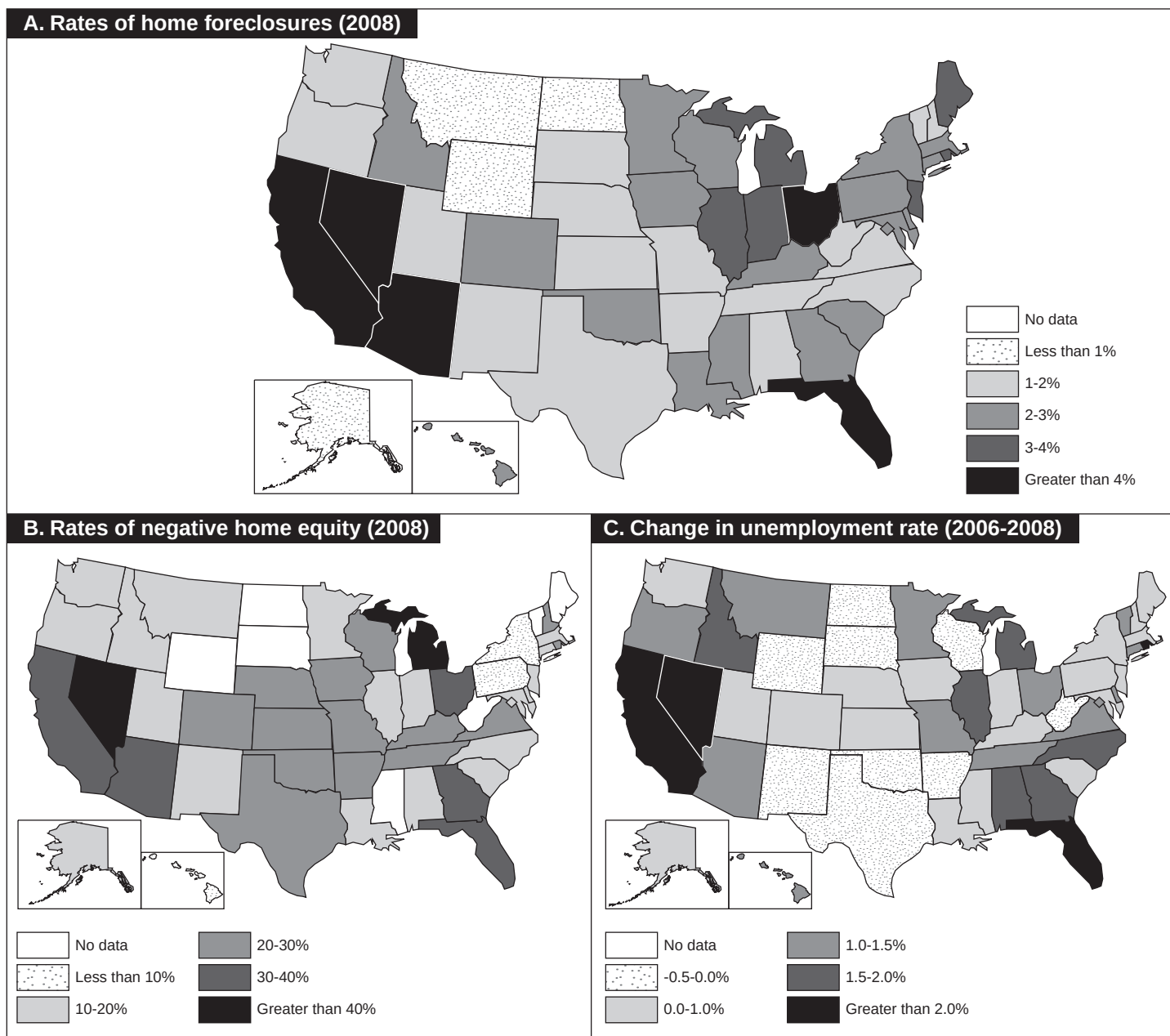
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- On April 28, 2009, Treasury announced that it would partially support additional loan refinancings under the HOPE for Homeowners program. Servicers and lenders that help make mortgages more affordable for struggling homeowners through HOPE for Homeowners will receive pay-for-success incentive payments comparable to some of the incentive payments made under a HAMP first-lien modification. Servicers can receive a \$2,500 up-front incentive payment for a successful HOPE for Homeowners refinancing. Lenders who originate the new HOPE for Homeowners refinanced loans are eligible for success fees of up to \$1,000 per year for up to 3 years, so long as the refinanced loan remains current. According to Treasury, it will use TARP funds targeted for HAMP for these incentive payments. Treasury has not yet estimated the overall cost or the number of borrowers it expects to reach with the HOPE for Homeowners incentive payments.

HAMP May Not Resolve the Challenges of a Growing Segment of Borrowers with Negative Equity in Their Homes

According to Treasury officials, HAMP's overriding policy objectives are to make mortgages more affordable for struggling homeowners; maximize participation by borrowers, servicers, and mortgage holders/investors; implement HAMP quickly; and maintain reasonable budget costs. As a result, HAMP, which deals with making borrowers' monthly payments affordable by reducing them to the target of 31 percent of their gross household incomes, does not focus directly on the issue of negative equity that is experienced by a large and growing segment of borrowers (so-called "underwater" borrowers). When a borrower owes more on the mortgage than the house is currently worth, the affordability of monthly payments may not be the only consideration in the borrower's decision to stay in the house. Several other factors may influence the borrower's decision to default, including the degree to which the borrower is underwater, the borrower's expectation of future house prices, the borrower's current employment status and wealth, and possibly the borrower's views on the moral and social acceptability of default. As shown in figure 4, many states with high foreclosure rates also have high proportions of mortgages with negative equity, and these proportions are often higher in states with large increases in unemployment.³⁷

³⁷Home foreclosures data (based on foreclosure inventories) are from the *National Delinquency Survey* by Mortgage Bankers Association, December 31, 2008. Negative equity is measured as properties with 5 percent or less equity to account for borrowers on the margin of being underwater. The data are available for only 44 states. See Table 1, *Summary of December 2008 Negative Equity Data from First American CoreLogic*, March 4, 2009. Unemployment rate data are from the *Unemployment Rates for States*, Bureau of Labor Statistics, <http://www.bls.gov/lau/lastrk06.htm> for 2006 and <http://www.bls.gov/lau/lastrk08.htm> for 2008. The percentage point change in unemployment is used to reflect the change in the economic status of borrowers in states.

Figure 4: Rates of Home Foreclosure, Negative Equity, and Unemployment by State



Sources: GAO analysis of Mortgage Bankers Association, First American CoreLogic, and Bureau of Labor Statistics data; Art Explosion.

Although HAMP does not address the issue of negative home equity directly, Treasury officials emphasized that underwater borrowers were not precluded in any way from applying for HAMP loan modifications and that HAMP had no loan-to-value ratio (LTV) ratio requirements. The officials also told us that ultimately the overall homeownership preservation program, Making Home Affordable (MHA), would have initiatives designed to address other factors affecting foreclosures, such as negative equity. For example, servicers are required to simultaneously evaluate borrowers for a trial loan modification under HAMP and HOPE for Homeowners refinance and to offer the HOPE for Homeowners option if possible. MHA will offer incentives to servicers under the HOPE for Homeowners program that are as generous as the incentives offered with HAMP modifications.³⁸ Under HOPE for Homeowners, borrowers could also benefit from principal reduction that would reinstate positive equity in their homes. In addition, borrower incentive payments under the HAMP first-lien modification program go toward paying down principal on a first-lien mortgage. Treasury officials also noted that other HAMP incentives could help address negative equity including the possibility of a principal write-down as part of reducing borrowers' monthly payments under HAMP.

Analyses by Fannie Mae showed that underwater borrowers who were eligible for loan modifications under HAMP because they were in default or in imminent danger of default could pass the NPV test for loan modification successfully. These analyses found that borrowers with high-LTV mortgages generally passed the NPV model test for loan modification.

