

Estimating the Effects of Mortgage Default Counseling

J. Michael Collins
University of Wisconsin-Madison

Maximilian D. Schmeiser
Federal Reserve Board

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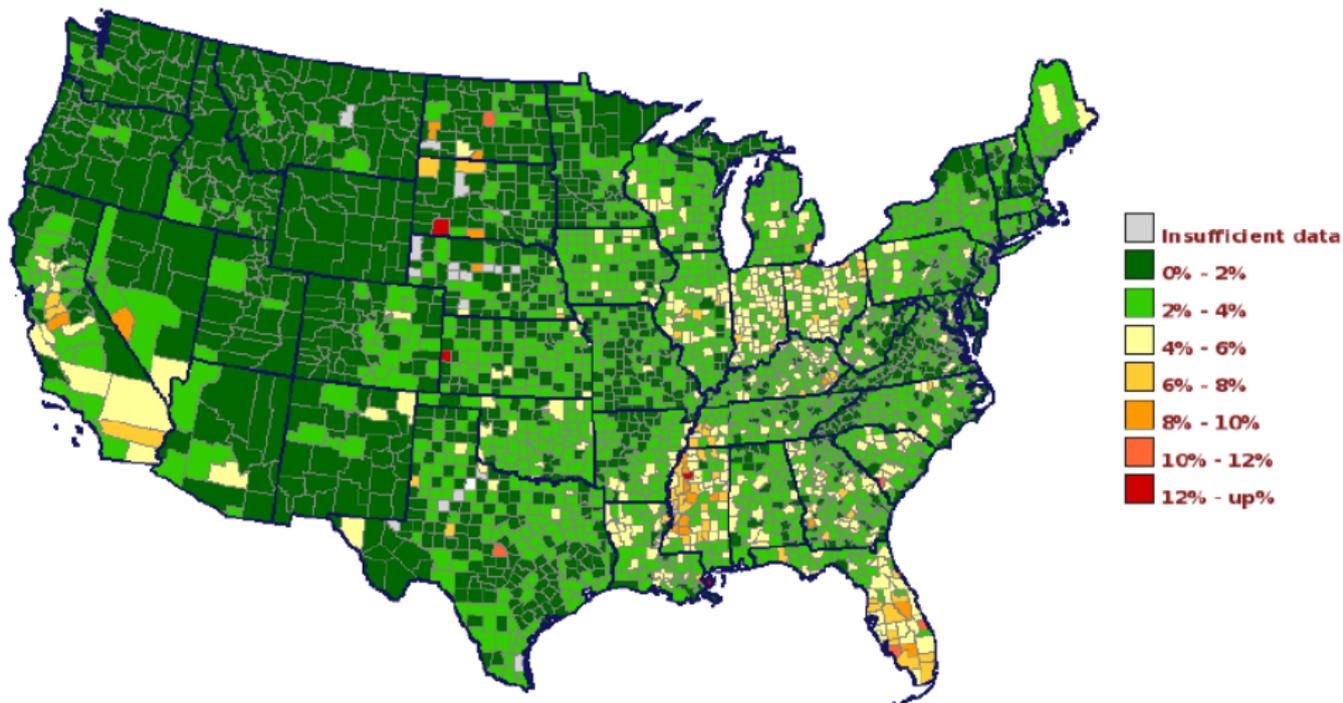
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Policy Context

- Recent recession and housing market collapse have resulted in millions of Americans becoming delinquent on their mortgages and at risk of foreclosure
 - March 2012: 7.44% of all mortgages 90+ days delinquent or in foreclosure
- Large number of foreclosed homes risks substantially prolonging the housing market downturn
- Several programs have been implemented by the federal government to help homeowners avoid foreclosure and keep their homes:
 - Home Affordable Modification Program (HAMP)
 - National Foreclosure Mitigation Counseling (NFMC) Program
 - Home Affordable Refinance Program (HARP)

