PLEADING IN INTERVENTION –

EXHIBIT A

Preliminary Report[1]

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**In the matter of the application of
THE BANK OF NEW YORK MELLON,
(as Trustee under various Pooling and Servicing
Agreements and Indenture Trustee under various
Indentures)**

I. Assignment

We have been asked by Counsel for the homeowner-intervenors to review the Settlement Agreement executed between the Bank of New York Mellon (as Trustee) and the Bank of America,[2] and provide an independent opinion regarding the potential effect of this agreement on homeowners whose loans are serviced by Bank of America.

II. Summary of Report

Homeowners whose mortgage loans are serviced by Bank of America[3] will be harmed by the settlement. The Settlement Agreement, if allowed to proceed, will speed up foreclosures, perpetuate existing servicing abuses in the system, and undermine federal programs designed to stabilize the housing market. The touted servicing "improvements" aim to increase the speed of foreclosures but fail to set standards to protect homeowners from wrongful or unnecessary foreclosure or abusive servicing. Investors will also be harmed by the Settlement Agreement, as there is a dearth of specific requirements ensuring that the servicing of defaulted loans maximize income to the owners of those loans.

A. The Settlement Agreement does nothing to end existing well known and obvious abuses by servicers such as their profiteering from defaulted loans, the continued use of dual tracks for homeowners striving for loan modifications while facing foreclosure, and the failure to employ loss mitigation strategies that save homes and return more income to the investors than foreclosures.

B. The Settlement Agreement undermines existing efforts to stabilize the housing markets because it is in conflict with the standards articulated by both the U.S. Treasury

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[1] Once more details are available about some of the terms of the settlement, we may have additional opinions.

[2] *See,* Exhibit B to Verified Petition, Bank of New York Mellon, June 29, 2011 (hereinafter referred to as "Settlement Agreement").

[3] The Settlement Agreement, by its terms, covers loans included in the listed trusts that are serviced by Bank of America Corporation ("BAC") and BAC Home Loans Servicing, LP ("BAC HLS"), which are collectively referred to as "Bank of America." We also employ this convention and references to Bank of America are intended to include the Bank itself, as well as the relevant servicing subsidiary or affiliate. Also covered in the Settlement Agreement, and in our discussion of Master Servicers, are the Countrywide parties.

Department's Home Affordable Modification Program ("HAMP") and the new Servicer Alignment Initiative governing the activities of the two government enterprises, Fannie Mae and Freddie Mac.

C. The servicing "improvements" likely will speed foreclosures without protecting homeowners:

1. The planned referral of defaulted loans to specialty subservicers whose portfolio will be limited to 30,000 loans includes no assurances that homeowners will be protected from illegal and abusive servicing and inappropriate foreclosures. Similarly, the guidelines governing the subservicers do not require a decision process that even ensures that investors' interests are primary.

2. The compensatory fee structure applicable to defaulted loans still held by Bank of America will radically speed up foreclosures without ensuring that either homeowners are protected from wrongful foreclosure or that investors' economic interests are primary.

III. Qualifications

Margot Freeman Saunders

Currently Of Counsel to the National Consumer Law Center ("NCLC"), Margot Freeman Saunders has worked for NCLC since 1991. Until 2005, she served as Managing Attorney of NCLC's Washington, D.C. office.

One of her principal duties at NCLC is to serve as a resource to legal services attorneys and attorneys engaged in private practice, as well as federal and state regulators on complex consumer law cases. Her job includes policy analysis in the areas of predatory lending, credit reporting, debt collection, electronic commerce and electronic benefits transfer, preservation of homeownership, and other consumer credit issues.

During the past twenty years she has regularly provided testimony to the House Financial Services Committee and the Senate Banking and Housing Committee (in addition to other congressional committees) regarding credit-related issues facing low-income households in America. Her responsibilities have required frequent appearances before, and meetings with, federal regulators. She has testified on numerous occasions before Congress on the meaning of, the causes for, and recommended solutions to predatory mortgage lending.

She has prepared and presented testimony on dozens of occasions to congressional committees. In just the past few years, she has testified before Congress six times. In July, 2011, she testified before the Consumer Credit Subcommittee of the House Financial Services Committee about a bill regulating rent to own contracts. On April 23, 2009, she testified before the full House Financial Services Committee on behalf of over fifty state and national groups representing consumers regarding pending legislation to address predatory mortgage lending. On March 11, 2009, she presented testimony to a subcommittee of the House Financial Services Committee on recommended reforms to the system of mortgage regulation. In September, 2008, she testified to the same House Committee on HUD's proposed changes to the Real Estate Settlement Services Act. In the previous year, she testified before both the House Ways and Means Committee and the Senate Finance Committee on the effect on the elderly of garnishing Social Security and other exempt benefits. She regularly provides substantial input to the testimony of other staff at NCLC, just as in her own policy work she is counseled and guided by the other consumer law experts at the Center.

Ms. Saunders has served on the Board of Advisors of the University of North Carolina School of Law Center for Banking and Finance since 2002. She was a member of the Federal Reserve Board's Consumer Advisory Council from 1996 to 1998, where she was Co-Chair of Consumer Credit Committee and Chair of Depository Institutions Committee.

Ms. Saunders' work includes writing analytical books and articles on issues relating to low-income consumers; providing training and expert testimony on issues affecting low income consumers; and providing analysis and assistance on credit math questions. She has authored or co-authored numerous articles in law reviews and other publications on consumer law, including, for example *The Credit Card Market and Regulation: In Need of Repair*, 10 N.C. Banking Inst. 23, University of North Carolina School of Law Banking Institute, 2006; and *Regulation of Consumer Credit: The Cause or the Cure for Predatory Lending?* Joint Center for Housing Studies, Harvard University, BABC, March 2004.

She is co-author of several of NCLC's practice treatises, including all editions of *Banking and Payments Law* (4th Ed. 2009) and Supplements, 2006, 2007, 2008, 2010, 2011 and the original and second editions of *Access to Utility Service*, (2nd Ed. 2000). She has been a contributing author to other NCLC manuals, including *The Cost of Credit: Regulation and Legal Challenges* (2004, 2005 Supplements) and the 2006, 2007, and 2009 Supplements to *Foreclosures – Defenses, Workouts, and Mortgage Servicing* (1st Ed. 2005).

Ms. Saunders received her undergraduate degree from Brandeis and her law degree from the University of North Carolina. She is a licensed attorney in the state of North Carolina.

<u>Diane E. Thompson</u>

Ms. Thompson has been Of Counsel to the National Consumer Law Center since 2006. Since joining NCLC, she has led the nation's advocates in analysis and critical suggestions on how to improve servicing standards affecting low income consumers. She has testified on loan modifications and servicing matters before the full Senate Banking Committee twice and once before the Housing Subcommittee of the Senate Banking Committee

Ms. Thompson is a the co-author of NCLC's *Truth In Lending* (7th ed. 2010) and a contributing author to the NCLC practices treatises, *The Cost of Credit: Regulation and Legal Challenges* (4th ed. 2009 and 2010 and 2011 Supplements), *Foreclosures: Defenses, Workouts, and Mortgage Servicing* (4th ed. 2009), *Foreclosure Prevention Counseling: Preserving the American Dream* (2d ed. 2009), and *Stop Predatory Lending* (2nd ed. 2007). She is the author of *Foreclosing Modifications: How Servicer Incentives Discourage Loan Modifications,* Wash. L. Rev. (forthcoming 2011) and the co-author of *The Truth, the Whole Truth, and Nothing But the Truth,* 25 Yale Journal on Regulation 181 (2008) and of *Installment Contracts in* <u>Residential Real Estate,</u> Illinois Institute for Continuing Legal Education (2003). Ms. Thompson has helped write NCLC's comments on numerous regulatory initiatives relating to mortgage lending and specifically regulations proposed under the Truth in Lending Act and the Real Estate Settlement Procedures Act.

