New England Public Policy Center
Research Report 11-3
September 2011

Research Report

State Foreclosure Prevention Efforts in New England: Mediation and Assistance

By Robert Clifford

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Acknowledgements

This paper could not have been completed without the assistance of many individuals both within and outside the Federal Reserve Bank of Boston. In particular I would like to offer thanks to the following individuals: to Lisa Tarquinio for assistance with background research, to Matthew Buckley for diligently fact-checking my work, to Sandra Hackman for her superb editorial services, to Elizabeth Murry for her mentorship and guidance throughout the writing process, to Lynn Browne, Karen Borgstrom, Prabal Chakrabarti, Carol DeRosa, Chris Foote, Alanna Kabel, Archie Manning, Bobbie Jo Marcoux, Peter Merrill, Roberta Palmer, Grace Pazden, and Lauren Blake Weliver for providing useful guidance and insightful comments, to Darcy Saas for her assistance throughout the production process, and to Yolanda Kodrzycki for reviewing multiple drafts and providing invaluable suggestions and support along the way. All remaining errors are my own.

State Foreclosure Prevention Efforts in New England: Mediation and Assistance

Introduction

The current housing foreclosure crisis in the United States was long in the making. A rapid increase in home prices from 1998 to 2006 created unrealistic expectations regarding future home values. These expectations spurred people to invest more in housing—often by taking on larger mortgages with lower downpayments. Meanwhile lenders loosened loan standards, reasoning that mortgage holders who got into financial trouble could sell or refinance their homes rather than default, and that higher home values would insulate the lenders from financial loss.[1] With higher loan-to-value ratios, homeowners and lenders alike became more susceptible to losses if housing prices fell.[2]

Declines in house prices from 2006 onward exposed this risk, prompting a large number of foreclosures.[3] Although initially concentrated among subprime borrowers, foreclosures among prime borrowers began to outpace subprime foreclosures by late 2008 as the U.S. economy plunged into a deep recession.

The number of foreclosures has remained stubbornly high ever since, with nearly 2.8 foreclosure filings in 2009, and a record of nearly 2.9 million in 2010.[4] And the outlook remains grim, with expectations of 2.25 million foreclosure filings in 2011, and nearly 2 million in 2012.[5] With foreclosures expected to weigh heavily on the housing market and economic recovery, federal, state, and local policymakers continue to search for ways to stem the tide.

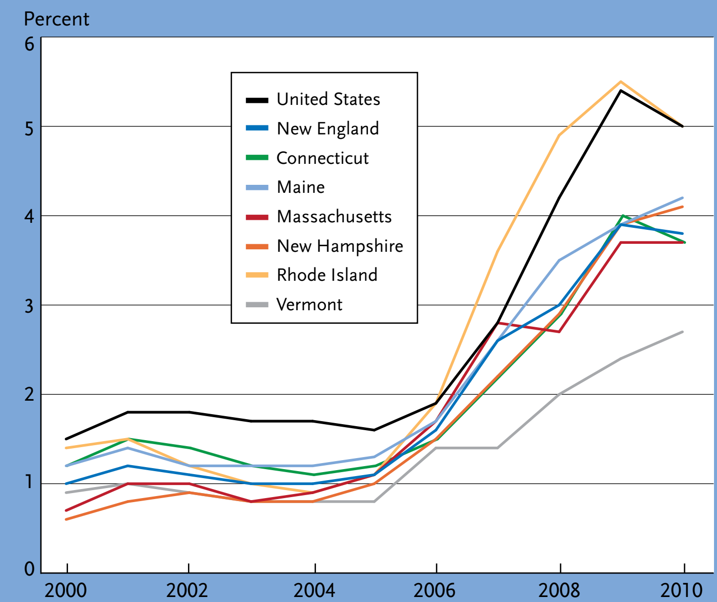
This crisis has led to an alphabet soup of federal programs to prevent foreclosures. These programs first targeted subprime borrowers, helping them refinance mortgages with high monthly payments into those with more affordable payments. However, these programs met with limited success. The largest federal effort came in 2009, with the allocation of $50 billion from the Troubled Asset Relief Program (TARP) to create the Home Affordable Modification Program (HAMP). This voluntary program offers payments to lenders that agree to modify the terms of delinquent mortgages, enabling homeowners to remain in their homes.