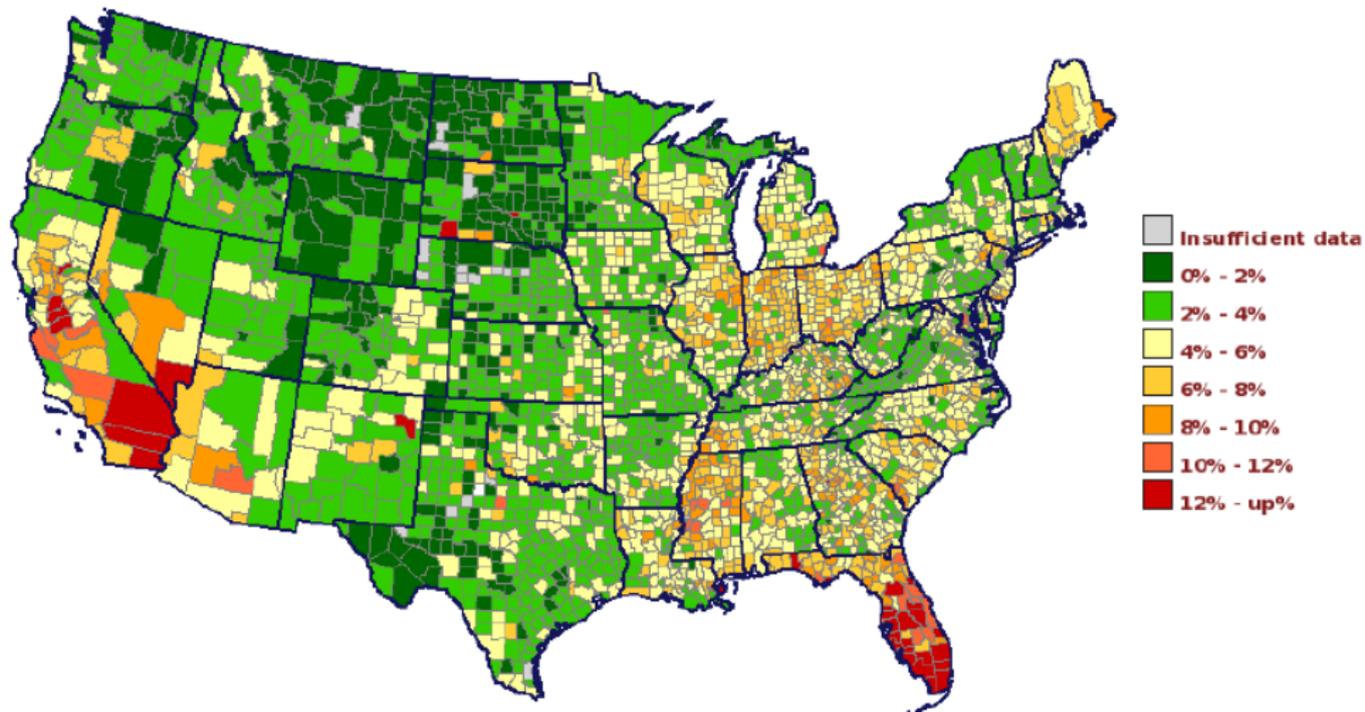
Mortgage Delinquency and Foreclosure Nationwide: April 2008