Ms. Thompson regularly serves as a resource to Congressional staffers on issues relating to mortgage servicing, predatory mortgage lending, as well as technical issues relating to the federal statutes governing mortgages. She served on the Federal Reserve Board's Consumer Advisory Council from 2003-2005 and meets with federal regulatory agencies, including the Federal Reserve Board, the Federal Deposit Insurance Corporation, and the Department of Housing and Urban Development, to discuss matters relating to predatory lending and mortgage servicing.

Much of Ms. Thompson's time is spent providing training and support to attorneys and housing counselors on matters relating to loan modifications and HAMP. Since HAMP was rolled out in 2009, Ms. Thompson has trained thousands of attorneys, housing counselors, and mediators in the details of its structure, through in-person trainings in Colorado, Florida, Illinois, Indiana, Kentucky, Maine, Massachusetts, Michigan, Nevada, New York, North Carolina, Vermont, Washington State, West Virginia, as well as via webinars and teleconferences.

Ms. Thompson worked from 1994 to 2007 at the East St. Louis office of Land of Lincoln Legal Assistance Foundation, where she was the Supervising Attorney of the Housing and Consumer Unit and served as the Homeownership Specialist, providing backup and support to attorneys representing low-income homeowners in 65 counties in downstate Illinois. During this time, Ms. Thompson represented hundreds of homeowners and frequently litigated home mortgage cases.

Ms. Thompson received her bachelor's degree from Cornell University and her law degree from NYU. She is a licensed attorney in the state of Illinois.

IV. Findings

This case arises because of the relentless problems that Bank of America has experienced with its servicing. As the Petition states:

> 6. A substantial dispute has arisen concerning the Sellers' alleged breaches of representations and warranties in the Governing Agreements, and the Master Servicer's alleged violations of prudent servicing obligations.[4]

The Petition further alleges that the servicing improvements contained in the Settlement Agreement executed by the parties on June 28, 2011 will resolve those problems, thereby protecting the investors:

> 11. The Settlement Agreement is attached to the Petition as Exhibit B. It will be described more fully in paragraphs 37-47 below, but, in short, it requires Bank of America and/or Countrywide to pay $8.5 billion ("Settlement Payment") into the Trusts, allocated pursuant to an agreed-upon methodology that accounts for past and expected future losses associated with the Mortgage Loans in each Trust. It also

[4] Verified Petition, Bank of New York Mellon, June 29, 2011, (hereinafter referred to as "Petition") ¶ 6.

> requires BAC HLS to implement, among other things, servicing improvements that are intended to provide for servicing performance by BAC HLS that is at or above industry standards and will provide a mechanism for BAC HLS to transfer high-risk loans to subservicers for more individualized attention.[5] (Emphasis added).

We disagree with this analysis. As we explain in Part A, our first finding is that the servicing improvements incorporated in the Settlement Agreement will do nothing to end well known and obvious abuses by Bank of America.

Further, as set out in Part B, we find that the "servicing improvements" in the Settlement Agreement will seriously undermine existing efforts to stabilize the housing markets because of conflicts with the clearer and better standards articulated by both the U.S. Treasury Department's Home Affordable Modification Program ("HAMP") and the new Servicer Alignment Initiative governing the activities of the two government enterprises: Fannie Mae and Freddie Mac. As a result, homeowners will be seriously harmed.

Finally, as explained in Part C, the servicing "improvements," requiring referral of defaulted loans to subservicers, contain no assurances that homeowners will be protected from illegal and abusive servicing and inappropriate foreclosures. The investors are not protected in the decision-making analysis dictated for the subservicers, and homeowners' interests are not even mentioned. Further, the compensatory fee structure applicable to defaulted loans still held by Bank of America will radically speed up foreclosures without ensuring that homeowners are protected from wrongful foreclosure or even that investors' economic interests are evaluated.

A. The Settlement Agreement Does Nothing to Address Identified Problems in Mortgage Servicing

As has been widely recognized, when servicers wrongfully foreclose, or fail to modify, or undermine the judicial process and imperil the legality of a foreclosure, homeowners, investors, and the American public at large all lose.[6] The foreclosure rate is now more than three times what it was in 1933, at the height of the Great Depression.[7] The crisis has impacted every part of our country and most of the world. Losses to individual families who lose their home due to foreclosure are

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[5] Petition, ¶ 11.

[6] *See, e.g.,* Ben S. Bernanke, Chairman, Bd. of Governors of the Fed. Reserve Sys., Speech at the Fed. Reserve Sys. Conference on Housing and Mortgage Markets: Housing, Mortgage Markets, and Foreclosures (Dec. 4, 2008), *available at* http://www.federalreserve.gov/newsevents/speech/bernanke20081204a.htm ("Despite good-faith efforts by both the private and public sectors, the foreclosure rate remains too high, with adverse consequences for both those directly involved and for the broader economy.").

[7] The U.S. foreclosure rate (measured as a percentage of outstanding mortgage loans in foreclosure) at the end of the second quarter of 2011 was 4.43%. Mortgage Banker's Ass'n, National Delinquency Survey Q2 2011, at 3. The foreclosure rate for non-farm mortgages peaked in 1933, below 1.4%. David C. Wheelock, *The Federal Response to Home Mortgage Distress: Lessons from the Great Depression*, 90 Federal Reserve Bank of St. Louis Rev. 133, 138–39 (2008).

projected to exceed $2.6 trillion,[8] with spillover effects on neighbors and communities in the trillions of dollars.[9]

The Settlement Agreement proposes "servicing improvements" of mortgage loans owned by the institutional trusts. In order to assess the improvements, we first identify the existing problems that must be addressed. Among the many abuses in the servicing industry several specific problems stand out: failure to evaluate homeowners for a loan modification in a timely way; proceeding with foreclosures and loan modifications simultaneously (on a "dual track"); and imposition of illegal fees and improper accounting for payments.

1. Delay and Deny.

There is a serious problem of servicers delaying processing loan modification applications long past any reasonable time frames. For example, the average length of time homeowners spend seeking a HAMP loan modification is 14 months.[10] Documents are lost; additional grounds for denial are advanced; prior agreements are disclaimed. Practitioners across the country report many instances of submitting the same documents multiple times, often as many as six or seven different times. Getting to a final modification remains difficult for homeowners and, even once achieved, is no panacea.

Delay and deny remains many servicers' standard response to loan modification. During delay, fees and interest accrue. These fees and interest can quickly mount up. These fees will ultimately be paid to the servicer, either by the homeowner or from the proceeds of a foreclosure sale. If, ultimately, the loan is modified, and the fees are capitalized, the servicer's monthly servicing fee will increase since it is calculated as a percentage of the outstanding principal.

The Settlement Agreement does mandate that servicers complete their evaluation of the homeowners' eligibility for all relevant loan modification programs within sixty days of receiving the homeowner's paperwork. However, in violation of industry standards, there are no mandates on

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[8] Staff of the Joint Economic Comm., 110th Cong., 2d Sess., State by State Figures: Foreclosure and Housing Wealth Losses (2008), *available at* http://jec.senate.gov/index.cfm?FuseAction=Reports.Reports&ContentRecord_id=392cb915-9c45-fa0d-5a46-f61f6e619381&Region_id=&Issue_id=.

[9] *See, e.g.,* Ctr. for Responsible Lending, Soaring Spillover: Accelerating Foreclosures to Cost Neighbors $502 Billion in 2009 Alone; 69.5 Million Homes Lose $7,200 on Average (2009), *available at* http://www.responsiblelending.org/mortgage-lending/research-analysis/soaring-spillover-accelerating-foreclosures-to-cost-neighbors-436-billion-in-2009-alone-73-4-million-homes-lose-5-900-on-average.html (estimating losses to neighboring property values due to the foreclosure crisis at $1.86 trillion dollars); Staff of the Joint Economic Comm., 110th Cong., 1st Sess., The Subprime Lending Crisis: The Economic Impact on Wealth, Property Values and Tax Revenues, and How We Got Here (2007), *available at* http://jec.senate.gov/index.cfm?FuseAction=Reports.Reports&ContentRecord_id=c6627bb2-7e9c-9af9-7ac7-32b94d398d27&Region_id=&Issue_id= (projecting foreclosed home owners will lose $71 billion due to foreclosure crisis, neighbors will lose $32 billion, and state and local governments will lose $917 million in property tax revenue); William Apgar & Mark Duda, Collateral Damage: The Municipal Impact of Today's Mortgage Foreclosure Boom, at 4 (May 11, 2005), *available at* www.hpfonline.org/PDF/Apgar-Duda_Study_Final.pdf (estimating costs to the City of Chicago per foreclosure upwards of $30,000 for some vacant properties).