However, a recent congressional oversight report found that HAMP is likely to prevent only 700,000 to 800,000 foreclosures—far short of its goal of 3 million to 4 million.[6] The report cites the fact that mortgages are far more than a simple relationship between borrowers and lenders as a major reason for the program's shortcomings.[7] The role of loan servicers—companies hired by banks to handle the day-to-day management of a mortgage—in the foreclosure process has made the monetary incentives of the voluntary program ineffective, as servicers can actually profit from foreclosure-related fees. HAMP tried to correct for this distortion by offering incentive payments to mortgage servicers as well as banks, but the former do not have to participate, and consequently most have not. Such shortcomings have not deterred further federal foreclosure prevention efforts, as emerging federal programs continue to try to prevent foreclosures (see Box 3).

At the same time, while grappling with tight budgets, a number of states have created their own foreclosure prevention programs, relying on various strategies to respond to the litany of challenges they pose. These efforts range from outreach campaigns that provide troubled homeowners with information on foreclosure resources, to legal assistance and counseling programs that guide troubled borrowers through the foreclosure process, to mortgage refinancing programs.[8]

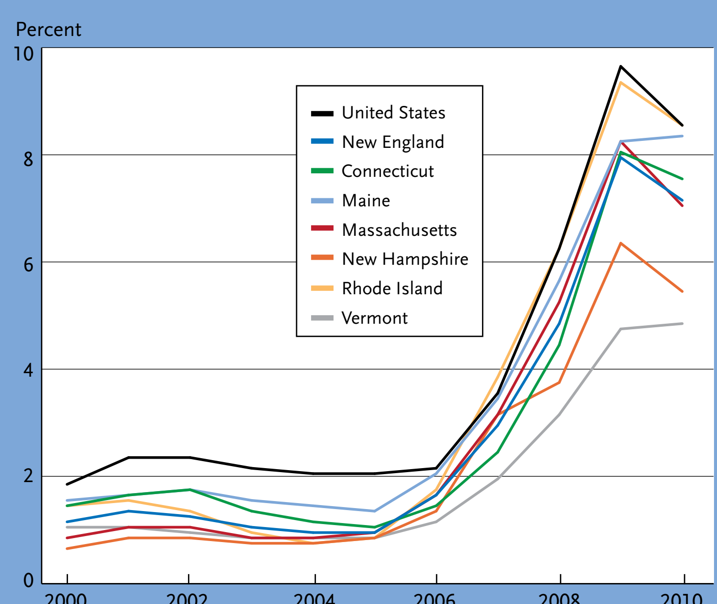
In 2007 the Federal Reserve Bank of Boston's Community Development unit documented early foreclosure prevention

Figure 1. Foreclosures Started as a Share of Outstanding Mortgages
2000–2010



Source: Mortgage Bankers Association/Haver Analytics
Note: "Foreclosures started" refers to the percentage of all mortgages in the pool sent to the foreclosure process each year.

Figure 2. Seriously Delinquent Mortgages as a Share of Outstanding Mortgages
2000-2010



Source: Mortgage Bankers Association/Haver Analytics
Note: "Seriously delinquent mortgages" include the percentage of mortgage payments at least 90 days past due plus the percentage of all mortgages in foreclosure.

efforts in the six New England states.[9] These programs included referral programs, consumer awareness campaigns, education and counseling for homeowners, and a refinancing program aimed at subprime borrowers. States in the region have recently expanded these programs and developed new ones focused on two major strategies. Five New England states have created foreclosure mediation programs, and two have developed financial assistance programs that target unemployed homeowners and those with negative equity: that is, their home is worth less than the amount owed on their mortgage.

This report focuses on these newer foreclosure prevention efforts. It explores how these programs are funded, weighs their benefits and shortcomings, and attempts to assess their record in preventing foreclosures. When possible, the report makes policy recommendations to improve these programs by drawing on relevant research and highlighting the successes of similar programs outside the region.

The review shows that mediation programs have the potential to play a role in nearly all residential foreclosures by facilitating a conversation between homeowners and lenders. Although this sounds simple, it requires that policymakers design programs with adequate incentives to ensure the participation of both parties. Mediation programs in which incentives are correctly aligned have been fairly successful in finding alternative solutions to foreclosures. However, further information and analysis is needed to better understand which aspects of these programs have enabled them to prevent foreclosures and to evaluate their long-term effectiveness.