Delinquent Payment: 90+ PD, Foreclosure, US, 200804*



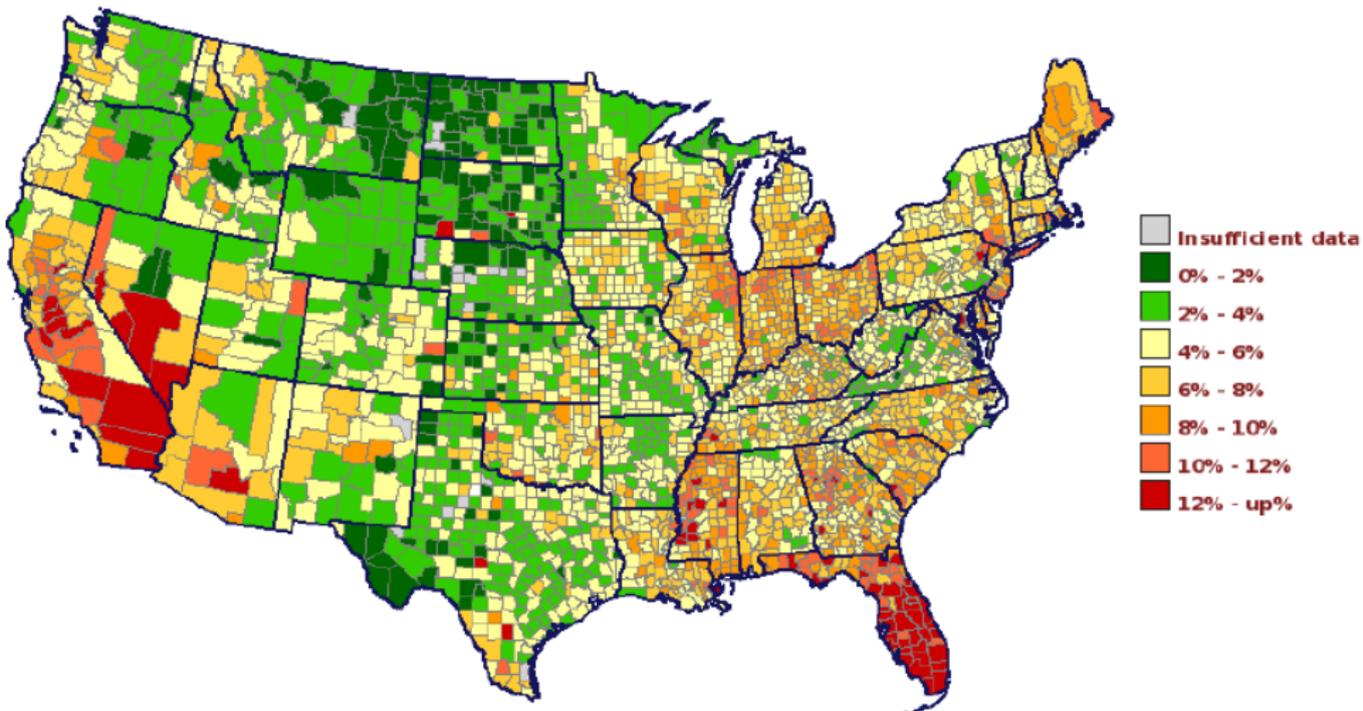
Mortgage Delinquency and Foreclosure Nationwide: April 2009