[10] *See* Paul Kiel & Olga Pierce, *Homeowner Questionnaire Shows Banks Violating Program Rules*, ProPublica, Aug. 16, 2010, http://www.propublica.org/article/homeowner-questionnaire-shows-banks-violating-govt-program-rules.

either the servicers or the subservicers to make sure that the homeowners have received their necessary packets to be able to provide the servicer with the required information.[11] Worse, the standards are completely open-ended, allowing servicers to request any document. Nor are any checks in place to make sure that documents received are not lost.

The Agreement also places strong incentives on the servicers to speed up the process of foreclosure.[12] This push to foreclosures undermines and hampers real consideration for home retention alternatives.

2. Dual Track.

One of the most frustrating problems facing homeowners attempting to obtain loan modifications has been the dual track system used by so many servicers. Reports of servicers conducting foreclosure sales while a consumer is making payments under a loan modification are widespread. Once a foreclosure is initiated, even high-level bank officials may not be able to stop it. Homeowners who are routinely assured that they will be receiving a loan modification by one department may nonetheless find themselves facing a foreclosure.

In part because loan modifications often require more deviations from the norm, loan modifications often take more time to work out than foreclosures do. But the two-track system pushes the foreclosure forward regardless, with the result that foreclosures frequently occur while homeowners are negotiating a loan modification, sometimes even after they have been approved for a loan modification, with sometimes devastating results, as these examples illustrate:

- Bank of America misapplied a California homeowner's payments under a repayment agreement and required her to enter into a new modification and capitalize the arrears to catch up on the repayment agreement (which she had, in fact, already completed). After the woman began sending payments that included her regular monthly payment and the improperly capitalized amounts, Bank of America rescinded the offer of a modification and initiated foreclosure proceedings, despite representations from high level bank employees to the homeowner's attorney that they would honor the modification.[13]

- One New York homeowner accepted a proprietary permanent modification with Bank of America in January 2010, and made all required payments under it for 17 months, when, in June 2011, Bank of America refused to accept the payment and asserted the loan was in foreclosure. Bank of America has denied the existence of any modification agreement.[14]

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[11] The Federal Housing Finance Agency's new servicing guidelines include repeated and strict requirements obligating the servicer to affirmatively contact the borrower and ensure that the borrower has received all of the required materials. These requirements are quite specific. *E.g.,* Freddie Mac Bulletin: Number 2011-11, June 30, 2011; Freddie Mac, *Borrower Contact – Freddie Mac Requirements Under the Servicing Alignment Initiative,* Publication Number 889, June 30, 2011, *available at* http://www.freddiemac.com/service/factsheets/pdf/borrower_contact_factsheet_889.pdf.

[12] For example, the Settlement Agreement charges the Master Servicer's substantial compensatory fees for failing to move to foreclosure on a strict timeline without the exceptions for variance available in industry standards. Settlement Agreement ¶ 5(c).

[13] Glantz v. BAC Home Loans Servicing, No. CCC-11-512115 (San Francisco County).

[14] Personal communication with Shabnam Faruki , Staten Island Legal Services regarding Stephen Harris.

- In a loan originally serviced by Countrywide and then transferred to BAC, the servicer failed to process the Wisconsin homeowner's loan modification requests for over ten months, refused payments, and initiated a foreclosure. Due to Bank of America's delay in this case, the homeowner is no longer eligible for loan modifications under the FHA-HAMP program, which has a twelve-month cap on delinquency.[15]

- In one unusual case in West Virginia, a foreclosure trustee refused to proceed with a sale and referred the homeowners to legal counsel when Bank of America attempted to foreclose on homeowners while they were under review for a loan modification.[16]

Yet, not only does the Settlement Agreement not prohibit dual track, it appears to mandate it. By requiring that the homeowner's eligibility for all applicable "loan modification programs" be evaluated simultaneously,[17] and insisting that servicers speed to foreclosure, dual track is virtually guaranteed.

3. Costs of Foreclosure and Fees.

Even if a foreclosure never happens, the cost of a loan modification increases as the servicer imposes various foreclosure-related (and often improper) fees on the homeowner,[18] and the homeowner suffers the financial, credit, and emotional toll of defending a foreclosure. These fees are lucrative to the servicer, but can price a modification out of a homeowner's reach.[19] The two-track system was instituted to encourage servicers to minimize delay, but it does not in the current market serve investors' interests well, since it does not reduce the costs skimmed by the servicer from the foreclosure sale.

Servicers have substantial incentives to impose significant fees on homeowners because they are usually permitted under the pooling and servicing agreements to retain all of those fees. Force-

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[15] Countrywide v. Andrew Akhahon, No. no 2009-CV-005321 (Milwaukee Co., Wis.).

[16] Kelford v. Bank of America N.A., Civil Action No. 11-C-46 (Braxton Co. W. Va.). The sale has been postponed pending the outcome of litigation.

[17] Settlement Agreement, ¶ 5(d).

[18] *See* Katherine Porter, *Misbehavior and Mistake in Bankruptcy Mortgage Claims,* 87 Tex. L. Rev. 121, 144-68 (2008) (reporting that servicers appear to be imposing often improper default-related fees on borrowers in bankruptcy proceedings).

[19] As fees rise, they are added to the principal balance that must be repaid. The result often is that homeowners can no longer afford the monthly payment necessary to repay the loan. Additionally, servicers sometimes demand payment of these fees upfront, which request becomes impossible to satisfy as the fees mount into the thousands of dollars. Finally, many modification programs put a limit on how far in arrears a homeowner may be, including the capitalized fees. *See, e.g., Problems in Mortgage Servicing From Modification to Foreclosure, Part II: Hearing Before the S. Comm. on Banking, Housing,& Urban Affairs*, 111th Cong. 8 (2010) (statement of Donald Bisenius, Executive Vice President, Freddie Mac) (noting that it is harder to bring a borrower current the more delinquent the borrower is). *Cf.* Hassan Shamji & Bulat Mustafin, *Measure of Modifications: A Look Across Servicers,* Moody's Resi Landscape 11, 12 (Feb. 1, 2011)(noting that capitalization of fees can doom a modification to re-default).

placed insurance in particular is often a locus of abuse.[20] There are multiple examples of force-placed insurance leading to foreclosure reported around the country.[21]

The imposition of these illegal fees is compounded by failure to account for or apply homeowners' payments correctly. These failures are routine and sometimes result in current homeowners being placed in foreclosure.

The cause may be a technical error, or a mistake by the servicer, but if the homeowner is pushed into default, denied a loan modification, or induced not to make payments in reliance on a loan modification, the result is the same: a wrongful foreclosure, at incalculable cost to the homeowners and likely loss to the investors.

There are no limits on the fees that servicers can charge homeowners for third party vendor services in the Settlement Agreement. In fact, the Agreement explicitly condones these charges and ensures that servicers can continue to impose them.[22] Likewise there are no requirements for waivers of late fees, which can make a significant difference in creating an affordable loan modification. Worse, the transfer of servicing to subservicers without sufficient oversight may actually increase accounting problems.

4. Abuses Ignored in Settlement Agreement.

Presumably the investors whose interests are represented by the Trustee in the instant action are familiar with the litany of servicing abuses.[23] The investors represented by the Trustee should also be cognizant of some of the industry standards (as is evidenced by the Settlement Agreement's mention of HAMP, required consideration of NPV analyses, allowance of principal reductions in unspecified circumstances, and incentives to decrease time between default and foreclosure). However, the Settlement Agreement is completely lacking in the necessary specificity to govern the future servicing of the trusts' loans which will address the well-documented abuses in the industry.