Although Treasury has said that HAMP does not exclude and will ultimately offer specific tools to address the problem of underwater borrowers, there is still the possibility that some of these homeowners, facing the prospect of owing far more than their homes are worth, will walk away from their mortgages. A possible relationship between growing numbers of mortgage holders with negative equity and rising foreclosure rates suggests that the problem may become more critical, especially if home price declines continue. Currently no clear consensus exists on how to deal with underwater borrowers. In particular, lenders and

³⁸Under the HOPE for Homeowners program, new insured mortgages cannot exceed 96.5 percent of the current LTV for borrowers whose mortgage payments do not exceed 31 percent of their monthly gross income and whose total household debt does not exceed 43 percent; alternatively, the program allows for a 90 percent LTV for borrowers with debt-to-income ratios as high as 38 (mortgage payment) and 50 percent (total household debt).

policymakers face an information problem in trying to help borrowers with negative equity because it is hard to determine which borrowers really need help in order to stay in their homes. Nonetheless, the possibility of using negative equity as a criterion for loan modification should be approached with caution, given limited historical experience with large segments of borrowers with negative home equity and the potential for providing incentives to borrowers who would not default on their mortgages without them. We are currently undertaking further analysis to better understand the relationship between negative equity and the risks of defaults and foreclosures.

Treasury's Projection of the Number of Loans That Could Be Modified under HAMP Was Based on Uncertainties in Key Assumptions and May Be Overstated

Treasury's estimate of the number of borrowers who would likely be helped under HAMP reflects uncertainty created by data gaps and the need to make numerous assumptions, and this projection may be overstated. Further, documentation of the many assumptions and calculations necessary for the analysis is incomplete and Treasury has not specified plans for systematically updating its projections. While we acknowledge that Treasury was moving quickly to develop estimates for a new and untried program for which there were limited comparable data, more thorough documentation would help establish a credible baseline against which to monitor and revise key program assumptions to ensure the program objectives are being met.

Treasury's Projected Number of Loans That Could be Modified Is Complicated, Challenging, and Uncertain

The process for estimating the expected number of home loans that could be modified under HAMP is complicated and challenging, and the projection is uncertain. Treasury officials faced challenges in projecting the number of loans likely to be modified under HAMP. First, Treasury had to cope with incomplete data on the characteristics of mortgage loans and borrowers. For example, there is no single source of information on existing mortgages. Loan databases vary in the information collected and in their presentation, making it difficult to develop comparable and consistent bases for empirical projections. Also, it is arguable whether models of borrower and lender behavior based on experience prior to the mortgage crisis are completely relevant in predicting behavior in stressed markets because of the unprecedented severity of the housing price decline exacerbated by weaknesses in the overall economy. These conditions complicate the analysis and create uncertainty. Furthermore, Treasury officials had to develop the estimate very quickly. HAMP was initially announced on February 18, 2009, and Treasury published detailed guidelines and authorized servicers to begin modifications only 2 weeks later, when HAMP guidelines were publicly released on March 4, 2009.

Such a time constraint limited Treasury's ability to undertake rigorous empirical analysis to provide a projection that is robust to changes in its assumptions.

Treasury Projected That HAMP Could Help Up to 3 to 4 Million Borrowers, but Loans That Would Remain Current under the First-Lien Subprogram Could Be Lower

In order to support Treasury's policy design and cost estimation, it developed an initial internal projection that up to 3 to 4 million borrowers who were at risk of default and foreclosure could be offered a loan modification under HAMP. However, because of the unsettled dynamics of the mortgage market and overall economic conditions, actual outcomes may well be different from the projection. Treasury projected that about two-thirds of the eligible 3 to 4 million borrowers would have their mortgages modified using TARP funds and that the remaining one-third—those owned or guaranteed by Fannie Mae or Freddie Mac—would be modified using GSE funds. However, consistent with recent experience, not all of the loans modified under HAMP would likely remain current over the 5-year life of the first-lien subprogram. According to Treasury officials, the redefault rate estimates that they examined were for loan modification programs that predated HAMP, which likely did not result in monthly mortgage payment reductions or contain incentive payments similar to those of HAMP.

According to HAMP guidelines, loans that originated on or before January 1, 2009, may be eligible, and new borrowers will be accepted until December 31, 2012. Because the maximum possible length of the first-lien modification program for each loan after the 90-day trial period is 5 years, loans that enter HAMP in 2012 will have to terminate participation in HAMP by 2017. After completion of the first-lien modification program, borrowers' mortgage payments could gradually increase to levels consistent with an interest rate cap that reflects market conditions at the time the loan modification is made.³⁹

³⁹We have previously discussed the interest rate cap.

Treasury's Projection of Loans Likely to Be Modified Depends on Several Uncertain Assumptions and Requires Complete Documentation

Based on our analysis of Treasury's description and documentation of its process for determining the number of loans that could be modified under HAMP, we identified four phases, consisting of projecting the following:

1. the likely number of borrowers at risk of default/foreclosure;
2. the proportion of loans held by borrowers with debt-to-income ratios greater than 31 percent that were eligible for payment reductions because these loans were likely unaffordable;
3. the proportion of borrowers likely to apply for loan modification as determined by servicers' and borrowers' expected participation; and
4. the proportion of loans that would likely pass the NPV test for loan modification and be offered the 90-day loan modification trial.

As previously noted, HAMP has several eligibility requirements, including that the property be an owner-occupied, single-family residence (one to four units) that is the borrower's primary residence and that the mortgage loan amount not exceed the current threshold for so-called "jumbo" loans.⁴⁰

To determine the number of eligible loans likely to become at risk of foreclosure, Treasury used data from a variety of sources to make its initial projection that roughly 50.3 million active loans, excluding those insured by FHA or guaranteed by VA, existed, including those in default and already in the foreclosure process.⁴¹ Excluding loans that did not meet HAMP's eligibility requirements, Treasury calculated that about 47.4 million, or 94 percent, of this group might be eligible for loan modification.

Next, based on current mortgage market conditions and expected future changes in the performance of different types of loans, in March 2009, program officials projected that over 10 million loans, or 21 percent of the

⁴⁰Jumbo loans, which are eligible for HAMP, are loans that exceed the loan limits set by the GSEs and include conforming jumbo loans (those that can be purchased by the GSEs but are priced higher than nonjumbo loans).

⁴¹The data sources included Mortgage Bankers Association data for securitized loans, FHFA reports on data for loans owned or guaranteed by Fannie Mae and Freddie Mac, and loan data reported by industry participants. According to the program guidelines, loans owned or guaranteed by FHA, the Rural Housing Service, and VA will also be included in the Making Home Affordable program. As already discussed, loans owned or guaranteed by the GSEs are not modified using TARP funds but are modified using GSE funds.

existing total loans, would likely become at risk of foreclosure through the fourth quarter of 2012 (step 1 of fig. 5).⁴² Treasury officials underscored that this estimate was not a formal Administration projection and did not reflect an Administration view about either the housing market or economic recovery. Uncertainties exist in this projection both because of the problematic nature of forecasting the future macroeconomic situations including home prices, unemployment rates and other factors that have influenced default and foreclosure rates as well as the difficulty forecasting borrower decisions to default. Further complicating the projections is a lack of knowledge about the potential number of vacant homes and the number of investor-owned homes that are improperly or potentially fraudulently classified as owner occupied. A recent estimate by the Joint Center for Housing Studies of Harvard University indicated that the homeowner vacancy rate for the nation had reached a record high of 2.8 percent last year. For homes built since 2000, the vacancy rate was 9.7 percent in 2008, a jump of almost 4 percentage points in just 2 years.⁴³ Because of the recent increase in vacancy rates and the potential number of homes owned by investors and not households, Treasury's estimate of owner-occupied homes, and thus of the number of borrowers HAMP could assist, may be overstated.

The second step of the estimation considers the HAMP's requirement that borrowers' current debt-to-income ratios exceed 31 percent. Extrapolating from limited data on borrowers' current debt-to-income ratios, Treasury projected that 80 percent of the over 10 million loans at risk of foreclosure would meet this requirement, or about 8.4 million loans, because these loans are likely unaffordable (step 2 of fig. 5).

Third, the estimation required an assumption about the participation of eligible borrowers who apply for loan modification. Treasury projected that 65 percent (about 5.5 million loans) of the targeted group of borrowers (borrowers at risk of foreclosure and with debt-to-income ratios exceeding 31 percent) would likely apply for loan modification under HAMP (step 3 of fig. 5). According to Treasury, this projection is consistent with its projection that enough servicers would participate in

⁴²Program officials indicated they had made projections of the number of loans that would be at risk of defaults and foreclosures from a number of sources, including the private and public sectors.

