Summary of AARP Solutions Forum

"The Foreclosure Crisis and Older Americans"

September 19, 2008

Panelists

William C. Apgar, Kennedy School of Government and Harvard Joint Center for Housing Studies
Michael S. Barr, Senior Fellow, Center for American Progress
George J. Gaberlavage, Director, Consumer Affairs, AARP Public Policy institute
Martin J. Gruenberg, Vice Chairman, Board of Directors, FDIC
Kathleen Keest, Senior Counsel, Center for Responsible Lending
David G. Kittle, Chairman Elect, Mortgage Bankers Association
Susan Reinhard, Senior Vice President, AARP Public Policy Institute
Marietta Rodriguez, President, AARP Foundation
Alison M. Shelton, Strategic Policy Advisor, AARP Public Policy Institute
Diane E. Thompson, of Counsel, national Consumer Law Center
U.S. Representative Barney Frank, Keynote Speaker

Overview

The AARP Public Policy Institute sponsored a Solutions Forum on September 19, 2008, to discuss the impact of the mortgage crisis on older Americans as well as proposals that could help both younger and older homeowners. The forum highlighted a groundbreaking new PPI report entitled "A First Look at Older Americans and the Mortgage Crisis", which presented the first analysis of delinquencies and foreclosures among Americans age 50 and over. Another purpose of this Solutions Forum was to stimulate discussion on several policy options to provide relief to homeowners in foreclosure and to prevent a similar crisis from occurring in the future.

The forum consisted of three panels: (1) a panel providing new data from AARP on the impact of the foreclosure crisis on older Americans; (2) a panel on legal and other barriers to mortgage loan modifications; and (3) a panel on proposals for preventing future mortgage crises.

Susan Reinhard and **Michael Barr** opened the forum by setting the context. Pointing to the recent turmoil in financial markets, Ms. Reinhard said that much of the focus has been on protecting investments and investors. However, this crisis has its roots in a consumer problem, namely the mortgage market, and the many homeowners at risk of losing their homes. Until recently, there has been very little discussion about older Americans and foreclosures, in large part because there hasn't been data. This forum will show that older Americans, age 50-plus, are indeed suffering from the mortgage crisis.

Mr. Barr noted that developments in the financial markets were moving very fast. He called for fundamental change, citing regulatory neglect, a lack of transparency and conflicts of interest. He also noted that voluntary programs to restructure mortgages and suspend foreclosures were not working.

IMPACT OF THE FORECLOSURE CRISIS ON OLDER AMERICANS

Robin Talbert, the moderator of the first panel, described the mission of the AARP Foundation as focusing on the needs of the most vulnerable older Americans.

Alison Shelton presented AARP's new data on the impact of the mortgage crisis on older Americans. Ms. Shelton described the lack of data on this issue from traditional databases. AARP bought from Experian a sample representing 2.5 million people, of which about 1 million are age 50 or over, for the six-month period ending on December 31, 2007.

AARP found that about 634,000 Americans age 50 and over were delinquent on their mortgages, and another 50,000 were in foreclosure or had lost their homes during the six months ending in December, 2007. About 28% of all delinquencies and foreclosures during the period were for people age 50 and over. Foreclosure rates for older African Americans and Hispanics are higher than for whites of any age. And having a sub-prime loan increases the chances of delinquency and foreclosure for older Americans by a multiply of nearly 17. Finally, older Americans are more affected by negative equity, i.e. a loan-to-value ratio of greater than 100 percent, than younger Americans.

Bill Apgar said the news is filled with descriptions of people who bought houses they couldn't afford. We can make it seem like this is the result of reckless behavior, but it's the result of thousands of little decisions to take a little bit more loan out to pay for the kids' education, to cover a health bill, to deal with the fact that housing costs are high relative to income. It's a reflection of the failure to deal seriously with our housing affordability issues – 3.5 million owners with a head age 50 or over devote more than 50 percent of their income to housing.