The standards enunciated for the evaluation of loan modifications and loss mitigation generally by both servicers and subservicers in paragraph 5(e) leave the servicers with virtually unlimited discretion, far more discretion than servicers are currently permitted to exercise under most federal loss mitigation programs. While servicers are required to consider a net present value analysis of a loan modification as compared to foreclosure (paragraph 5(e)), this required consideration is virtually meaningless for the following reasons:

- No standards for the modification are offered (e.g., interest rate reduction, extended terms, principal reductions, income ratios) nor are the terms of the NPV analysis (e.g., expected re-

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20 *See, e.g.,* Jeff Horwitz, Ties to Insurers Could Land Mortgage Servicers in More Trouble: Force-Placed Polices Impose Costs on Both Homeowner, Investor, Am. Banker, Nov. 10, 2010.

21 *See, e.g.,* Kate Berry, *Pipeline: A Roundup of Credit Market News and Views*, Am. Banker, Nov. 11, 2010 (citing research by Amherst securities) (reporting on a Florida case) .

22 Settlement Agreement ¶ 5(a)(iv) and (a)(xi).

23 The Petition indicates that the parties to it are "some of the world's largest and most sophisticated investors." Petition, ¶ 7.

default rate, REO discount, expected time-to-sale) specified. As such these standards appear to be left entirely to the discretion of the servicers (or subservicers) conducting the analysis.

- Servicers are only required to "consider" the NPV analysis. They are not required to use its results.
- Among the other criteria servicers and subservicers are permitted to consider is their subjective belief that the homeowner is engaged in "strategic default."
- Servicers may refuse to perform a loan modification, even one that is projected to return a benefit to the investor, for any reason the servicer deems "prudent" in its judgment.

Similarly, the servicers are permitted to continue to accrue post-default fees, directly and through third-party vendors, without limitation or oversight.[24] These fees often provide an incentive to servicers to pursue foreclosure over modification.

The Settlement Agreement leaves Bank of America and its subservicers to continue business as usual with regard to excessive and illegal fees, improper accounting, and failure to evaluate homeowners for loss mitigation. It perpetuates and exacerbates the dual track system of simultaneous foreclosures and loan modifications.

The Settlement Agreement not only fails to address the well-recognized servicing problems; it outlines a methodology for servicing defaulted home loans which represents a significant retreat from current industry standards. This retreat means that, for those loans serviced under the Settlement Agreement, more homes will be lost to foreclosure and investors' interests will not be maximized in the servicing process.

B. The "Servicing Improvements" Required by the Settlement Agreement Significantly Undermine Existing Industry Standards – Hurting Homeowners.

The "servicing improvements" contemplated in the Settlement Agreement primarily consist of two prongs: expedited referral to subservicers for default servicing and expedited foreclosure processing. The few details that are provided about implementation of servicing standards are in conflict with the current industry standards embodied in government loan modification programs and the loan modification protocols adopted by the GSEs.

Current industry standards are defined by the requirements imposed on all servicers who have agreed to comply with the terms of the Treasury Department's Home Affordable Modification Program ("HAMP")[25] and Home Affordable Foreclosure Avoidance ("HAFA").[26] Bank of America

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[24] Settlement Agreement, ¶ 5(a)(iv) and (a)(xi).

[25] The Home Affordable Modification Program (HAMP) is designed to help financially struggling homeowners avoid foreclosure by modifying loans to a level that is affordable for borrowers now and sustainable over the long term. The program provides detailed loan modification guidelines that are used by most servicers. *See, e.g.* Administrative Website for Servicers, HAMP, administered by Fannie Mae, https://www.hmpadmin.com/portal/programs/hamp.jsp.

[26] Home Affordable Foreclosure Alternatives (HAFA) is designed to mitigate the impact of foreclosures on borrowers who are eligible for a loan modification under the Home Affordable Modification Program (HAMP), but either chose not to pursue a HAMP modification, did not qualify for one, or failed to make their payments in a HAMP modification. *See, e.g.* Home Affordable Foreclosure Alternatives (HAFA), https://www.efanniemae.com/sf/servicing/hafa/.

has agreed to comply with HAMP's requirements in its servicing of loans, subject to investor restrictions. In doing so, Bank of America has also agreed to participate in HAFA. HAMP governs loan modifications. HAFA provides that servicers must offer HAMP-eligible homeowners who do not qualify for HAMP, who decline HAMP, or who fail a HAMP modification, the opportunity for a deed-in-lieu or short sale. By statute and determination of the U.S. Treasury, these standards are industry standards.[27]

Additionally, the standards of the mortgage industry have long been informed by the nation's two largest investors in home loans—the government sponsored enterprises, or GSEs: Fannie Mae and Freddie Mac. The government regulator of the GSEs, the Federal Housing Finance Agency, recently issued an updated framework to align the default servicing of both GSEs to improve quality, ensure home retention is maximized, and protect taxpayers.[28] This servicing alignment articulates industry standards for loan servicing once it is fully implemented, which is expected to be in the fall of 2011.[29] The Servicing Alignment will accomplish its dual goals of preserving homeownership and protecting investor (taxpayers) returns using a) clear guidelines, b) incentive payments to servicers, and c) penalties against servicers for determined failures.
Although the FHFA guidelines will not directly apply to the loans covered by the Settlement Agreement, the FHFA guidelines are relevant to the analysis of the value of the requirements in the Agreement. The FHFA guidelines establish a floor for the industry standards, which is sometimes raised by HAMP. The Settlement Agreement purports to match or raise industry standards. Relaxation of industry standards should not be permitted.

We have publically criticized the current servicing regime under HAMP, the GSEs' standards, the proprietary servicing programs, the federal banking agencies' enforcement efforts, and even the new Servicing Alignment. Indeed, we do believe that the existing regulatory regime governing servicers has failed to protect homeowners from servicing abuses, and failed to ensure even that investors' income is maximized from defaulted home loans, and thereby has significantly contributed to the devastation of so many of our neighborhoods.

However, although imperfect, and inadequately enforced, both the HAMP guidelines and the new Servicing Alignment articulate goals for improving home retention and protecting homeowners' interests. Both HAMP and the FHFA's Servicing Alignment establish clear rules, with intuitive and logical instructions and incentives, reporting requirements and measurable outcomes, all designed to preserve homeownership and the assets of homeowners, while protecting the interests of investors.

In contrast, the differences between the Settlement Agreement and the specific requirements applied both by HAMP and the FHFA standards are considerable. In some regards, the Settlement Agreement is simply too vague—not requiring sufficiently rigorous actions to ensure compliance. In

[27] *See, e.g.,* 15 U.S.C. § 1639a (Pub. L. No. 111-22, div. A, tit. II, § 201(b) (May 20, 2009); Making Home Affordable[SM] Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at 18 (2011) ("MHA reflects usual and customary industry standards for mortgage loan modifications, short sales and DILs contained in typical servicing agreements, including pooling and servicing agreements (PSAs) governing private label securitizations.").

[28] Federal Housing Finance Agency News Release, "*Fannie Mae and Freddie Mac to Align Guidelines for Servicing Delinquent Mortgages,*" April 28, 2011. Available at http://www.fhfa.gov/webfiles/21190/SAI42811Final.pdf.

[29] Federal Housing Finance Agency News Release, "*Fannie Mae and Freddie Mac to Align Guidelines for Servicing Delinquent Mortgages,*" April 28, 2011. Available at http://www.fhfa.gov/webfiles/21190/SAI42811Final.pdf.

other, much more problematic, instances, the Settlement Agreement rewards or incentivizes activity that is adverse to either the explicit goals or the explicit directions imposed on servicers by HAMP or FHFA. While providing strong incentives to speed up foreclosures, the Agreement completely fails to meet the following basic standards:

- Ensure that homeowners are treated fairly;
- Mandate that the foreclosure will inure to the benefit of the investors, rather than just the servicer; and
- Eliminate the incentives that encourage problematic behavior by servicers of defaulted home mortgages.

The effect of the Settlement Agreement's mandates and system of incentives on the servicing of defaulted loans will be detrimental to homeowners: fewer homes will be preserved from loss.