⁴³See *The State of the Nation's Housing 2009*, Joint Center for Housing Studies of Harvard University, 2009.

HAMP to cover approximately 90 percent of the potential loan population and that the borrower response rate would be more than 50 percent. In developing the participation rate, Treasury officials told us they considered a number of possible combinations of the servicer representation rate and borrower participation rate, including a borrower participation rate of 70 percent. However, Treasury's estimate of lender participation has not yet been borne out by experience. As of July 14, 2009, 27 loan servicers (including the 5 largest U.S. servicers) had signed participation agreements. Treasury estimated that these participants represented about 76 percent of non-GSE loans (see app. I for a listing of the servicers that had signed agreements as of July 14, 2009). As previously noted, HAMP covers GSE loans, as well as non-GSE loans. According to Treasury officials, servicers with signed participation agreements represent around 85 percent of GSE and non-GSE loans in the country. Treasury officials noted that the process of signing up servicers is ongoing, that servicer participation rates have been increasing, and that several servicers were "in the pipeline" and ready to sign contracts shortly. In deciding to participate, servicers can be influenced by several factors, including their own capacity to modify loans and the appeal of the government's incentive programs. It remains to be seen how many more servicers will decide to sign up for HAMP.

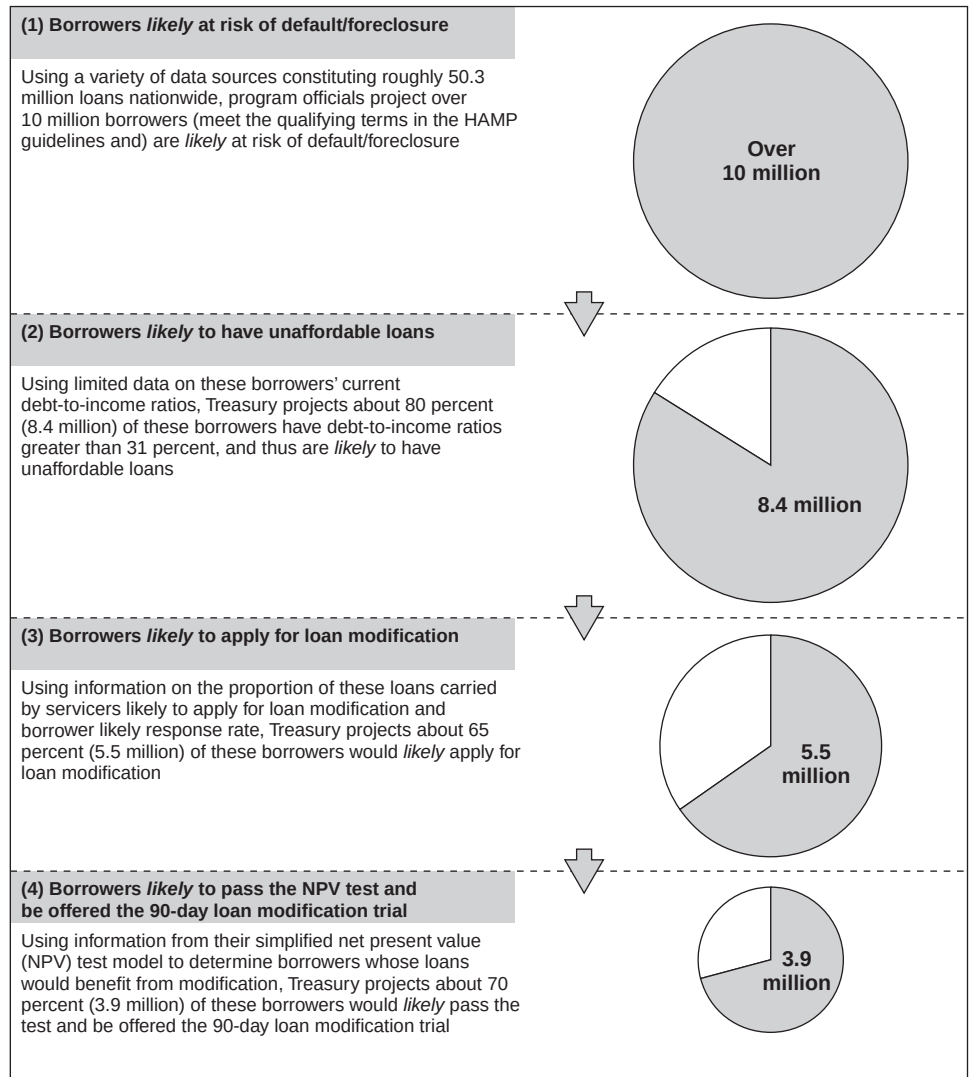
Treasury's projected response rate for borrowers may also be too high. The program that is most like HAMP—FDIC's IndyMac Federal Bank loan modification program—thus far has had a maximum response rate of 50 percent for borrowers, well below the rate projected for HAMP.⁴⁴ Treasury stated that HAMP's participation rate will likely be higher, in part because of the outreach Treasury has done to publicize it. According to Treasury officials, a number of steps have been taken to raise awareness of the first-lien modification program consistent with the Presidential announcement and the high-profile nature of HAMP. These steps include creating a Web site that is targeted toward borrowers and that, according to Treasury officials, received over 27 million page views as of July 18, 2009. Treasury officials also said that, according to servicers, more than 1 million letters had been mailed to borrowers to inform them about HAMP and that servicers had reviewed several hundred thousand current and delinquent loans for potential eligibility.

⁴⁴On July 11, 2008, FDIC was named conservator of IndyMac Federal Bank. Soon after, FDIC developed a loan modification program to convert nonperforming mortgages owned or serviced by the bank into affordable loans.

However, Treasury's estimate includes borrowers holding mortgages on homes that may not be owner-occupied, which are specifically excluded from HAMP participation. Further, not all potentially eligible borrowers may decide to participate in HAMP for a variety of reasons—for example, because of their experience with loans that eventually became unaffordable or because they may have limited knowledge about HAMP. Moreover, borrowers cannot participate in HAMP unless their servicers also do. Borrowers with servicers who elect not to participate in HAMP will thus be excluded. All these factors suggest that Treasury's estimate of the participation rate may well be optimistic, but Treasury has planned to provide resources to support the targeted projection.

Treasury's fourth step in the process of calculating how many homeowners the first-lien modification subprogram would help was to estimate the number of loans that were likely to pass the NPV test required to start a 90-day loan modification trial. Treasury officials developed a simplified NPV test model to help determine the expected number of loans that would be modified. As previously discussed, the NPV test is considered positive for loan modification if the total expected cash flow of a modified loan is greater than the total expected cash flow of an unmodified loan. Servicers are required to modify loans when the NPV test shows this "positive" outcome, while they have the discretion to modify loans that do not pass the NPV test or to pursue alternatives to foreclosure such as short sales or deeds-in-lieu. Treasury estimated that about 70 percent (3.9 million) of the at-risk population of borrowers tested would likely pass the NPV test and be offered the 90-day trial modification (see step 4 in fig. 5).

Figure 5: Treasury's Projections of Homeowner Participation in HAMP, Reflecting Uncertainties Due to Data Gaps and Necessary Assumptions, 2009-2012



Source: GAO analysis of OFS documents, as of March 2009.

Note: The data include loans modified using TARP funds and loans modified using GSE funds.

Among the 3.9 million borrowers likely to be offered trial modifications, not all of the borrowers will successfully complete the trial period. In addition, some borrowers will subsequently default on their modified loans after completing the trial period. According to Treasury officials, the redefault rate estimates that it examined were consistent with the Office

of the Comptroller of the Currency's (OCC) and Office of Thrift Supervision's (OTS) analyses of loan modifications, as well as with FDIC's IndyMac Bank estimates. For example, the IndyMac Federal Bank loan modification program, which is the program most like Treasury's, used a 40 percent redefault rate in its base NPV spreadsheet to determine the value of modifying a loan.⁴⁵ In their most recent quarterly Mortgage Metrics Report dated June 30, 2009, OCC and OTS reported the percentage of borrowers that had redefaulted (60 days or more delinquent) on their modified loans ranged between about 23 percent at 3 months following modification to about 52 percent at 12 months following modification.⁴⁶ However, Treasury officials stressed that it was difficult to compare potential HAMP redefault rates to those for other loan modification programs because of significant differences in program features. In particular, they noted that loan modifications that did not result in monthly mortgage payment reductions similar to those required under HAMP (31 percent debt-to-income threshold) or contain incentive payments similar to HAMP's would not provide an adequate basis for comparison. Also, the data cover activities of only certain member institutions (9 national banks and 4 thrifts) and, therefore, may not fully represent all market segments, including the subprime lending market. In addition, the redefault rates reported by others are for loans that have been recently modified (typically within the last 12 months or less), while the life of the HAMP, over which redefaults would be measured, covers five years.