Today, seniors increasingly carry mortgage debt into retirement. By 2007, 53 percent of all homeowners age 50 or older had a mortgage up from 35 percent two decades ago.

The Experian data has been available for a while, but it's ironic that it was not being presented by HUD or Treasury or the Federal Reserve Board. There's something wrong that we don't have basic information about the dimension of this crisis. Mr. Apgar called on the government to put up some small amount of money in order to build a database that can really guide future policy deliberations.

Marietta Rodriguez noted that the Experian findings confirm many of the assumptions that NeighborWorks and other service providers have been dealing with in the last four years. Ms. Rodriguez indicated that some early data from NeighborWorks' National Foreclosure Mitigation Counseling Program showed that early 35 percent of homeowners who received counseling under the program are age 55 and older, and 21.5 percent of

counseling was provided to minority clients age 50 and older, particularly African-American women and Latin women in single-headed households.

Questions and Answers

Suzanna Montezemolo of AARP asked about the situation of renters after a foreclosure. Bill Apgar responded that we need to make better quality rental housing available to seniors, so that renting is a viable alternative to home ownership. But it is also true that foreclosures are going to put pressure on existing rental markets. Michael Barr added that we are seeing disruptions to renters when the home they are renting goes into foreclosure.

Hershel Liepo from the Comptroller of the Currency asked about the seasoning of the mortgages, refinancing and equity stripping. Alison Shelton responded that the Experian database has information on the age of the loan, home equity loans and lines of credit, and much other information.

Mauricio Soto of the Urban Institute asked for a context for the foreclosure rates in the Experian dataset, including historical data if it is available. He also asked the panel if the 1990s goal of homeownership for everybody was still appropriate, or attainable. Alison Shelton answered that Experian does have historical data, but it's very expensive so AARP didn't buy it. Marietta Rodriguez argued that homeownership is absolutely still appropriate for Americans, because it's a stabilizing force for families and communities, and because it allows older Americans to age in place. What we need is appropriate homeownership, appropriate financing, and education. Is homeownership right for everybody? No, but we should educate people so they can make the right decision.

GETTING THROUGH THE CRISIS: REMOVING IMPEDIMENTS TO MORTGAGE MODIFICATIONS

Kathleen Keest noted that she was standing in for Kurt Eggert, and presenting his paper. People have lost sight of the original cause, she said, which is that there's a self-reinforcing downward spiral that begins with foreclosures, which exacerbates a housing decline, which then creates more foreclosure. We need a circuit breaker, and the securitization process is standing in the way of solutions. We have a lot of voluntary loan modification programs which aren't working very well.

The Eggert paper envisions a regulatory model that includes routine oversight of servicers, where regulators go in periodically and try to catch things as they happen. Servicer duties should include loss mitigation.

Eggert's second recommendation concerns changing the bankruptcy law. Right now in Chapter 13 bankruptcy the court can reorganize your second home, investment properties, your yacht – but not your primary residence. So a logical solution would be to allow courts to modify payments on primary residences, but industry strongly opposes this. Eggert proposes a compromise that would establish a payment plan on the basis of fair market value, but also establish a sort of extra lien on the difference between the fair

market value and the balance of the debt. The plan would not force a sale of the house, but the second lien would be repayable when the house was sold.

A third recommendation concerns the government purchase of loans. It's similar to other proposals for a homeowners loan corporation. Eggert described a few potential pitfalls. One is to avoid having lenders sell their worst debt to the government while keeping the best debt, by having the purchase price reflect the real value and risk of the loan, so that the loss is taken by investors and lenders up front, rather than onto taxpayers at the back end. Perhaps an independent board should decide what types of loans to buy and the principal write-down. Another big hurdle is that the second lien holders can hold up everything because they have nothing to lose, so Eggert suggested using eminent domain to purchase those second liens.