The dangerous disconnect between the Settlement Agreement and industry standards starts at the top. The FHFA servicing alignment, for example, has as its express goals to reduce foreclosures and avoid home loss while increasing investor income from defaulted mortgage loans.[30] In contrast, the Settlement Agreement does not even mention any intention of either serving the needs of homeowners or ensuring that home retention is achieved whenever possible. While paragraphs 5(d) and (e) set out vague and inconsistent requirements for consideration of loss mitigation strategies, there is no stated goal either in those paragraphs—or anywhere else in the documents—to promote home retention where practicable.

A comparison between the specific rules in the Settlement Agreement and the Treasury Department rules governing treatment of defaulted home loans[31] shows considerable differences. In the following specific provisions, the Settlement Agreement is in direct conflict with both HAMP and HAFA standards. The provisions also conflict with the FHFA's explicit directions in the Servicing Alignment:

- The requirement in paragraph 5(d) that servicers "simultaneously evaluate the borrower's eligibility for all applicable modification programs;"
- The requirement in paragraph 5(d) that servicers "shall render a decision within sixty (60) days of receiving all requested documents from the borrower;"
- The factors listed in paragraph 5(e) that servicers are required to consider before offering a qualifying homeowner a loan modification; and
- The limitations on principal reductions contained in paragraph 5(e).

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[30] Federal Housing Finance Agency News Release, "*Fannie Mae and Freddie Mac to Align Guidelines for Servicing Delinquent Mortgages,"* April 28, 2011. Available at http://www.fhfa.gov/webfiles/21190/SAI42811Final.pdf.

[31] The rules governing HAMP and HAFA are promulgated by the U.S. Department of Treasury in a Handbook available on the program's website. https://www.hmpadmin.com. Making Home Affordable[SM] Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at 18 (2011) ("MHA reflects usual and customary industry standards for mortgage loan modifications, short sales and DILs contained in typical servicing agreements, including pooling and servicing agreements (PSAs) governing private label securitizations.").

In addition, the compensatory fee structure, discussed in section C-2 of this Report, undermines the prescriptions of both HAMP and the FHFA about when loans may be referred to foreclosure and when loans can be sold.

All of these conflicting provisions are particularly problematic because HAMP allows servicers to decline to perform a modification if doing so conflicts with investor restrictions.[32] The net impact of these conflicts is to impair significantly homeowners' access to HAMP modifications.

1. Simultaneous Evaluation

The HAMP and HAFA guidelines specify that homeowners should first be considered for HAMP, then evaluated for proprietary modifications, and only after those options are both rejected, evaluated for a short sale or deed-in-lieu under HAFA.[33] The FHFA Servicing Alignment includes a specific order in which the servicer is required to evaluate different loss mitigation strategies:

> A homeowner's eligibility for workout options will be considered in the following order:
> - Reinstatement
> - Repayment Plan
> - Forbearance
> - HAMP
> - Freddie Mac modifications
> - Home Affordable Foreclosure Alternatives (HAFA) Short Sale
> - Freddie Mac Short Sale
> - HAFA Deed-in-Lieu
> - Freddie Mac Deed-in-Lieu[34]

Both the HAMP/ HAFA rules and the FHFA rules prevent abuse of homeowners and help maximize investor returns by ensuring that homeowners eligible for the most positive outcomes are not steered to results that may provide higher returns for the servicer. The sequential evaluation process limits servicers' ability to skip over a HAMP loan modification or a short sale to a proprietary modification or a deed-in-lieu, for example. The Settlement Agreement, which requires simultaneous consideration of a homeowner for the full range of modifications available,[35] undermines this important consumer protection.

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[32] Making Home Affordable^{SM} Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at 18 (2011).

[33] Making Home Affordable^{SM} Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at 115 (setting out the sequence in the HAFA context), 163 (describing the requirements upon completion of an unemployment forbearance) (2011).

[34] Servicing Alignment Initiative: Loan Modification and Workout Processes, May 25, 2011, *available at* http://www.freddiemac.com/singlefamily/news/2011/0525_sai.html.

[35] Settlement Agreement, ¶ 5(d).

The requirement for simultaneous evaluation of all modification programs is particularly pernicious to homeowners given the widespread problems reported involving servicers steering homeowners to less desirable proprietary modifications. Many advocates for homeowners have reported that Bank of America and its affiliates routinely refuse standard HAMP forms, in violation of the HAMP rules.[36] Bank of America's insistence that homeowners use its forms may result in homeowners being improperly steered to proprietary modifications without HAMP evaluations. Requiring the simultaneous evaluation of homeowners for proprietary and HAMP modifications, along with other modification options, will only worsen this problem.

2. Time Within Which to Render a Decision

HAMP requires that a decision be made within 30 days of the receipt of the homeowners' packet[37] and limits the documents that may be requested.[38] Both standards are critical to limit servicer abuse and ensure that modifications are promptly processed. Yet paragraph 5(d) the Settlement Agreement permits servicers to extend this time to 60 days. This extension is not in compliance with HAMP nor is the carte blanche granted servicers to request any and all documents from homeowners. These different standards undermine the important limitations in HAMP.

3. Factors Determining Eligibility for Loan Modification

In the HAMP NPV analysis, the potential income from a foreclosure is measured against the potential income from a loan modification with affordable loan terms. A positive NPV means that the investor is forecast to make more money from an affordable loan modification than it would from foreclosure. So, by definition, the investors' interests are protected in the NPV test. Homeowners' interests are also more protected because the affordable loan modification allows them to stay in their homes with sustainable mortgages.

The critical issue in the determination of eligibility for a loan modification is what factors are used to measure whether the loan is affordable (for example, what percentage of income to be spent on the mortgage loan is considered affordable), and what ways the loan terms can be changed to make the payments affordable (for example, reducing the interest rate, extending the term, and reducing the principal owed on the loan). HAMP describes with considerable particularity all of these factors and also prescribes the order in which the various factors are applied to construct an affordable and sustainable modification.

One component of the initial eligibility screen under HAMP is the requirement that the current mortgage payment exceed 31% of the homeowner's gross monthly income.[39] This provides an objective measure as to the affordability of the loan and provides, when coupled with income verification, a more effective and transparent guard against the possibility of "strategic default" than

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[36] Making Home Affordable℠ Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at 60 (2011) ("When provided by or on behalf of the borrower, the RMA form must be accepted by servicers in lieu of any servicer-specific form(s).").

[37] Making Home Affordable℠ Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at 70 (2011).

[38] Making Home Affordable℠ Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at 65 (2011).

[39] Making Home Affordable℠ Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at 46-47 (2011).

the blanket consideration of ability to pay in the Settlement Agreement.[40] The broad language in the Settlement Agreement invites a wide-ranging and open-ended exploration of the homeowners' circumstances, which is likely to be intrusive to the homeowner and provide the servicer with arbitrary grounds for disqualifying homeowners from loan modifications.

If the homeowner passes the initial HAMP eligibility test, the servicer must proceed to verify income and process the potential modification through the waterfall analysis. Under the standard, sequential analysis, once initial eligibility is determined, homeowners must then be screened to determine if they "qualify" for a HAMP modification. Aside from income verification, the key piece of this analysis is constructing an affordable modification according to a standard protocol, by capitalizing arrears, reducing the interest rate, extending the term, and providing principal forbearance until an affordable payment of 31% of the homeowner's income is reached. Once a modification providing an affordable payment has been constructed, servicers must then run it through the Net Present Value test to determine if investors would benefit from the modification as opposed to doing nothing or proceeding with the foreclosure.

Servicers under HAMP may deny a loan modification only for a specified set of reasons,[41] not, as the Settlement Agreement proposes, "other factors as would be deemed prudent in its judgment."[42] Significantly, under HAMP, a servicer is required to offer a loan modification if it is NPV positive (and is permitted to offer one even if it is NPV negative).[43] The Settlement Agreement, by contrast, gives complete discretion—without any direction—to the servicer regarding the terms to consider in evaluating the NPV test, and in whether the loan modification should be provided. Servicers under the Settlement Agreement are under no "obligation on the part of the Master Servicer to offer any modification or loss mitigation strategy to any borrower."[44] In other words, even if the modification would provide a financial benefit to the investors, the servicer is under no obligation to offer it. Such a broad grant of discretion serves the interests neither of homeowners nor investors.