Treasury officials have indicated that some of their key assumptions involve significant uncertainties, and these uncertainties make the need for complete and accurate documentation of the assumptions and analyses supporting the estimates of critical importance. The lack of adequate documentation and incomplete specification of many of the assumptions underlying Treasury's projection of the number of borrowers who could be helped by HAMP makes it difficult to assess the reliability of the

⁴⁵ According to FDIC, the redefault rate used in its NPV spreadsheet was estimated per historical re-default experience for other modification programs and a program specific projection.

⁴⁶ See Office of the Comptroller of the Currency and Office of Thrift Supervision, *OCC and OTS Mortgage Metrics Report: Disclosure of National Bank and Federal Thrift Mortgage Loan Data First Quarter 2009*, June 2009. This report presents key data on first lien residential mortgages serviced by national banks and thrifts, focusing on mortgage performance, loan modifications, payment plans, foreclosures, short sales, and deed-in-lieu-of-foreclosure actions.

estimates and, going forward, may hinder efforts to evaluate how well the first-lien program is meeting its objectives.⁴⁷ In order to improve the validity of the overall projection of the number of loans that would be modified under HAMP, it is essential that the process be supported by detailed information and complete documentation and that the key assumptions and calculations are regularly reviewed and updated.

Treasury Has Developed but Not Finalized the Oversight Structure for HAMP, and Is Not Systematically Evaluating Servicers' Capacity during Program Admission

Treasury has taken a number of important steps toward implementing operational procedures and internal controls for HAMP including establishing an organizational structure for overseeing HAMP; delegating implementation authorities and responsibilities to its financial agents; and drafting work flows, such as the allocation process for each participating servicer. However, significant gaps in its oversight structure remain, including the lack of a full complement of permanent staff in OFS's Homeownership Preservation Office (HPO), the office responsible for HAMP governance, and the lack of a finalized comprehensive system of internal control for the program, including policies, procedures and guidance for program activities. In addition, it is unclear when comprehensive processes will be in place to address noncompliance among servicers, including processes to ensure that servicers evaluate borrowers in imminent danger of default for HAMP participation. Further, Treasury has not established procedures to consistently evaluate the capacity of participating servicers to fulfill HAMP requirements or to assess any risk that individual servicers may pose to the program during the admission process. Moreover, some servicers have raised concerns about the complexity and burden of HAMP's data collection and reporting requirements, suggesting that these servicers may not have the capacity to fulfill HAMP requirements. Without a consistent method of evaluating all servicers during program admission, Treasury is limited in its ability to identify, assess, and address potential risks that could prevent servicers from fulfilling program requirements.

⁴⁷For example, Treasury has not provided supporting documentation for why a borrower response rate of 70 percent is reasonable. Also, program officials have not provided detailed information and supporting documentation for the program's projection of the proportion of the existing total loans that would likely become at risk of foreclosure.

Treasury and Its Financial Agents Have Taken Steps to Design Procedures and Controls to Implement HAMP but Have not Finalized a Comprehensive System of Internal Control

In implementing HAMP, Treasury developed an organizational structure that delegates some administrative and oversight responsibilities to its financial agents while retaining authority for overall HAMP implementation. According to Treasury, the broad responsibilities that have been delegated to its financial agents—Fannie Mae, Freddie Mac, and Bank of New York-Mellon—have been delineated in the agreements that have been signed with these entities, with specific roles assigned to each entity:

- Fannie Mae, as the HAMP program administrator, is responsible for developing and administering program operations including registering, executing participation agreements with, and collecting data from servicers.
- Freddie Mac, as the HAMP compliance agent, is responsible for compliance and audit of the program, including onsite and remote servicer reviews and audits. According to Freddie Mac, its authorities include conducting announced and unannounced information technology testing, security reviews, and audits. In addition, Freddie Mac officials said they would manage any corrective action and report compliance violations to Treasury and other regulatory agencies.
- Bank of New York-Mellon, as Treasury's custodian and payment agent for TARP, is responsible for remitting mortgage payment reductions and program incentive payments to participating servicers.

Individual servicers enter into servicer participation agreements that set out their responsibilities, including processing loan modifications that adhere to program guidelines; reporting complete and accurate data to Fannie Mae; receiving and distributing incentive payments for borrowers and investors; properly applying payments to borrower accounts; and developing, enforcing, and conducting internal reviews of an internal control process that monitors and helps ensure program compliance. As previously discussed, the servicer participation agreement specifies actions Fannie Mae may take if a servicer fails to perform or comply with any of its material obligations under the program including reducing the amounts payable to the servicer, requiring repayment of previous payments made under HAMP under certain circumstances, requiring the servicer to submit to additional program oversight, or terminating the servicer participation agreement.

Within Treasury, OFS's HPO has primary responsibility for HAMP implementation. According to Treasury, roles within HPO include audit

oversight, Congressional and regulatory liaisons, communications and marketing, policy development, data analysis, and operations. HPO officials told us that they rely on several other OFS and Treasury support offices, including those involved with compliance and risk, internal controls, cash management, and human resources to assist HPO with various aspects of HAMP governance.

While much of Treasury's organizational structure for HAMP has been established, as we have previously reported, hiring efforts for HAMP are still ongoing.⁴⁸ Although HPO was created in November 2008, and its current structure established in March 2009, some of its positions continue to be filled with temporary detailees from other offices or agencies, and many positions remain vacant. According to Treasury officials, all director positions within HPO have been filled. However, although Treasury has continued to seek a highly qualified candidate to fill the position of Chief Homeownership Preservation Officer, as we stated in our most recent TARP 60-day report, it has been filled by interim chiefs. According to Treasury, as of July 16, 2009, 11 positions are filled with permanent employees and 3 are filled with temporary detailees, while 17 positions remain vacant. According to OFS's strategic workforce plan, Treasury will perform a review of each major component of OFS on a bi-monthly basis to assess continuing workforce needs and determine where adjustments are needed, including whether positions are filled by appropriate staff, whether position descriptions need to be updated, and whether there are staffing gaps that need to be addressed.

According to Treasury, as of July 2009, a bi-monthly review of HPO had not yet been conducted but would be scheduled later in the month. Because HAMP is a new and untested program involving significant outlays of taxpayer dollars to privately owned companies (servicers) and mortgage holders/investors, it will be important for HPO to continue to regularly evaluate the number of staff and their competencies to ensure that it has the resources needed to effectively govern the program. Consistent with GAO's internal control standards, the quality of human capital policies and practices including, but not limited to, hiring affects the control environment.⁴⁹ A strong control environment will depend, in part, on the competence of staff hired to manage and perform program

⁴⁸GAO-09-658.

⁴⁹GAO, *Standards for Internal Control in the Federal Government*, GAO/AIMD-00-21.3.1 (Washington, D.C.: November 1999).

operations. As we have previously recommended, Treasury should continue its hiring efforts in an expeditious manner to ensure that Treasury has the personnel needed to carry out and oversee TARP initiatives. Potential weaknesses in the control environment due to hiring and staffing deficiencies may limit Treasury's ability to plan, direct, and control HAMP operations and could put taxpayer funds at risk.