Martin Gruenberg said he believes older Americans, in particular, have been a target of subprime mortgage lending because they often have accumulated equity in their homes and are targeted for refinancing. Refinancings have accounted for a majority of the sub-prime lending at its peak.

Mr. Gruenberg then talked about the FDIC's leadership in taking over troubled IndyMac, which has a large servicing operation which makes it possible for the FDIC to undertake loan modifications. The FDIC believes that sustainable loan modifications are in the interest of homeowners, neighborhoods, and investors and the holders or these mortgages. Recent FDIC sales of non-performing single-family home loans have come in at about 32 percent of book value, versus 87 percent of book value for sales of performing loans.

The FDIC has suspended most foreclosure actions for the IndyMac loans, in order to have time to evaluate the portfolio. In the IndyMac case, more than 60,000 mortgages are more than 60 days past due or in foreclosure, and of these about 40,000 are owned or serviced by IndyMac and could qualify for modification. The FDIC believes that about one-third of these will qualify for modification, in cases when it improves the value of the loan. The FDIC is using a combination of interest rate reductions, extended amortization and forbearance to arrive at an affordable payment, which it defines as about 38 percent of debt to income.

Since the FDIC announced the program in late August it has sent out over 7,400 loan modification offers. In the first three weeks of the program, well before the 30-day deadline that homeowners have to respond, over 1,500 homeowners have accepted the offers. In addition, Fannie Mae and Freddie Mac have agreed to be part of this program, which could make several thousand additional loans eligible. The FDIC also hopes that its loan modification program will serve as a model for others across the country.

David Kittle said there is enough responsibility to go around, but to identify a single entity or event, such as loan modification, as the sole cause of the financial crisis might not be the best course of action.

Mr. Kittle said that the MBA has long advocated for transparency in their business. Since 2003, the MBA has been advocating for a national standard against predatory

lending. MBA has proposed a new HUD settlement statement and a new one-page good faith estimate, where all the lines actually match. The MBA is also advocating that mortgage brokers have licensing, education, increased net worth requirements and a national registry. The MBA helped to start Hope Now, which has helped over 2 million people in foreclosure through the end of August. The MBA strenuously opposes "cram down" features in bankruptcy, however, which it argues would raise loan costs. When bankruptcy modification was permitted in 1978 for investment properties and second homes, these became higher risk loans that now require 20-25 percent down and one-and-a-half points over the rate for an owner-occupied home.

Mr. Kittle pointed out that nobody wins when a borrower goes into foreclosure. Short sales typically result in losses of about 19 percent compared to a loss of almost 40 percent when a loan goes through a full foreclosure sale. .

Aggressive marketing is in fact predatory lending and it is, across the spectrum, most severe on seniors, said Mr. Kittle. Seniors have great credit scores. And they are very proud people, so that when they get into a tough financial situation because of an illness or the economy, it's an embarrassment to have to call the lender and say that they are going to be behind on payments. Communicating with the borrower is the biggest challenge for MBA's member servicers.

Questions and Answers

Mr. Barr started the Q&A session by pointing out that there are ways of doing broad-scale loan modifications with relatively few legal changes, and he has a paper with Jim Feldman on how to do this by changing REMIC provisions under the tax code. Mr. Barr then asked Mr. Gruenberg whether the FDIC experience with IndyMac could serve as an example for the Treasury, which is now effectively running both Fannie Mae and Freddie Mac.

Mr. Gruenberg answered that the FDIC had been encouraged that Fannie and Freddie essentially permitted the FDIC to apply its loan modification program to the IndyMac program that they are implementing. So this suggests potential, although he wouldn't want to go beyond that.

Ms. Keest said that she had just been talking to an economist about the impact on the price of mortgages if the bankruptcy fix were enacted. And that economist cited Adam Levitin of Georgetown's paper saying something like a 20 basis points difference, rather than the larger spread that was talked about earlier. Mr. Kittle responded that loans on investment and second homes cost more than a loan on a primary residence, and this is because of the changes to bankruptcy laws 30 years ago.