4. Limitations on Principal Reductions

Under HAMP, servicers are required to evaluate the feasibility of reducing the principal balance of loans that have a current loan-to-value ratio (LTV) greater than 115%, but servicers are not mandated to provide the principal reduction. Other loans may also be considered for principal reductions.[45] There is no limit on the amount by which the principal may be reduced, although incentives are provided to investors for reducing the principal down as low as 105% of LTV.[46] Significantly, principal may be reduced as low as the value the home would have after a

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[40] Settlement Agreement, ¶ 5(e).

[41] *See, e.g.,* Making Home Affordable[SM] Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at § 2.3.2 (2011) (listing possible non-approval notices).

[42] Settlement Agreement ¶ 5(e)-(f).

[43] Making Home Affordable[SM] Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at 81 (2011)

[44] Settlement Agreement, ¶ 5(d).

[45] Making Home Affordable[SM] Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at 75 (2011).

[46] Making Home Affordable[SM] Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at 104 (2011).

foreclosure—called the REO number. The rationale for this is that the REO number is the value the property would have to the investor if the foreclosure proceeded and the investor purchased it. Non-interest bearing principal forbearance, which for accounting purposes is treated identically with principal reductions, is explicitly permitted to reduce the interest-bearing principal of the loan below LTV.[47]

The rules for the GSEs do not permit principal reductions, unlike HAMP. In this limited instance, the Settlement Agreement appears more favorable to homeowners than the GSE rules. Nonetheless, the Settlement Agreement is less favorable than the HAMP rules for non-GSE loans, which would otherwise cover these loans.

Unlike the HAMP rules, the Settlement Agreement restricts principal reduction to the current market value.[48] Moreover, the provisions in the Settlement Agreement requiring that "normal" market conditions be assumed and no REO sale values be included in broker price opinion are likely to give an inflated value of the home. If the servicer liquidates the home at a foreclosure, there is likely to be a delay in marketing the home, and the REO discount will very much be in play. It does not serve investors well to deny homeowners the possibility of reducing the principal to the actual value of the home, factoring in the time to sell post-foreclosure and the actual, post-foreclosure, REO sales value. The limitation on principal reduction in the Servicing Agreement excluding the REO number is arbitrary, contrary to HAMP, and it will make it considerably more difficult for homeowners to qualify for affordable loan modifications.

5. Foreclosure Referral and Foreclosure sale

HAMP strictly limits when a loan may be referred to foreclosure and when a home may be sold at a foreclosure sale in order to, in the words of the Handbook, provide "Protections Against Unnecessary Foreclosure."[49] Referral to foreclosure may not happen under HAMP until one of the following events occurs:

- The homeowner is evaluated for HAMP and found ineligible;
- The homeowner fails to make a payment on a trial payment plan;
- The homeowner fails to respond to reasonable solicitation efforts by the servicer;
- The homeowner declines to be evaluated for HAMP; or
- Any escalated cases following a HAMP denial have been resolved.[50]

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[47] The principal forbearance rules specifically allow forbearance below the current LTV, provided that the total amount of forbearance is no more than 30% of the unpaid principal balance. Making Home Affordable℠ Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at 78 (2011).

[48] Settlement Agreement, ¶ 5(e).

[49] Making Home Affordable℠ Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at 58 (2011).

[50] Making Home Affordable℠ Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at 58 (2011). A few categories of escalated cases are excepted from this restriction. *See* Making Home Affordable℠ Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at § 3.4.2 (2011).

These limits apply regardless of how long it has been since the first default on the loan. Similar restrictions apply to homeowners who have entered into or are being evaluated for the Federally Declared Disaster Forbearance[51] or the Unemployment Program Forbearance.[52]

Additionally, HAMP limits when a home can be sold at foreclosure. No home can be sold at foreclosure that is in a trial or permanent modification, that is in the process of being evaluated for a modification, or that has an escalated dispute pending between the homeowner and the servicer.[53] Again, no time limits apply.

The FHFA guidelines also limit foreclosure referrals and sales. The servicer is prohibited from initiating a foreclosure *so long as the homeowner and servicer are engaged in a good faith effort to resolve the delinquency.*[54] More specifically –

- Servicers are required to solicit every homeowner who is 31 or more days delinquent for an alternative to foreclosure.[55]
- Specific information must be provided to the homeowner to ensure that the homeowner understands the home retention options and alternatives to foreclosure.[56]
- A strict order of consideration for different home retention strategies to be evaluated before referral to foreclosure.[57]
- The servicer is required to conduct a formal review of each case to ensure that the homeowner has been considered for all foreclosure alternatives before the loans is referred to foreclosure.[58]
- Even after the foreclosure processing begins, financial incentives are provided to encourage servicers to continue to help homeowners pursue a foreclosure alternative.[59]

While the FHFA standards are not perfect, they far exceed the imprecise and confusing standards articulated in the Settlement Agreement.

In contrast, the compensatory fee provisions in the Settlement Agreement provide strong incentives for servicers to ignore the HAMP and FHFA requirements. The referral timelines for first lien mortgages provide no exceptions for loan modifications, whether in negotiation or actually

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[51] Making Home Affordable℠ Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at 58 (2011).

[52] Making Home Affordable℠ Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at 108-109 (2011).

[53] Making Home Affordable℠ Program, Handbook for Servicers of Non-GSE Mortgages v.3.2, at 44, 59 (2011).

[54] Federal Housing Finance Agency News Release, "*Fannie Mae and Freddie Mac to Align Guidelines for Servicing Delinquent Mortgages,"* April 28, 2011, *available at* http://www.fhfa.gov/webfiles/21190/SAI42811Final.pdf.

[55] Freddie Mac Bulletin, Number 2011-11, Borrower Contact Requirements. June 30, 2011.

[56]Freddie Mac Bulletin, Number 2011-11, Borrower Contact Requirements. June 30, 2011.

[57] Servicing Alignment Initiative: Loan Modification and Workout Process, May 25, 2011.

[58] Federal Housing Finance Agency News Release, "*Fannie Mae and Freddie Mac to Align Guidelines for Servicing Delinquent Mortgages,"* April 28, 2011, *available at* http://www.fhfa.gov/webfiles/21190/SAI42811Final.pdf.

[59] Frequently Asked Questions – Servicing Alignment Initiative, Q8, *available at* http://www.fhfa.gov/webfiles/21191/FAQs42811Final.pdf.

performing.[60] Because homeowners are counted as delinquent during their trial modification (which will be at least three months long, but could be much longer),[61] it is quite possible that servicers operating under the Settlement Agreement would refer homeowners making payments under a trial modification to foreclosure, in violation of both HAMP and common sense.

The first lien foreclosure sale timelines in the Settlement Agreement are also inconsistent with the FHFA standards. The Settlement's guidelines provide exceptions only for "time periods during which . . . the borrower is performing pursuant to HAMP or other loss mitigation efforts mandated by Law"[62] a foreclosure would be permissible (and incentivized) for homeowners while they are negotiating a loan modification. A homeowner *negotiating* a HAMP modification (or a proprietary modification) or appealing a wrongful denial of a HAMP modification is not *performing pursuant to* HAMP. This section of the Settlement Agreement provides a strong disincentive for servicers to even consider, let alone pursue, proprietary modifications: The time limits would apply even when homeowners are performing under a proprietary modification and the Master Servicer would still be required to pay a compensatory fee Master Servicer to the Trust for these loans.

6. Summary of the Differences between Industry Standards and the Settlement Agreement

This table illustrates the stark departure from industry standards contained in the "servicing improvements" required by the Settlement Agreement.

	HAMP Requirements	**FHFA Requirements**	**Settlement Agreement Requirements**
Express Goals	Avoid foreclosure through affordable and sustainable loan modifications	Reduce foreclosure and increase investor income	Unclear
Precise Guidelines for Servicers	Extensive in HAMP	Developed by Freddie Mac and Fannie Mae	Absent
Evaluation Process for Loan Modifications	HAMP evaluation is generally first, unless the homeowner declines HAMP. Alternatives only if HAMP ineligible	Explicit list requiring evaluation for HAMP, then alternatives in order	Simultaneous evaluation required for all loan modifications
Time Required for Decision	Within 30 days from receipt of homeowner's packet	Incentive fees paid to servicers for completing modifications within 60 days of delinquency	Within 60 days of receipt of B's information
Basic Eligibility for Loan	Unaffordable loan payments and NPV analysis	Modified principal and interest payments must	Unclear

[60] Settlement Agreement, ¶ 5(c)(i)(A).