In addition to establishing an organizational structure for HAMP, Treasury has developed and, according to program officials, continues to refine key operational procedures and internal controls that it anticipates executing when the initial first-lien modification payments are made to servicers under HAMP. In particular, Treasury has drafted flow charts which delineate aspects of the overall HAMP process, using key internal control points with corresponding narrative descriptions. According to Treasury, internal controls have been implemented for transactions that have already occurred. To date, transactions have primarily involved the setting of servicer caps. On July 17, 2009, Treasury began a simulation involving Treasury, Fannie Mae, and Bank of New York-Mellon of the HAMP disbursement process that tested internal controls over the disbursement of TARP funds. However, complete policies and procedures for HAMP are still in draft and are scheduled to be completed by September 30, 2009. To ensure that program guidelines are followed consistently and resources are used appropriately throughout the HAMP process in the coming stages of the program, it will be important for Treasury to finalize and monitor its internal control system. As part of our future TARP work, we will continue to review Treasury's ongoing efforts to establish and implement a comprehensive system of internal control.

Treasury officials noted that they are developing performance measures for HAMP, an early draft of which includes process measures such as the number of servicers participating in the program and the number of borrowers being reached, as well as outcome measures such as average debt-to-income ratios (pre and post modification) and redefault rates. However, many of the specifics of these performance measures have not yet been defined. For example, Treasury has not specified the sources of the data to be used or the definitions of success for each measure. Further, the draft performance measures do not include measures of servicer performance, including whether servicers are meeting program requirements related to modifying loans for borrowers not yet in default. Treasury officials indicated that they will work with servicers to set more precise process measures for the program, including average borrower wait time for inbound borrower inquiries, the completeness and accuracy of information provided to applicants, and response time for completed

applications. Treasury officials also told us that by August 4th, Treasury will begin issuing monthly reports with some servicer-specific performance measures, including the number of trial modifications each servicer has extended to eligible borrowers, the number of trial modifications that are underway; the number of final modifications and, eventually, the long term success of those modifications. According to the Senate committee report accompanying the Government Performance and Results Act of 1993, annual performance goals are the major means for gauging progress toward accomplishment of longer-term program goals. In developing performance measurements, it will be important for Treasury to be able to evaluate HAMP's progress toward its goals, including preserving homeownership, and to define outcome measures that will be objective, measurable, quantifiable, and reflects the goals and mission of HAMP.

While HPO continues to refine the areas of the HAMP operational process that require direct Treasury involvement, Fannie Mae has begun mapping out the overall HAMP program process—including registration and data collection set up for participating servicers—and assessing potential risks in the overall processes to specify points for internal control. In addition, Treasury officials noted that they are currently reviewing with Fannie Mae its documentation of the processes around the calculation of incentive payments and the invoicing process. Treasury officials said Fannie Mae has provided Treasury for its review and comment the most recently available draft internal control documentation for HAMP processes for which controls have been designed, completed or executed. Treasury officials said they are participating in regular meetings with Fannie Mae personnel to discuss the different HAMP processes and associated internal controls.

According to Fannie Mae, the agency is developing controls to ensure the effectiveness of operations throughout the modification process, including those needed prior to making the first modification payment to servicers. For example, Fannie Mae officials noted that—working with Treasury and other agencies—they had developed automated edit checks for loans that were being electronically evaluated for HAMP eligibility. Fannie Mae has documented certain internal controls, including those that focus on registering, executing contracts with, and setting up servicers in HAMP electronic systems; the HAMP payment process; and the HAMP reporting process. Fannie Mae is working with Treasury to develop processes and internal control documentation for additional steps in the HAMP process, including, for example, trial modification administration and data collection and reporting. Fannie Mae has set a timeline for the

development, assessment, and testing of the administrative and set-up, record keeping and reporting, paying agent, and electronic data management processes for HAMP. According to the timeline, most processes will be designed by mid-August, with assessment and testing to continue through late October 2009. According to Treasury, as of June 30, 2009, Fannie Mae, in coordination with Treasury, performed effectiveness testing for three areas—servicer set-up, servicer caps, and incentive accruals (calculations of HAMP payments owed to each servicer in the immediate future). However, some processes that were scheduled to be completed by now are still under development. Specifically, setting up the trial modification process in Fannie Mae’s electronic data system, and the initiation and eligibility aspects of the official modification process were all scheduled to be completed in June 2009, but were still under development as of July 2009.

Freddie Mac has begun defining and documenting its HAMP compliance testing program. According to Freddie Mac, compliance reviews will take three approaches:

- announced reviews (remote and onsite), which will provide a structured and consistent process to assess servicer compliance;
- unannounced reviews (remote and onsite), which will provide the ability to review any loan at any time; and
- data analysis, including third-party data verification, which will provide ongoing analyses of servicers to identify patterns or trends that require investigation.

Freddie Mac plans to use these three approaches to verify participating servicers’ adherence to program guidelines and has begun to consider how potential areas of noncompliance will be identified. For example, Freddie Mac will conduct trial period reviews, which are on-site audits and file reviews targeting larger servicers and are intended to assess the strength of the servicer’s control environment, systems, and staffing. According to Treasury, the first trial review was completed in June 2009, two reviews began or will begin in July 2009, and four reviews are scheduled to begin in August 2009. In addition, to ensure that all eligible borrowers are given the opportunity to participate in the program, Freddie Mac indicated that it will use performance reporting data to track modification volume against expectations. According to Treasury officials, Freddie Mac will also develop a “second look” process, whereby it will audit modification applications that have been declined. Freddie Mac will coordinate with

servicers to address specific cases that surface as a concern, as well as more generally address potential operational weaknesses where errors prove more systematic. To identify fictitious modifications, such as modifications reported by a servicer on a loan that does not exist, Freddie Mac will take steps such as investigating borrower complaints and running database tests to identify multiple modifications for a single borrower.

However, it is unclear when Freddie Mac will have procedures in place to address identified instances of noncompliance among servicers. In particular, while Treasury has emphasized in program announcements that one of HAMP's primary goals is to reach borrowers who are still current on mortgage payments but at risk of default, no comprehensive processes have yet been established to assure that all borrowers at risk of default in participating servicers' portfolios are reached. For example, the program guidelines do not specify how servicers are to document inquiries from borrowers claiming to be at risk of default. According to Treasury officials, some procedures have been put in place to ensure that this goal is reached. For example, they said that Freddie Mac would assess whether servicers were offering modifications to borrowers who were not yet delinquent by reviewing servicer call records of borrowers in this situation who contacted servicers. However, it is unlikely that these reviews will provide a complete assessment of servicers' responses to borrower inquiries.

Neither Treasury Nor Its Financial Agents Are Systematically Evaluating the Capacity of Servicers to Fulfill HAMP Requirements during Program Admittance

Servicers are required to fulfill extensive program requirements, which for some servicers will necessitate increasing staffing and updating data collection systems. However, Treasury and its financial agents are not consistently assessing the ability of prospective HAMP servicers to meet distinct HAMP requirements and guidelines during the program admittance process. In November 2008, the federal banking regulators stated that banking organizations needed to ensure that their servicers were sufficiently funded and staffed to work with borrowers to avoid preventable foreclosures while implementing effective risk mitigation measures. However, in its March 2009 report, COP noted that servicers were generally understaffed, lacked the capacity to handle the pre-HAMP demand for loan workout requests, and had no apparent ability to handle a greater volume of loan modifications, such as that expected to be

generated under HAMP.⁵⁰ Furthermore, on July 9, 2009, the Secretaries of the Treasury and HUD sent a letter to participating servicers that identified a general need for servicers to devote substantially more resources to HAMP's loan modification program. In this letter, the secretaries asked that servicers appoint a high-level liaison to be the point of contact for implementation of the MHA program, expand their servicing capacity, and improve the execution quality of loan modifications. Consistent with GAO standards for internal control, program managers should identify potential program risks, and analyze them for their possible effect.⁵¹ As mentioned above, participating servicers agree to fulfill program requirements set forth in all program guidelines, including the servicer participation agreements they sign with Fannie Mae. The HAMP servicer registration process guidelines contain controls to validate the servicers and their portfolio size and activity level, and Treasury officials said that they were conducting weekly phone calls with servicers and planning a servicer conference.