Ms. Keest also mentioned a paper from Alan White of Valparaiso, who looked at servicers' remittance reports for 27 pools of mortgages. White found that 46 percent of the modifications involved either no payment changes, or payment increases. Less than one percent of the loan modifications White looked at involved principal reductions.

Mr. Gruenberg said the FDIC has determined that pooling and servicing agreements, to a greater or lesser degree, all allow significant opportunities for loan modifications. And the FDIC has also found that it's in everybody's interest for the modifications to be long-term and sustainable for the borrower, not a one- or two-year deal.

Alys Cohen from the National Consumer law Center asked Mr. Gruenberg about how they determined their 38 percent debt-to-income ratio, whether they had any information about residual income, and whether the FDIC is looking at other measures of affordability. Mr. Gruenberg responded that the FDIC reached the general conclusion that the 38 percent ratio is meaningful, and also is the one they can use based on the financial information available to them.

Alys Cohen asked Mr. Kittle about whether the MBA would make available more detailed data, so that policy people could drill down and understand problems better. Mr. Kittle responded that MBA data covers over 85 percent of loans that are serviced, which makes it credible. Releasing more information may have to do with privacy issues, although he would need to check.

Idriya Abdullah of the D.C. Department of Insurance, Securities and Banking said that not everybody was a victim and that we need to address the issue of consumer greed. Mr. Barr agreed that consumer greed was part of the problem but that has been overemphasized in the media, and there should be more attention to the greed of every other player in the system. Mr. Gruenberg said that while greed is a component, the majority of sub-prime mortgages were refinancings, and knowing the marketing that goes on, people were induced with representations that they could lower their monthly payment and also take equity out, and as a result they were refinanced into problematic mortgages. Mr. Kittle said that he needed to disagree because people also refinanced to pay off vacations, cars, lifestyle choices, even education.

Nina Simon of AARP Foundation asked Mr. Gruenberg whether the FDIC was writing down principal and, if not, why not. Mr. Gruenberg responded that the FDIC judged, based on legal authorities, that reducing interest rates was an easier way to reach affordability than principal write-downs.

PREVENTING FUTURE HOUSING MARKET CRISES

Diane Thompson started her presentation by arguing that we've reached a point where nobody – not homebuyers, not investors, not the industry – understands today's products. So while financial education is important, we've reached a point where no consumer is going to be able to understand these mortgages.

Also, research indicates that if you give people a payment stream representing a 35% interest rate, they will assume that it is an interest rate of about 10 percent. Even very highly educated people can only deal at any one time with two to three decision points.

Consumers need to focus on the most important features of the cost of credit. We already have two key disclosures in the Trust in Lending Act: the finance charge, which is a dollar amount of the total cost of credit -- the fees plus the rate); and the annual

percentage rate (APR), which combines the fees and the interest into a percentage rate like an interest rate over the life of the loan. The problem is that the Federal Reserve Board has allowed the finance charge to become essentially deregulated over the last 20 years, and they've allowed an increasing carve-out of almost ad hoc exceptions to the finance charge. The other piece of bad news is that HUD and the other agencies have undercut the use of the APR by not including it and not highlighting it in their disclosures.

We need to strengthen the APR so that consumers can do meaningful shopping and protect their own interest.

Bill Apgar said the key is to remember that financial markets didn't get here overnight, these structural weaknesses have been around for a while. He said that if he had just one recommendation, it would be that everybody who engages in the same activity in an economic sense should be governed by the same regulation in the market.

Mr. Apgar said that there has been assumption that if we just give people more things to read, they will be smarter and make better choices. We just need to recognize that consumers have limited ability to make informed choices in the mortgage arena, and in complex matters people may not be the best judge of what's best for them in some instances. I say this with no disrespect to consumers, or with no statement that we want a nanny state.