[61] According to data released by Treasury, a significant number of trial modifications take more than six months to convert to permanent modifications. *See, e.g.,* Making Home Affordable Program Performance Report through April 2011 at 6. In April 2011, Bank of America reported that it had 9,695 trial modifications on its books that were at least six months in duration, more than three times any other single servicer. *Id.* at 7.

[62] Settlement Agreement, ¶5(c)(i)(B).

Modification		result in 10% reduction in payments, and a housing expense to income ratio more than 10% but equal to or less than 55%.	
Structure of Modification	Standard waterfall, with interest rate reduction, term extension, and principal forbearance; interest rate and payment fixed at affordable level	Capitalize arrearages, adjust interest rate, extend term, forbear principal.	Unclear
Principal Reductions	Permitted without limitation	Not permitted	Limited to reduction to appraised value, based on sales outside of foreclosure
Limits on Dual Track	Evaluation required before referral to foreclosure; pending foreclosures must be stopped; no foreclosure sale during evaluation, modification, or appeal	Evaluation required before referral to foreclosure; certification required before foreclosure	Appears to be permitted and encouraged, even to point of foreclosure sale
Fees to Homeowners	No fee for modification, late fees waived, other default fees must be reasonable	Fees limited and may be waived	No limit on fees to homeowners.
Appeals Process	In-house and independent process; foreclosure sale stayed during appeal	In-house and independent process; foreclosure sale stayed during appeal	None

C. The Servicing "Improvements" Likely Will Speed Foreclosure without Protecting Homeowners

At the heart of the servicing "improvements" are two proposals: referral of loans in default to specialty subservicers and compensatory fees should Bank of America not ensure that loans are moved to foreclosure sale sufficiently quickly. Neither of these proposals by themselves helps homeowners; both, if left unaddressed, are highly likely to harm homeowners.

1. Referral to Subservicers Will Not Protect Homeowners from Illegal and Abusive Servicing

The centerpiece of the Settlement Agreement's servicing improvements is the transfer of loans in default to subservicers.[63] Most of the ink in the Settlement Agreement discussing the transfer to subservicers is devoted to detailing the speed of transfers, yet there are few checks on these subservicers. Implicit in this structure is the belief that simply by transferring loans to subservicers, without putting any checks on how those loans are serviced, servicing will improve. This perspective does not account for the risks inherent in any transfer of servicing, including lost or misapplied payments, nor does it acknowledge that the abuses in servicing extend to both large and

[63] The loans that must be transferred range from loans that are 45 days past due without good contact with the homeowner to loans which are in foreclosure or bankruptcy. Settlement Agreement, ¶ 5(b).

small servicers, and that even specialty servicers who specialize in servicing loans in default have failed to process loans appropriately.

While transfer of servicing once a loan is in default to subservicers may change the incentive structure for the Master Servicer, encouraging the Master Servicer to keep the loans performing, so as to prevent the loss of servicing rights and income, the Settlement Agreement fails to ensure that the interests of subservicers are aligned with the interests of either investors or homeowners. The Settlement Agreement allows subservicers to continue to make arbitrary decisions without oversight and contemplates paying subservicers more for foreclosure and home sales than for loan modifications.

The transfers to servicers must happen relatively quickly: The Institutional Investors and the Master Servicer must agree on a proposed list to submit to the Trustee within 30 days of signing and the Trustee is given 45 days to approve the subservicers.[64] (Presumably this has already occurred, as the Settlement Agreement was signed over 60 days ago, on June 28, 2011.) The Master Servicer is expected to bring subservicers online within three months of the Trustee's approval.[65] As soon as even one subservicer is operational, transfer of servicing of loans must begin.[66]

Subservicers are only required to meet certain minimum requirements. For example, they must be licensed in the state in which they are operating, and they must agree to comply with applicable laws.[67] Beyond these minimal requirements, the checks on subservicers are confined to the following:

> a) subservicers are limited to servicing no more than 30,000 of the loans from the Covered Trusts at any point in time;[68]
> b) only one subservicer may be assigned to loans owned by each trust;[69]
> c) subservicers must return performing loans to the Master Servicer after 12 months;[70] and
> d) the incentives provided to subservicers in the fees they will receive.[71]

The primary feature of the servicing improvements, then, is the transfer of loans in default to specialty subservicers. Presumably, the parties believe that the threat of transfer of the servicing rights will motivate Bank of America to work harder to keep loans performing and that the subservicers, with smaller portfolios and rewards for resolving delinquencies, will provide superior servicing on loans in default. Unfortunately, the Settlement Agreement puts in place no checks to make these fond hopes of servicing improvements a reality.

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64 Settlement Agreement, ¶ 5(a)(i).

65 Settlement Agreement, ¶ 5(a)(v).

66 Settlement Agreement, ¶ 5(a)(vii).

67 Settlement Agreement, ¶ 5(a)(iii) deals with the minimal requirements for subservicers.

68 Settlement Agreement, ¶ 5(a)(vii).

69 Settlement Agreement, ¶ 5 (a)(viii).

70 Settlement Agreement, ¶ 5(a)(ix).

71 A "representative" structure for subservicer compensation is set out in Exhibit E of the Settlement Agreement.

The Agreement is missing critical guidance for subservicers:

a. There are no clear directives that the servicing of these defaulted loans preserve homeownership or maximize investors' income.

b. There are no outcome measurements, no performance matrices, no reporting requirements to ensure that subservicers are increasing income to investors or appropriately treating homeowners.

c. The minimal requirements for subservicers do not ensure that the subservicers included in the list are capable of engaging in better servicing protocols than the Master Servicer has been.

d. The Agreement provides no protection for homeowners from problems that may be occasioned by the transfer, including lost records, misapplied payments, or general confusion on the part of homeowners as to where payments should go or how to resolve disputes with the servicer.

e. The incentive fee structure provides only weak incentives for home retention

Given the lack of directives, outcome measurements, or significant standards, the driving force for the servicing of the loans in default is the subservicers' fee structure. The chart below, a reproduction of Exhibit E of the Settlement Agreement, shows the monthly fees and the incentive fee structure for subservicers with portfolios of more than 1000 loans.

Exhibit E
Representative Subservicer Compensation

Base Fee:
For each Mortgage Loan, a monthly fee pursuant to the chart below

End of Month Status Volume:	**1,000 plus loans**
0-29 Days Past Due	$25
30-89 Days Past Due	$55
90+ Days Past Due	$100
Foreclosure	$100
Bankruptcy	$90
REO Property	$65

Incentive Fees	**Incentive Fee Type Incentive Amount**
No contact incentive	$100
Paid in Full (previously 60+ days past due)	1.50% of UPB – Minimum: $500; Maximum: $5,000
Short Payoff (Refinance or Note Sale)	1.25% of UPB – Minimum: $500; Maximum: $5,000
Modifications	1.50% of UPB
Payment Plan or other workouts	0.75% of UPB
Short Sale	1.50% of Sales Price – Minimum: $500; Maximum: $5,000
Deed in Lieu	0.5% of UPB – Minimum: $500; Maximum: $3,000
REO Disposition	1.00% of Sales Price – Minimum: $750; Maximum: $5,000

This chart has at least one large gap in its description of the incentive structure for subservicers. The chart does not account for default fees and fee splitting agreements with third-party vendors, other than fees paid by the listing broker. These fees have been a significant profit center for servicers, particularly in the post-foreclosure REO context.

Indeed, compensating servicers for REO dispositions appears to promote double dipping. Servicers will have already received payments for property maintenance and inspection fees, and yet under the Settlement agreement they are paid another 1% disposal fee. The limitation on double dipping in Exhibit E is confined to payments by the listing brokers; it does not clearly cover fees paid by other third-party vendors nor is it clear if compensation would change should the listing broker be an affiliate of the subservicer.