Delinquent Payment: 90+ PD, Foreclosure, US, 2009Q4*



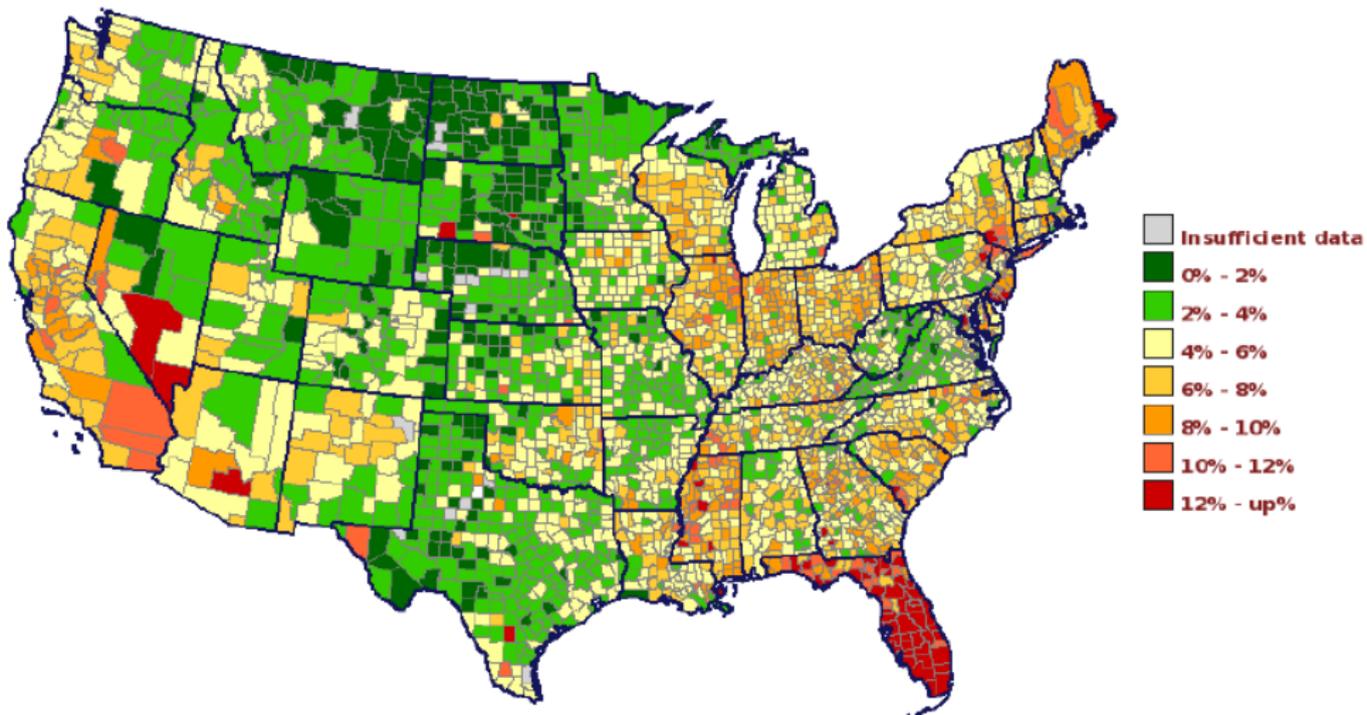
Mortgage Delinquency and Foreclosure Nationwide: April 2010

Delinquent Payment: 90+ PD, Foreclosure, US, 2010Q4*



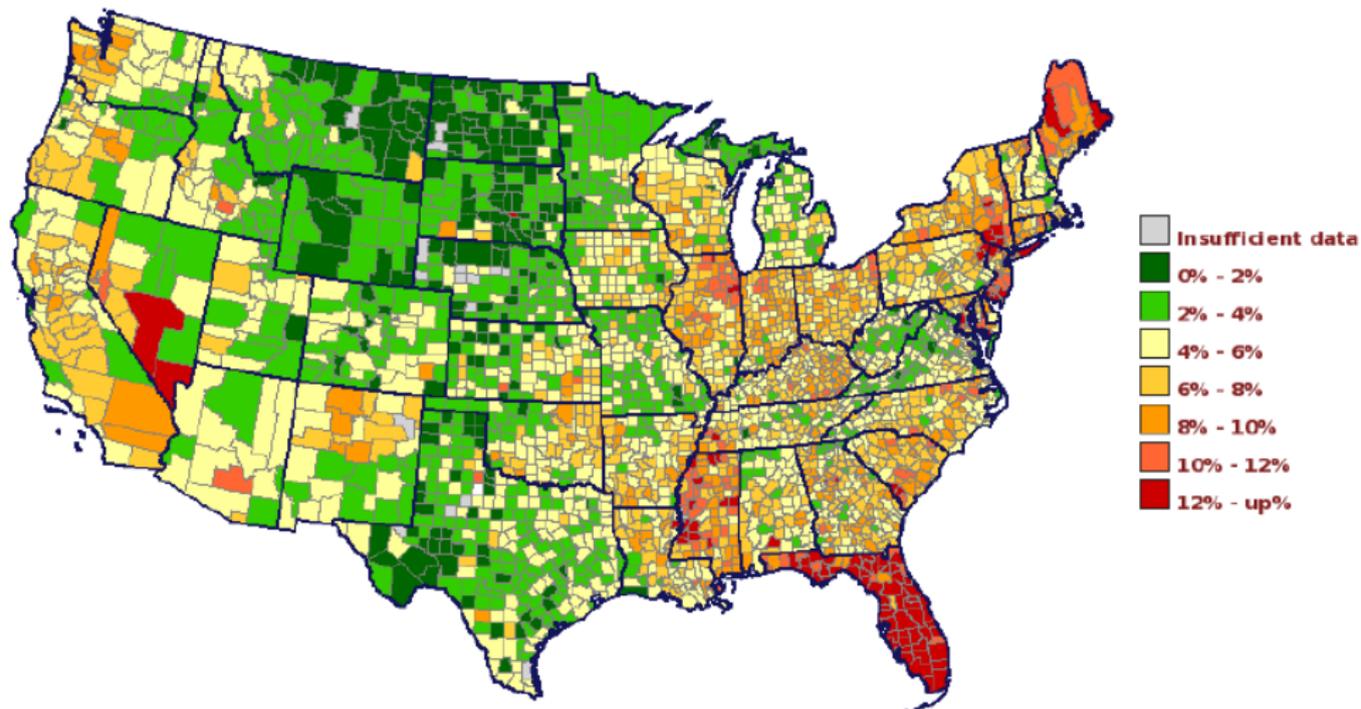
Mortgage Delinquency and Foreclosure Nationwide: April 2011