Our recommendation is that we need to move beyond consumer counseling and expanded disclosure, not that those are unimportant, to how advice is delivered. We don't go to a doctor or lawyer, and they hand you a guidebook of options and tell you to make a choice. In some instances you want people to cut through the complexity and give us some advice. The problem is that consumers falsely think that these mortgage lenders and loan officers are trusted advisors, when in fact they are incentivized sellers of products.

Finally, seniors are in a special situation, with lots of equity and some limited cash. We need to find a workable use of reverse mortgages or other ways to tap that equity, otherwise ten years from now we'll have more problems with people picking off equity from this vulnerable group.

Michael Barr said that he takes it as fact that human beings are not fully rational actors with perfect information and foresight, even though this is the basis for most of our regulations. In the context of saving, we've used behavioral insight to increase retirement saving through "opt-out" 401(k) plans. Just by changing the starting point for consumer action, we've had remarkable progress.

So maybe we could have an opt-out home mortgage system. For example, you apply for a loan and you are automatically signed up for, let's say, a 30-year fixed-rate mortgage with understandable terms in which the APR reveals the true cost of credit. And that will be your mortgage unless you opt out. Now, the market has an incentive to get you to take a higher cost mortgage, so we need to make the system "sticky" by including penalties if

the private sector gets you to take an unreasonable product, or doesn't provide reasonable disclosures.

Questions and Answers

A member of the audience asked about reverse mortgages after the correction in financial markets. Mr. Apgar responded that we don't know what the answers are, there has been some growth in the FHA program but mortgage advertisements still contain the same deceptive concepts. Mr. Barr added that Carl Schultz and others have done work showing that people don't have enough retirement savings if you don't count their housing equity.

Another audience member asked about the recent interest in giving the FHA a larger role, and how the FHA would need to do things differently so as to avoid some of the problems it had in the past. Mr. Apgar responded that the FHA is a "challenged" organization which in past years was sluggish, and recent modernization has not gone far enough to give them the internal capacity to manage the new risks they have been given.

Keynote Speech by Chairman Barney Frank, House Financial Services Committee

Barney Frank began by saying that people fib when they say, "I don't like to say I told you so." Because everybody likes to say "I told you so." And those on the liberal side, who have been advocating for a strong public policy role in working alongside the market, they're entitled to say "I told you so." Representative Frank remembered back to his first month in Congress, in 1981, and he was standing next to Ronald Reagan when Reagan said, "Government is not the answer to our problem; government is the problem." He said that you now see Chairman Bernanke and Secretary Paulson going up and down Wall Street saying, "we are from the government, and we are here to help you."

Representative Frank met on Monday with the leader of one of the financial institutions in this country who said his company might soon stop providing financing for people to buy cars. Representative Frank pointed out that this means they don't make as many cars, and they don't sell as many cars.

Representative Frank said he thinks highly of Mr. Bernanke and Mr. Paulson, and although it's inappropriate in a democracy to have them in this position, they had no choice. He said that Wall Street is referring to Mr. Bernanke as the Loan Arranger and his faithful companion, Paulson. According to Representative Frank, we've reached a point where we need to institutionalize this, and that's what we're doing. But we need to do it well.

The cause is a failure to have government regulation over risky activities, said Representative Frank. He described some experiments that the U.S. has had in regulation. Mortgages are originated by two groups: regulated entities called banks and credit unions and thrifts and the unregulated mortgage companies. If the regulated entities had made mortgage loans, we would not have had this crisis, Frank asserted. He said that AIG's regulated insurance business was very prosperous, but then they got into highly unregulated, exotic instruments, and now they have to sell off the regulated part to

pay off the debts incurred by the un-regulated part. Representative Frank continued with a description of recent events in the financial field, where the more regulated institutions, the commercial banks, are buying up the under-regulated investment banks. Bear Stearns bought out by J.P. Morgan/Chase. Barclays finally bought up much of Lehman, and Bank of America bought up Merrill Lynch and Countrywide. Representative Frank said that some people asked him why he supported BofA buying up Countrywide, and he answered that he'd be for Syria buying up Countrywide. Representative Frank said the push-back has been that people say it's all the fault of the Community Reinvestment Act, which he said was simply untrue. Representative Frank said that the institutions covered by the CRA didn't make the mortgage loans that got us in trouble, although some CRA entities did buy up what shouldn't have been bought, but they weren't the ones who caused this problem.