Freddie Mac conducted readiness reviews of a limited number of servicers. However, Treasury officials told us that the readiness reviews were not intended to be used to evaluate servicers prior to entering the program, but instead were part of the program implementation process. Freddie Mac officials noted that the objective of these reviews was to assess servicers' readiness to (1) understand the requirements of the HAMP program; (2) effectively execute program requirements within their infrastructure; and (3) ensure compliance with program requirements by implementing new policies, procedures, and controls. Treasury described the reviews as a snapshot of how an initial group of servicers understood and could implement HAMP requirements. According to Treasury and Freddie Mac, readiness reviews of seven of the largest servicers that own or service some loans not owned by Freddie Mac or Fannie Mae have been completed and no additional readiness reviews are planned. As a result, 20 servicers that have executed agreements as of July 14, 2009, will not receive readiness reviews. Thus, without systematically conducting readiness reviews—or using other means of assessing servicer capacity—during the admittance process Treasury cannot identify, assess, and

⁵⁰Congressional Oversight Panel, March 2009. Loan workouts include forbearance plans and loan modifications, which are options to avoid foreclosure discussed previously in this report.

⁵¹[GAO/AIMD-00-21.3.1](#).

address risks associated with servicers that lack the capacity to fulfill all program requirements.

Moreover, Freddie Mac officials told us that they had initially planned multiday servicer readiness reviews that included both interviews and documentation reviews, but they indicated that the reviews to date consisted only of interviews with senior executives and that information gathered during the interviews was not verified. Freddie Mac also initially stated that if deficiencies were identified during servicer readiness reviews, a remediation plan would be developed and appropriate follow up actions instituted, but it later indicated that the reviews conducted did not involve any follow-up monitoring as a result of identified deficiencies. It is unclear how Treasury and Freddie Mac will follow up with servicer deficiencies identified as part of these reviews.

While Freddie Mac noted that servicers that had received readiness reviews were optimistic about their ability to meet program requirements, they also indicated that servicers needed adequate time to fully design, develop, test, and implement new procedures and infrastructure to properly handle cash movement and incentive disbursements. In addition, as part of these reviews servicers expressed concerns about their capability to monitor potential fraud among borrowers and said that they need greater guidance in identifying, assessing, mitigating, and disclosing potential noncompliance situations including those involving fraud, waste, and abuse.

Moreover, some servicers have expressed concerns about their ability to meet all program requirements, particularly with regard to data collection and reporting, outside of the readiness reviews. On April 6, 2009, Fannie Mae announced requirements for data collection and reporting by participating HAMP servicers and on July 6, 2009 it issued an update to this guidance.⁵² According to these guidelines, servicers are required to report selected data during the modification trial period and when the modification has been approved. Once the modification has been approved, servicers must begin reporting activity on HAMP loans on a monthly basis. These data reports are submitted to Fannie Mae in its role as HAMP program administrator and record keeper, and include loan identifiers, servicer registration and bank account information, and loan-

⁵²HAMP Supplemental Directive 09-01 and Home Affordable Modification Program (HAMP) Servicer Reporting Requirements.

level data such as borrower identification information and NPV test results. However, according to a HOPE NOW survey of some of its servicer members, none of the nine servicers that provided written responses could provide all of the 106 data elements that Treasury had deemed high priority, with servicers reporting that they could collect between 38 and 87 of these high-priority data elements.⁵³ In addition, during an outreach meeting Treasury held with 13 HAMP servicers, some participating servicers indicated that they would have difficulty collecting data and providing reports for all of the required data elements, citing barriers such as capacity issues, limited system platform capabilities, lack of experience with particular data elements, and incomplete guidance on data definitions and report templates. Similarly, all six of the servicers that we contacted also told us that they would need to develop separate platforms to capture HAMP data they had not collected in the past. For example, three out of the six small to large servicers specifically cited as a concern collecting demographic information (race, ethnicity, gender, etc.), which will be required as of October 1, 2009, because of the sensitive nature of the information.⁵⁴ Treasury updated its data definition document again on July 20, 2009. According to Treasury, HAMP's phased in data collection and reporting approach was developed to try to limit the burden of these requirements on servicers.

Treasury officials noted that nearly all of the servicers that were expected to participate in HAMP had already been approved through a GSE eligibility process.⁵⁵ Currently, all 27 participating HAMP servicers were GSE-approved servicers. However, some HAMP requirements are distinct from requirements set by GSEs. For example, as previously noted, some

⁵³HOPE NOW is an alliance between counselors, mortgage companies, investors, and other mortgage market participants to maximize outreach efforts to homeowners in distress to help them stay in their homes and creates a unified, coordinated plan to reach and help as many homeowners as possible. The Department of the Treasury and the U.S. Department of Housing and Urban Development encouraged leaders in the lending industry, investors and non-profits to form this alliance.

⁵⁴To help servicers implement HAMP, Fannie Mae issued a supplemental directive concerning the collection of such data. HAMP Supplemental Directive 09-02, Fair Housing Obligations under the Home Affordable Modification Program (Apr. 21, 2009).

⁵⁵Servicers who wish to service mortgages for Freddie Mac or Fannie Mae must meet certain criteria before being approved to service these loans. Eligibility requirements for both Freddie Mac and Fannie Mae primarily include being able to service mortgages in a manner acceptable to the GSE, meeting certain net worth requirements, agreeing to provide audit records and financial statements, and meeting specified insurance requirements.

servicers have expressed concern about meeting HAMP requirements. Therefore, even when HAMP participating servicers are GSE-approved, the servicers' capacity to implement a large-scale loan modification program has not been assessed and is unknown. Furthermore, in the future, HAMP servicers may include those that only service non-GSE loans. Treasury officials indicated that they plan to develop eligibility requirements for non-GSE servicers, but the assessment criteria and processes for implementing these requirements remain unclear. Consistent with GAO's standards for internal control, program managers should identify risks, consider all significant actions between the program and other parties, and analyze risks identified for their possible effect.⁵⁶ Without a comprehensive assessment of servicers' capacity or the potential risks servicers pose before they enter into participation agreements and receive taxpayer funds, Treasury and its financial agents cannot adequately determine the potential areas of risk individual servicers may pose. Further, they cannot mitigate the potential negative effects of these risks and may not be able to provide the additional support and guidance some servicers may need to properly meet all program requirements. We will continue to look at servicers' capacity to effectively implement HAMP as part of our ongoing TARP oversight responsibilities.

Conclusions

In our March 2009 report on TARP, we reported that significant program components and controls were under development for HAMP. Currently several components have not yet been implemented, and although the central program—the first-lien modification initiative—has been implemented, many of its administrative processes and its internal control policies and procedures are not yet finalized. HAMP is the cornerstone effort under TARP to meet the act's purposes of preserving homeownership and protecting home values. But as of the date of this report a number of HAMP programs remain largely undefined. Our analysis found weaknesses with the design and monitoring plans for the counseling feature of the first-lien modification program and the rationale for the HPDP program and with Treasury's estimate of the number of borrowers that might be helped under the first-lien modification program. Furthermore, we identified weaknesses with HAMP's management infrastructure and found that the development of some processes and internal controls was behind schedule. Finally, we are concerned that

⁵⁶ [GAO/AIMD-00-21.3.1.](#)

Treasury is not fully vetting servicers with which they contract to make modifications. One of Treasury's stated goals is to complete initial modifications quickly. But, unlike other TARP programs, such as the Capital Purchase Program, HAMP expenditures—which are projected to be up to \$50 billion—are not investments that will be partially or fully repaid but expenditures that, once made, will not be recouped. For this reason, a system of effective internal control over program expenditures is of critical importance.

The design of the first-lien modification program, which has been designed to reduce borrowers' mortgage payments to affordable levels by modifying their loans, does appear to largely meet the act's goals. Servicers that have entered into HAMP servicer participation agreements have reported that over 180,000 borrowers have entered into the trial period for the modification of their first-lien mortgages. A number of features have been built into the first lien-modification program to try to ensure that the program's objectives of helping borrowers in danger of foreclosure are met. The key feature is a cost-sharing arrangement between Treasury and the mortgage holder/investor to lower mortgage payments to 31 percent of the borrower's income combined with various incentive payments to servicers, mortgage holders/investors, and the borrower intended to facilitate and ensure the long-term success of the loan modification. One of HAMP's features intended to help reduce the rate of redefault on modified loans requires borrowers with high total household debt to obtain housing counseling. Treasury is not tracking whether all borrowers told they must obtain counseling do so, and thus may not know if this provision is having its intended effect or if a potential lack of borrower compliance may limit its impact.