Delinquent Payment: 90+ PD, Foreclosure, US, 201104*



Mortgage Delinquency and Foreclosure Nationwide: April 2012

Delinquent Payment: 90+ PD, Foreclosure, US, 2012Q4*



Motivation

- Allocated \$400+ million for NFMC Program for mortgage default counseling with limited evidence of its effectiveness
 - Primarily due to limited provision of default counseling prior to housing crisis
 - Homeowners could generally sell their home if they ran into trouble
 - Frequency of default counseling so low as to make quantitative analysis difficult/little data with which to evaluate
 - Selection into counseling on unobservable characteristics related to mortgage outcomes (motivation, financial knowledge, etc.)
- However, several years into the crisis we now have:
 - Widespread default and use of counseling
 - Numerous sources of data on borrowers, counseling and mortgage outcomes available
 - Months, if not years, of observations following receipt of counseling and/or a loan modification

Research Question

- Examine the effect of mortgage default counseling on borrower outcomes (receipt of a modification; REO) controlling for selection into counseling
- Examine whether the timing of counseling receipt affects borrower outcomes
- Compare parameters of modifications for borrowers who received counseling relative to those who did not receive counseling
- Compare outcomes for borrowers who receive a loan modification with and without counseling

Roles & Rationales for Default Counseling

- What is the purpose of foreclosure counseling and how can it help a borrower?
 - Diagnose payment problem
 - Review income and expenditures/create a budget
 - Prioritize non-mortgage debts
 - Maximize potential income (i.e. Food Stamps enrollment)
 - Form repayment strategies, including mortgage modification or selling the home (if possible)