Representative Frank said that in 1994, the Democratic Congress passed and Bill Clinton signed the Homeowners Equity Protection Act, which told the Federal Reserve to protect people by outlawing certain kinds of mortgages. Alan Greenspan refused to do that, and nothing happened in regulation. Mr. Bernanke has issued regulations that will limit sub-prime mortgages going forward using exactly the authority that Alan Greenspan refused.

Representative Frank said he was surprised to learn that the Federal Reserve has $800 billion, which it earns through its money-making businesses and its management of the economy. And under a 1930 statute, Bernanke can lend that to any entity in American on any terms he sees fit, and take whatever he wants as collateral. It is more power than any individual would have in a democracy. Representative Frank said that Bernanke is not looking to do this, that Bernanke made it very clear he is eager to give this up.

Either we do this in a systematic way, Frank said, or Bernanke will continue to have to do this. Representative Frank enumerated the reasons that he's for the financial rescue package. First, we have to deal with the consequences of these bad decisions. Second, Bernanke could have done it anyway. And three, this gives us a chance to write some social content into it as we did with Fannie and Freddie.

Representative Frank said that Congress will be talking about severance packages, as they did with Fannie Mae and Freddie Mac. He said that we need to change the incentive structure, so that heads of companies make money if a bet pays off, and also if it doesn't pay off they can go home to dinner. Frank then asked a rhetorical question: Some people say that financial leaders will boycott the program if severance packages are included, but are they saying that these financial leaders would not get on board with something that would help their own institutions and the whole country?

Representative Frank said he's also been talking with Senator Dodd about buying up a lot of mortgage paper so that we can reduce the number of foreclosures, both as a social matter for individuals and also for the macroeconomic situation. Between the government running Fannie Mae and Freddie Mac, and the FDIC running IndyMac, he said, we should now be able to substantially reduce foreclosures. This isn't to stop housing prices from dropping, but to change the pace at which it happens.

Representative Frank concluded that it's now necessary for the government to come in and fix things, but he said this can only be done in the context of our promising ourselves that we will not allow it to recur and that this is not just a benefit for Wall Street. People's 401(k)s and mutual funds are at risk. The American people will be the main victims.

Questions and Answers for Barney Frank

Ruth Susswein of Consumer Action asked whether there would be sufficient consequence to the lenders. Representative Frank answered that there has to be a regulator over the investment banks and hedge funds and private equity, to limit risk-taking.

Charles Lowery of the Center for Responsible Lending asked whether the law passed at the end of July is still sufficient. Representative Frank answered that the silver lining in this cloud is that between Fannie Mae and Freddie Mac and this bill, the government will be the owner of a lot of mortgage paper, and will be able to move from the jawboning stage to reducing foreclosures.

A representative from La Raza's National Council asked whether Latino home buyers will be protected from strict rules re credit scores. Representative Frank answered that between 2002 and 2007 FHA originations were cut by two-thirds, and instead people were going to sub-prime deals. But now the FHA is being pumped up and will be able to help people with lower credit scores.

Suzanna Montezemolo of AARP asked whether there would be anything in the new legislation that would weave in a bankruptcy fix that the Senate voted on and rejected earlier this year, that would allow bankruptcy judges to restructure primary mortgage debt. Representative Frank said that Senator Schumer had raised it at a meeting with leadership, and he himself would like to see it. He is skeptical, however, that they have the votes. Also, as mentioned earlier, the government will own many of these mortgage loans and will take maximum advantage of that fact.