Program guidelines and specific operational procedures have not been established for four other HAMP subprograms, and the need for one of these—the \$10 billion Home Price Decline Protection (HPDP) program—remains unclear. HPDP is designed to encourage investors to modify more mortgages by providing incentives to partially offset probable losses from home price declines. However, Treasury officials told us that they had not independently estimated the number of new modifications that incentive payments under this program might generate. Further, according to Treasury officials, incentives under HPDP might be paid to modify loans that already would have qualified for modification under the first-lien modification program using the NPV test. Although HPDP may provide incentives for some loan modifications that would otherwise not be made, without demonstrating the need for these incentive payments for all loans modified in a given area experiencing home price declines, Treasury may

not be maximizing assistance for helping homeowners avoid potential foreclosure as required by the act.

Treasury's estimates of the number of borrowers HAMP might help with first-lien loan modifications are also problematic. We recognize that Treasury was moving very quickly to develop these estimates for a program that has no relevant historical point of comparison. As a result, some of the key assumptions and calculations regarding the number of borrowers whose loans would be successfully modified under HAMP using TARP funds were necessarily based on limited analyses and data. However, Treasury's estimates of the number of homeowners who would likely participate in its HAMP loan modification program may be overstated. In developing these estimates, Treasury did not take into full account some of the variables underlying its assumptions about the behavior of both borrowers and servicers and did not provide full documentation for some of the key assumptions and analyses. Because of the lack of relevant historical data, the changing nature of the mortgage market, and the weaknesses in the national economy, the key assumptions and calculations are surrounded by uncertainty, and documentation is essential to establishing a baseline against which to monitor them. Treasury also did not indicate that it planned to update the information that it used in its assumptions, leaving open the possibility that its calculations could rapidly become outdated. Establishing a documented baseline and regularly updating these estimates would help Treasury and its stakeholders monitor program progress, identify problem areas as they emerge, and focus program resources.

Finally, administrative processes, including staffing, and a comprehensive system of internal controls have yet to be finalized. Of particular concern is the fact that the key leadership position for HAMP within HPO has not been permanently filled and that many other positions affecting HAMP remain open. Furthermore, although the office has been established for 10 months and its current structure has been in place since March 2009, HPO has yet to complete a bimonthly workforce planning review, as called for in each TARP office under OFS's strategic plan. Given, the importance of HPO's role with respect to monitoring the financial agents and privately owned servicers involved in the \$50 billion HAMP program, having enough staff with appropriate skills is essential to governing the program effectively. While some processes and internal controls have been developed for the early stages of program implementation, many more controls will need to be finalized as the program progresses, the first modifications are completed, and payments begin to ensure that taxpayer dollars are safeguarded, program objectives are achieved, and program

requirements are met. We also noted that Treasury had no plans to develop processes to systematically evaluate the capacity of servicers to fulfill specific HAMP requirements or to identify risks individual servicers might pose when they applied for the program. Some servicers have raised concerns about their ability to meet extensive program guidelines, and another TARP oversight entity has questioned whether servicers have the staff and operational framework to implement a large-scale loan modification program. Without a means of reviewing the capacity of servicers to fulfill program requirements, Treasury cannot be assured that initial modifications will be completed quickly—one of Treasury’s stated priorities for the program—or that they will be consistent with program guidelines. Because Treasury does not systematically evaluate servicers prior to admittance to the program, it is unable to identify, assess, and address risks, including those associated with servicers that lack the capacity to fulfill requirements such as collecting and reporting complete and accurate data, before executing a contract with them under HAMP. Given the magnitude of the investment in public funds for HAMP, and the fact that the program is structured to make direct purchase payments, rather than investments that may yield a return to the taxpayer as in other TARP programs, it is important for Treasury to work expeditiously to establish effective processes and controls to manage the program.

Recommendations for Executive Action

As part of its efforts to continue improving the transparency and accountability of HAMP, we recommend that the Secretary of the Treasury take the following actions:

- consider methods of (1) monitoring whether borrowers with total household debt of over 55 percent of their income who have been told that they must obtain HUD-approved housing counseling do so, and (2) assessing how this counseling affects the performance of modified loans to see if the requirement is having its intended effect of limiting redefaults;
- reevaluate the basis and design of the HPDP program to ensure that HAMP funds are being used efficiently to maximize the number of borrowers who are helped under HAMP and to maximize overall benefits of utilizing taxpayer dollars;
- institute a system to routinely review and update key assumptions and projections about the housing market and the behavior of mortgage-holders, borrowers, and servicers that underlie Treasury’s projection of the number of borrowers whose loans are likely to be modified under

HAMP and revise the projection as necessary in order to assess the program's effectiveness and structure;

- place a high priority on fully staffing vacant positions in HPO—including filling the position of Chief of Homeownership Preservation with a permanent placement—and evaluate HPO's staffing levels and competencies to determine whether they are sufficient and appropriate to effectively fulfill its HAMP governance responsibilities;
- expeditiously finalize a comprehensive system of internal control over HAMP, including policies, procedures, and guidance for program activities, to ensure that the interests of both the government and taxpayer are protected and that the program objectives and requirements are being met once loan modifications and incentive payments begin; and
- expeditiously develop a means of systematically assessing servicers' capacity to meet program requirements during program admission so that Treasury can understand and address any risks associated with individual servicers' abilities to fulfill program requirements, including those related to data reporting and collection.

Agency Comments and Our Evaluation

We provided a draft of this report to Treasury for review and comment. We received written comments from Treasury that are reprinted in appendix II. We also received technical comments from Treasury that we incorporated as appropriate.

In its written comments, Treasury stated that it would consider GAO's recommendations seriously as it moved forward. Specifically, Treasury stated that in response to its discussions about the program with GAO and others, it would continue to assess and implement changes to features of the program to improve its ability to assist the greatest number of borrowers most in need of assistance at the least cost to taxpayers. Treasury noted that there had never before been a government program designed to incentivize mortgage modifications and help struggling homeowners on the scale of the HAMP program, and that there were many uncertainties inherent in making projections about participation, cost and performance for a program that is unprecedented in size, scope, and goals. Accordingly, Treasury indicated that it planned on actively evaluating the program, testing key assumptions, and updating cost and participation estimates as the program progressed. Treasury also stated that it planned to staff positions in the Homeownership Preservation Office as quickly as possible. Treasury noted that it recognized that a strong compliance

system was critical to program effectiveness, and it was committed to finalizing its compliance processes as a top priority of the program. Lastly, Treasury stated that it planned to continue to assess servicers' capacity to meet requirements of the HAMP program and to work aggressively with servicers to ensure that capacity, implementation, and compliance requirements are met. As part of our ongoing monitoring of Treasury's implementation of TARP, we will continue to monitor Treasury's progress in implementing these and other planned initiatives in future reports.

We are sending copies of this report to the Congressional Oversight Panel, Financial Stability Oversight Board, Special Inspector General for TARP, interested congressional committees and members, Treasury, the federal banking regulators, and others. This report also is available at no charge on the GAO Web site at <http://www.gao.gov>.

If you or your staffs have any questions about this report, please contact Richard J. Hillman at (202) 512-8678 or hillmanr@gao.gov, Thomas J. McCool at (202) 512-2642 or mccoolt@gao.gov, or Mathew J. Scire at (202) 512-8678 or sciremj@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made major contributions to this report are listed in appendix III.

A handwritten signature in black ink, reading "Gene L. Dodaro". The signature is fluid and cursive, with a large, stylized "D" and a long horizontal stroke extending to the right.