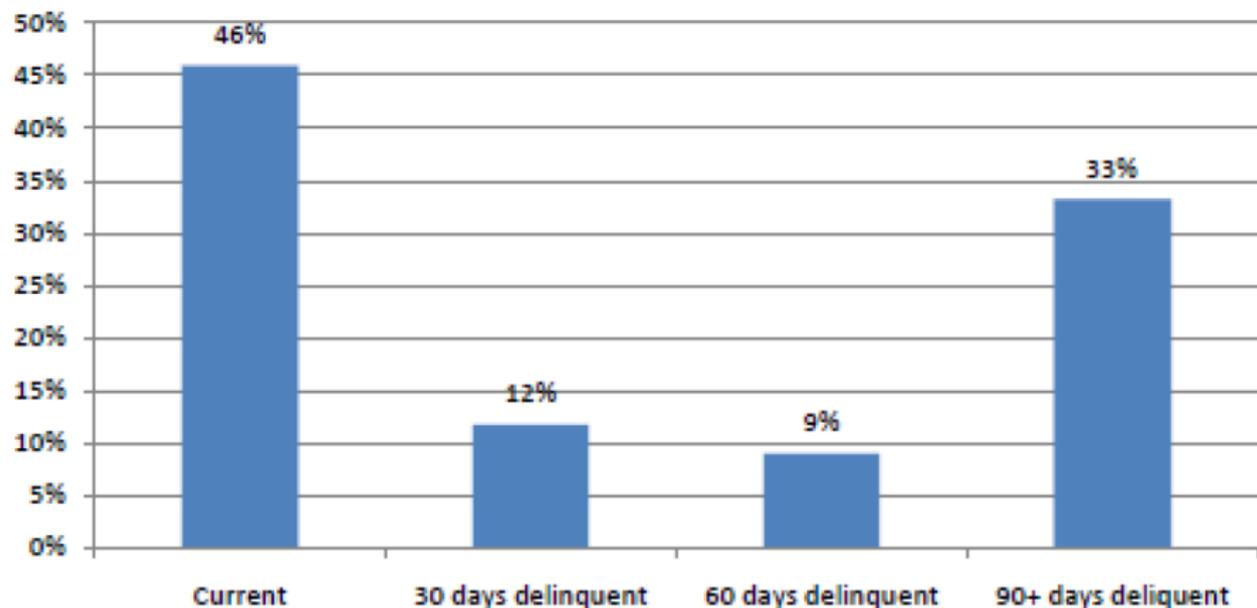
Roles & Rationales for Default Counseling

- Complex contracts that targeted populations fail to understand
- Modification process is complex and often frustrating; counselor can better navigate the system
- Lack of information about alternatives including public and private programs
- Emotional distress as a barrier to information processing
- Trusted 3rd party advisor in time of hardship
- But...
 - Limited potential if income reduced or eliminated
 - Quality and availability are uneven

Data

- Use Wells Fargo Bank, N.A. Corporate Trust Services (CTS) database linked to administrative data on counseling from Homeownership Preservation Foundation's HOPE hotline (888-995-HOPE)
- CTS is a service of Wells Fargo Bank, N.A. that provides information on a variety of investment vehicles administered by the bank
- CTS data cover nearly six million securitized mortgages for which Wells Fargo serves as the trustee
- HOPE hotline has fielded over one million calls from borrowers
- Have counseling data spanning January 2008 through December 2010 and CTS loan data from January 2008 through May 2011
- Obtain 22,000 matched borrowers and use comparison group of 50,000 randomly selected uncounseled borrowers who were delinquent at some point in the sample period