Where the homeowner has executed a deed-in-lieu, the REO compensation is clearly double-dipping, since the deed-in-lieu will not resolve the matter but will still require REO disposition. Servicers who obtain a deed-in-lieu, then, can expect to receive total compensation of at least 1.5%: 0.5% for the deed-in-lieu and another 1% for the REO disposition. That rough parity between a modification and an REO disposition subsequent to a deed-in-lieu does not account for any default fees recovered from the homeowner, fees charged the homeowner for obtaining a deed-in-lieu, or fees obtained from third-party vendors in the REO disposition, other than a fee obtained from the listing broker.

As a result of this gap in accounting for subservicer compensation, the benefit from both default servicing and foreclosure is understated. This means that subservicers will have stronger incentives to refuse to modify a loan and to proceed with a foreclosure than is reflected in this representative incentive chart.

Important details about the structure of subservicer compensation are missing. It is not clear, for example, how the subservicer would be compensated in the event the homeowner brought the loan current with a lump sum payment. We presume that "Paid in Full," refers to a full payoff of the note, including a sale or refinancing, but it could also mean that the default was paid in full and the loan brought current. If it means, as we think, only payment in full of the note, and not the arrearages, then it remains an open question whether subservicers will receive any incentives to work with homeowners to bring the loan current with a lump sum payment. If there are not such incentives, subservicers may be inclined to provide incomplete or confusing information on the amount of arrears or how the loan could be brought current, or to insist that homeowners enter an expensive payment agreement instead of bringing the loan current.

Further problems with the incentive structure emerge upon examination. The subservicers' monthly fee will drop dramatically once a homeowner resumes payments. After a loan modification has been executed, the loan is no longer considered in arrears, so the servicer's monthly fees for the year during which the homeowner is making payments on the executed loan mod are based on a loan that is not in default. Instead of receiving $100 a month for servicing the loan, the servicer receives only $25 a month. A year of servicing a successful loan mod thus brings in only $300. In comparison, servicing of loans that remain 90 days behind yields $100 a month, or $1200 a year. This encourages subservicers to choose resolutions, such as a deed-in-lieu, short sale, or foreclosure, where a homeowner remains in default status for longer rather than moving quickly to a modification and perpetuates a pervasive problem in the existing schema of servicer incentives.

Also, because servicers may have a constant supply of loans in default to be transferred to susbservicers once they dip below the 30,000 threshold by resolving a case, subservicers are encouraged to reach resolutions that result in a compensation payment quickly. The subservicer will not receive incentive payments for performing the loan modification until the end of twelve successful payments, at which time the loan is also transferred back to the Master Servicer. Subservicers are likely to collect considerably more by pushing a loan into a short sale or a deed-in-lieu, largely because more loans can be processed into these resolutions in the same time it takes to process one modification. Once one loan is removed from its mini-pool, the subservicer will receive the incentive payment for resolution and another loan to service, with another chance to recover an incentive payment. One result of this feature is that it prioritizes resolutions that can happen quickly. In this schema, modifications are per se disadvantaged. There is no time to obtain documents from the homeowner, to evaluate and process the modification, and to execute the final loan modification agreement. Even after execution of the loan modification, there is a 3-month waiting period while the homeowner makes payments under a trial modification, followed by a year of payments on the modification before the servicer can return the loan to the Master Servicer and receive its incentive payment and the chance to have a chance at another loan.

A short sale, for example, may be pulled off in a matter of a few months, allowing servicers to earn the highest monthly fee throughout their time servicing these loans and earn the fee incentive of 1.5% of the sales price with a quick turn-around. As a loan which is sold in a short-sale will be replaced by another loan in default from the Master Servicer, the total income—from monthly fees and incentive fees—will likely be many multiples of the fees earned for nursing a loan modification from eligibility determination through to transfer back to the Master Servicer. The combination of reduced fees once the loan is no longer in default status, the zero-sum nature of the servicing outcomes (once subservicers reach their cap of 30,000 loans, they cannot get additional loans to service until they have resolved existing loans), and the delay in receiving incentive payments shrinks the incentives to perform modifications.

Although the referral of loans to specialty subservicers seems designed to increase Bank of America's incentives to keep loans performing and will reduce its ability to profit from default-related fees, nothing in the proposed Settlement Agreement actually requires the responsible servicing of loans by subservicers. Provisions for responsible servicing by subservicers are critical to protect the interests of homeowners. Transfer to subservicers may increase the risk of errors in loan accounting, abusive debt collection practices, and confusion on the part of homeowners accustomed to dealing with one entity. While subservicers must meet certain standards, such as state licensing,[72] these standards provide no assurance that the subservicers will perform better than Bank of America has in the past. There are no standards applicable to these subservicers that require, or even measure,[73] success implementing loss mitigation strategies or loan modification net present value analyses, or even commitment to maximizing income to the investor in the decision of whether to pursue foreclosure or permit home retention loss mitigation strategies. Given the lack of standards and the weak incentive structure, the referral to subservicers is unlikely to improve the servicing of loans in default.

[72] Settlement Agreement, ¶ 5(a)(iii).

[73] The attestation reports required by Bank of America in ¶ 5(f) simply require reporting "for each covered trust, concerning its compliance with the Servicing Improvements required by this Settlement Agreement," and that an annual report be completed for each covered trust.

2. The Compensatory Fee Structure Speeds Up Foreclosures without Protecting Homeowners from Wrongful Foreclosure

The compensatory fee structure for defaulted loans retained by Bank of America—or which have not yet been assigned to subservicers—detailed in paragraph 5(c)(iii) provides very significant financial incentives for Bank of America to speed up the foreclosure process. Under that structure, Bank of America must remit to the trust a monthly compensating fee based on how long, compared to standard timelines, it takes to refer a loan to foreclosure and how long to process that foreclosure. The fee per loan can reach the equivalent of a month's interest if the time for referral to foreclosure or for completion of foreclosure exceeds the standard timelines. We believe that the intent of this structure is to speed up foreclosures, and that speeded up foreclosures are the likely result of this compensatory fee structure.

The speeded up foreclosure process is likely to impede any meaningful review of foreclosure alternatives and therefore will result in unnecessary foreclosures and sales of homes. Homes will be sold while homeowners await the results of their loan modification application, and the accelerated process will cause homeowners to incur unnecessary foreclosure fees, that further prices modifications out of reach. With the referral to foreclosure come fees added to a homeowner's account. There are many documented instances where these fees have prevented a homeowner from being able to afford a loan modification.

The compensatory fee structure set forth in paragraph 5(c)(iii) applies to loans retained for servicing by Bank of America. Under this structure, should Bank of America fail to refer a loan to foreclosure in a timely way, or fail to liquidate the property at a foreclosure sale quickly enough, Bank of America faces the prospect of paying to the Trust an amount equivalent to the monthly interest due on that loan. There are no corresponding penalties for errors in servicing that harm homeowners. This lopsided incentive structure will foster foreclosures at the expense of homeowners. Moreover, these accelerations will not even permit the evaluation of loss mitigation strategies that would protect investors, let alone homeowners.

The system as proposed provides no exceptions for instances when a homeowner and a servicer are in the midst of negotiating a loan modification or when the homeowner is performing under any loan modification for the initial referral or performing under a proprietary loan modification or any other non-HAMP loan modification not mandated by law for a foreclosure sale. The result is that the dual track system, of proceeding with foreclosures while negotiating loan modifications, a system repudiated by HAMP and by the Federal Housing Finance Authority in the recent Servicing Alignment, is encouraged and even mandated, with the predictable result of an increase in wrongful foreclosures.

The cumulative impact of the settlement's acceleration of the foreclosure process is a de-emphasis on modifications or other loss mitigation strategies, with a consequent weakening of the incentives to prevent foreclosure.

V. Conclusion

For the reasons described above, in our independent opinion, we believe that homeowners will be harmed if the Settlement Agreement is permitted to govern the servicing of home loans by Bank of America.

Respectfully submitted,

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