Gene L. Dodaro
Acting Comptroller General
of the United States

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Chairman

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Vice Chairman
Committee on Appropriations
United States Senate

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The Honorable Dave Camp
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Committee on Ways and Means
House of Representatives

Appendix I: List of Servicers That Have Signed HAMP Participation Agreements, as of July 14, 2009

Dollars in thousands			
Name of Institution	Original cap	Adjustments to cap	Revised cap
Select Portfolio Servicing	\$376,000	\$284,590	\$660,590
CitiMortgage, Inc.	2,071,000	(991,580)	1,079,420
Wells Fargo Bank, NA	2,873,000	(462,990)	2,410,010
GMAC Mortgage, Inc.	633,000	384,650	1,017,650
Saxon Mortgage Services, Inc.	407,000	225,040	632,040
Chase Home Finance, LLC	3,552,000		3,552,000
Ocwen Financial Corporation, Inc.	659,000	(105,620)	553,380
Bank of America, N.A.	798,900	5,540	804,440
Countrywide Home Loans Servicing LP	1,864,000	3,318,840	5,182,840
Home Loan Services, Inc.	319,000	128,300	447,300
Wilshire Credit Corporation	366,000	87,130	453,130
Green Tree Servicing LLC	156,000	(64,990)	91,010
Carrington Mortgage Services, LLC	195,000	(63,980)	131,020
Aurora Loan Services, LLC	798,000	(338,450)	459,550
Nationstar Mortgage LLC	101,000	16,140	117,140
Residential Credit Solutions	19,400		19,400
CCO Mortgage	16,520		16,520
RG Mortgage Corporation	57,000		57,000
First Federal Savings and Loan	770		770
Wescom Central Credit Union	540		540
Citizens First Wholesale Mortgage Company	30		30
Technology Credit Union	70		70
National City Bank	294,980		294,980
Wachovia Mortgage, FSB	634,010		634,010
Bayview Loan Servicing, LLC	44,260		44,260
Lake National Bank	100		100
IBM Southeast Employees' Federal Credit Union	870		870
Total	\$16,237,450	\$2,422,620	\$18,660,070

Source: Treasury, OFS.

Note: Where Treasury has made no adjustments to the cap, we have listed the same amount for the revised cap as the amount listed for the original cap.

Appendix II: Comments from the Department of the Treasury



ASSISTANT SECRETARY

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

July 20, 2009

Thomas J. McCool
Director, Center for Economics
Applied Research and Methods
U.S. Government Accountability Office
441 G Street, N.W.
Washington, D.C. 20548

Dear Mr. McCool:

The Treasury Department (Treasury) appreciates the opportunity to review the GAO's latest report on Treasury's Troubled Assets Relief Program, entitled Home Affordable Modification Program. Treasury welcomes the recognition by the GAO that "The design of the first-lien modification program, which has been designed to reduce borrowers' mortgage payments to affordable levels by modifying their loans, does appear to largely meet the act's goals," as we continue to implement the Home Affordable Modification Program (HAMP) as part of the Administration's broad commitment to strengthening our nation's housing market. There is important work ahead, and we will consider the GAO's recommendations seriously as we move forward.

The current foreclosure crisis requires immediate aggressive action. The speed with which HAMP has been announced and implemented represents an enormous undertaking. This Administration has acted quickly to confront the economic challenges facing our economy and our housing market. Within weeks of assuming office, President Obama worked with Congress to enact the largest economic recovery plan since World War II. Shortly after signing the American Recovery and Reinvestment Act, the President announced Making Home Affordable (MHA), a critical element of our Financial Stability Plan.

Making Home Affordable is a comprehensive plan to stabilize the U.S. housing market and offer assistance to millions of homeowners by reducing mortgage payments and preventing avoidable foreclosures. The President's plan includes the Home Affordable Modification Plan (HAMP), which commits \$50 billion of TARP funds to loan modifications that will provide sustainably affordable mortgage payments for millions of borrowers.

President Obama announced MHA within a month of taking office. Just two weeks after announcing the program on Feb. 18th, the Administration published detailed program guidelines for HAMP and authorized servicers to begin doing modifications immediately. The first servicer contracts were signed on April 13, 2009. While many challenges remain, our progress in implementing HAMP to date has been substantial. As of July 20, 2009, we have signed contracts with 27 servicers. Between loans covered by these servicers and loans owned or guaranteed by the GSEs, more than 85 percent of all mortgage loans in the country are now

covered by the program. Over 325,000 modification offers have been extended and over 160,000 trial modifications are underway. Already, MHA has been more successful than any previous program to encourage mortgage modifications for at risk borrowers.

We recognize that challenges remain in implementation and scaling of the program, and are committed to working with the servicers to overcome those challenges and reach as many borrowers as possible. The recommendations in GAO's latest report are constructive as Treasury continues to implement its financial stability programs and enhance OFS performance. The GAO recommendations also track several initiatives that Treasury is already undertaking.

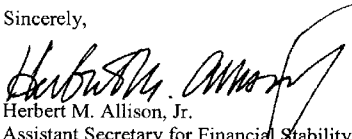
As the report indicates, there are many uncertainties inherent in making projections about participation, cost and performance for a program that is unprecedented in size, scope, and goals. There has never before been a government program designed to incentivize mortgage modifications and help struggling homeowners on the scale of the HAMP program. As the program progresses, we plan on actively evaluating the program, testing key assumptions, and updating cost and participation estimates. We also plan to continue to assess servicers' capacity to meet requirements of the HAMP program and to work aggressively with servicers to ensure that capacity, implementation and compliance requirements are met. We recognize that a strong compliance system is critical to program effectiveness, and are committed to finalizing our compliance processes as a top priority of the program.

As a part of our efforts to expedite implementation of the MHA program, Secretaries Geithner and Donovan recently wrote a letter to the CEOs of all of the servicers currently participating in the MHA program. The letter requested that the CEOs designate a senior liaison, authorized to make decisions on behalf of the CEO, to work directly with us on all aspects of MHA and attend a program implementation meeting with senior HUD and Treasury officials on July 28, 2009. In addition, the letter outlined the following three key implementation steps: (1) On August 4th, Treasury will begin publicly reporting results by servicer under the program; (2) In order to minimize the likelihood that borrower applications are overlooked or that applicants are inadvertently denied a modification, Treasury has also asked Freddie Mac, in its role as compliance agent, to develop a "second look" process pursuant to which Freddie Mac will audit a sample of MHA modification applications that have been declined; and (3) Treasury will work with servicers to set more exacting operational metrics to measure the performance of the program, such as average borrower wait time for inbound borrower inquiries, the completeness and accuracy of information provided to applicants, document handling, and response time for completed applications.

Treasury has implemented and continues to adapt an extensive and robust internal control system for HAMP. In response to our discussions about the program with GAO and others, we will continue to assess and implement changes to features of the program to improve its ability to assist the greatest number of borrowers most in need of assistance at the least cost to taxpayers. Lastly, Treasury continues to staff its positions in the Homeownership Preservation Office as quickly as possible. All director-level positions have been filled, and additional staff continues to be added on a regular basis.

Once again, Treasury appreciates the opportunity to review the report and GAO's thoughtful recommendations. We look forward to demonstrating further progress as program implementation continues.

Sincerely,



Herbert M. Allison, Jr.
Assistant Secretary for Financial Stability

Appendix III: Contacts and Staff Acknowledgments

GAO Contacts

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Staff Acknowledgments

In addition to the contacts named above, Susan Offutt (Chief Economist); Lynda Downing, Harry Medina, John Karikari (Lead Assistant Directors); and Tania Calhoun, Emily Chalmers, Rachel DeMarcus, Christopher Klisch, Damian Kudelka, Marc Molino, Mary Osorno, Julie Trinder, Winnie Tsen, and Jim Vitarello made important contributions to this report.

Related GAO Products

Troubled Asset Relief Program: June 2009 Status of Efforts to Address Transparency and Accountability Issues. [GAO-09-658](#). Washington, D.C.: June 17, 2009.

Auto Industry: Summary of Government Efforts and Automakers' Restructuring to Date. [GAO-09-553](#). Washington, D.C.: April 23, 2009.

Small Business Administration's Implementation of Administrative Provisions in the American Recovery and Reinvestment Act. [GAO-09-507R](#). Washington, D.C.: April 16, 2009.

Troubled Asset Relief Program: March 2009 Status of Efforts to Address Transparency and Accountability Issues. [GAO-09-504](#). Washington, D.C.: March 31, 2009.

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Auto Industry: A Framework for Considering Federal Financial Assistance. [GAO-09-242T](#). Washington, D.C.: December 4, 2008.

Troubled Asset Relief Program: Status of Efforts to Address Defaults and Foreclosures on Home Mortgages. [GAO-09-231T](#). Washington, D.C.: December 4, 2008.

Troubled Asset Relief Program: Additional Actions Needed to Better Ensure Integrity, Accountability, and Transparency. [GAO-09-161](#). Washington, D.C.: December 2, 2008.

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