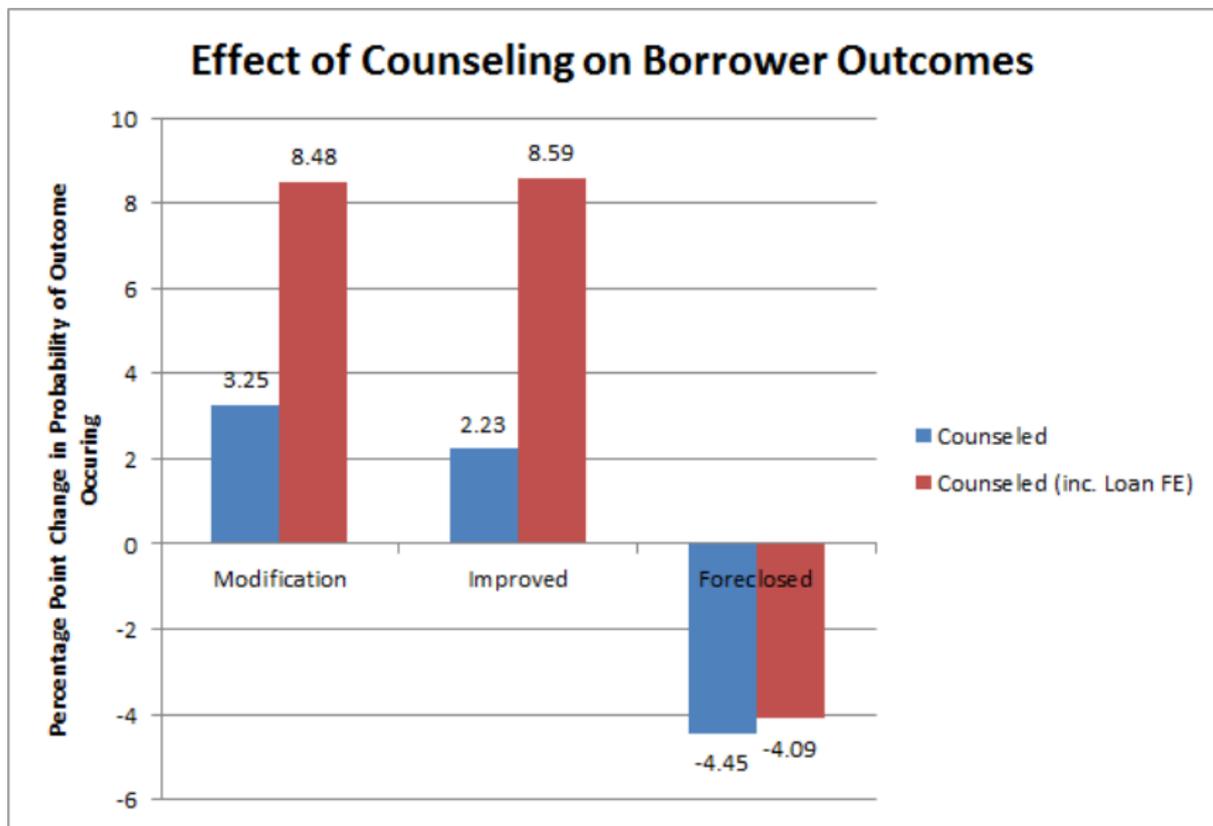
Delinquency Status at Time of Counseling



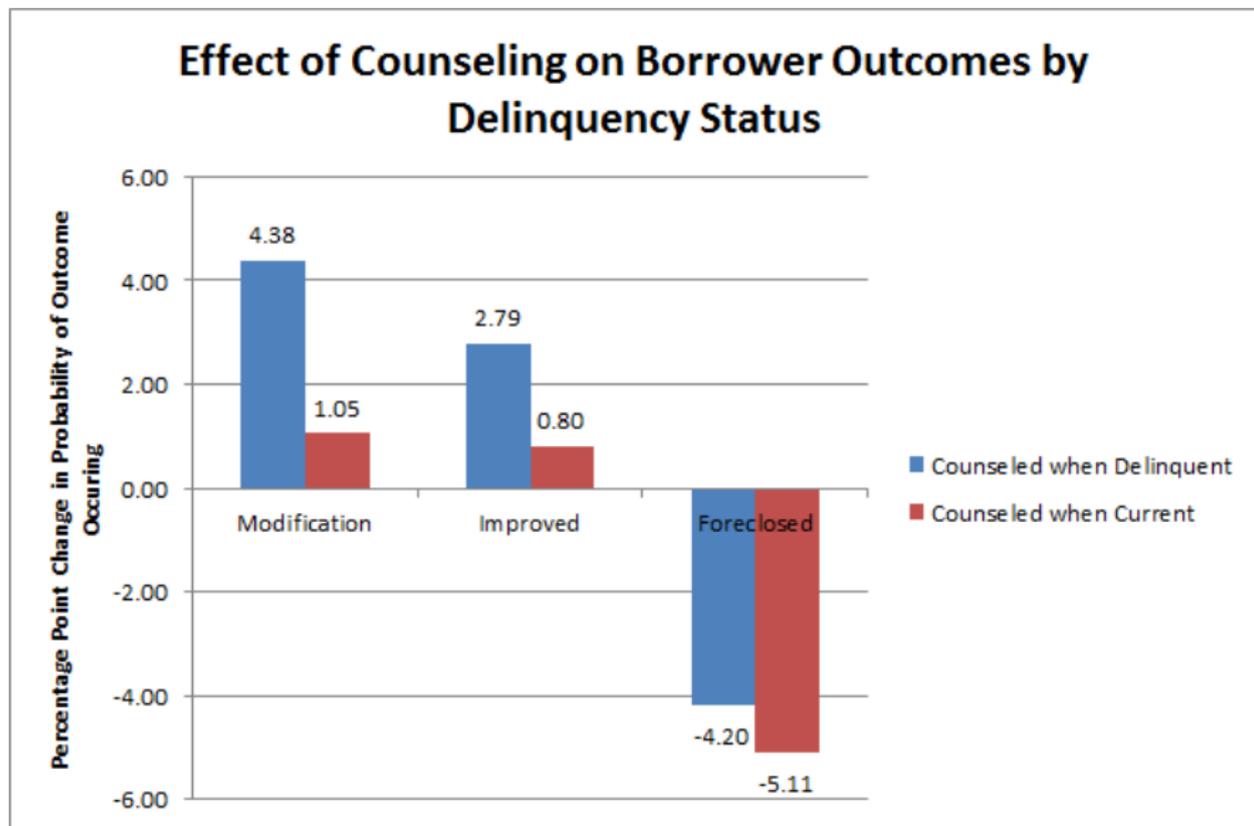
Empirical Methods

- Estimate the performance of counseled borrowers relative to uncounseled borrowers on four mortgage outcomes: missing a payment; improving loan status; repossession of home (REO); and receiving a loan modification
- Control for various factors including: LTV at origination; year origination; current FICO; ARM; loan balance; MSA unemployment; FHFA Housing Price Index (HPI); quarter and state fixed-effects
- Alternately include individual fixed-effects to control for unobserved heterogeneity

Impact of Counseling on Borrower Outcomes



Impact of Counseling on Borrower Outcomes by Timing



Impact of Counseling on Terms of Modification

- Counseled borrowers who receive a loan modification get better terms than uncounseled borrowers:
 - \$110 lower monthly payment on average
 - 5 basis points lower interest rate on average
- Counseled borrowers perform better post-modification:
 - Approximately 0.6 percentage point lower probability of subsequent REO
 - Approximately 0.2 percentage point lower probability of redefault

Conclusions

- Counseling consistently increases the probability of receiving a loan modification
 - Approximately 8.5 percentage point (44%) increase relative to uncounseled borrowers
- Counseling reduces probability of REO (completed foreclosure/loss of home) by 4.1 percentage points (55%)
- Delinquency status when borrower receives counseling matters
 - Delinquent borrowers more likely to receive mod, also more likely to end in foreclosure
- Among borrowers receiving loan mods, counseled borrowers significantly less likely to subsequently lose their home to REO than uncounseled borrowers
- Likely due to the fact that they receive better terms on their loan modifications (lower monthly payment, lower interest rate, etc)

Conclusions

- Counseling works
- Timing of counseling receipt is very important
- Earlier is generally better; although easier to get mod when delinquent
- In general, investment in counseling should yield positive results for borrowers
- However, no amount of counseling solves lack of income, loss of job, etc. with which to meet mortgage obligations

Contact Information

Maximilian D. Schmeiser
Economist
Consumer Research Section
Federal Reserve Board
Washington, DC 20551
Phone: 202-728-5882
Email: max.schmeiser@frb.gov