In comparison, financial assistance programs are narrowly focused, and provide financing directly to troubled homeowners who are likely to avoid foreclosure with such aid, thus avoiding the challenges of negotiating with a lender. These programs require a combination of foresight to address the changing nature of foreclosures, and flexibility to react to the shortcomings of the programs' initial designs. The major challenge facing financial assistance programs has been the scale of funding required, though such assistance is typically provided in the form of loans paid back over time.

The next section provides a brief overview of foreclosure trends in New England and the challenges these pose, to show why finding alternatives to preventable foreclosures is good public policy. The third section examines foreclosure mediation programs, and reveals how their design affects the programs' success in preventing foreclosures. The fourth section reviews financial assistance programs in New England states, and examines how qualifications for receiving assistance affect the programs' ability to help troubled homeowners. The concluding section combines lessons from the review of both mediation and financial assistance programs to provide general policy recommendations for current and future foreclosure prevention efforts.

Why preventing foreclosures is good public policy

In 2005, before the housing downturn began, roughly 18,000 mortgages in New England—about 1 percent of all mortgages—had a foreclosure initiated (see Table 1).[10] This annual figure was below the national level of around 1.6 percent (657,000) of all mortgages. Such foreclosure activity was fairly consistent in the preceding years of the housing crisis (see Figure 1). However, in 2006 the number of foreclosures in the region and the nation began to accelerate, nearly quadrupling to reach around 4 percent (73,877) in New England in 2009 and more than 5 percent nationwide (2.4 million).

Foreclosure rates have varied significantly across the region during the downturn, ranging from a peak of less than 3.0 percent in Vermont in 2010 to a peak of 5.5 percent in Rhode Island in 2009 (see Figure 1). While foreclosure activity across New England has dipped slightly from peak levels, more than 7 percent of all mortgage holders—nearly 133,000 homeowners—remained seriously delinquent in 2010 (see Figure 2). That is, they were more than 90 days past due on their mortgage, or languishing somewhere in the foreclosure process. That rate was slightly below the national rate of 8 percent. This combination of near-historic highs in foreclosure starts and a significant number of seriously delinquent households in the foreclosure pipeline indicates that foreclosures are likely to remain a major concern in the coming years.

With foreclosures at such elevated levels, it is important to understand why policymakers and the public should want to facilitate reasonable alternatives to foreclosure when possible. When homeowners experience foreclosure, the outcome not only affects households and

Table 1. Foreclosure Activity in the United States and New England, 2005–2010

Annual foreclosures started

	2005	2006	2007	2008	2009	2010
United States	657,087	791,649	1,278,991	1,924,187	2,391,515	2,183,355
New England	18,750	28,890	48,585	56,487	73,877	71,253
Connecticut	5,657	7,448	11,838	15,381	20,880	19,223
Maine	1,492	2,205	3,591	5,061	5,561	5,748
Massachusetts	7,876	13,184	22,887	22,230	30,490	29,777
New Hampshire	1,793	2,769	4,382	5,842	7,730	7,888
Rhode Island	1,307	2,498	5,021	6,879	7,528	6,844
Vermont	415	792	928	1,263	1,678	1,887

Source: Mortgage Bankers Association/Haver Analytics
Note: Foreclosures started refers to the total number of loans for which a foreclosure has been initiated during the year, that is, the number of loans sent to the foreclosure process.

lenders but can also pose significant negative externalities on communities and state and local governments. At the household level, not only do families lose what is typically their largest investment. The disruption can also lead to housing displacement or homelessness, economic shocks such as impaired credit, untenable work situations, and significant stress, affecting family relationships and personal well-being.[11] Foreclosures also impose a number of costs on lenders, such as forgone mortgage payments, the costs of maintaining the property, legal fees and services, and declines in resale values.[12]

In neighborhoods and communities, foreclosures drag down property values, lead to abandoned and unkempt properties, and raise crime rates, factors that increase the risk of more foreclosures.[13] The effects on state and local governments are far reaching as well, and include lost revenues from a shrinking property tax base, growth in demand for services for displaced families plus police and fire protection for abandoned properties, and potentially significant pressures on court systems—squeezing budgets on both the revenue and spending sides.[14]

Given these financial and social costs, it is in the interest of all parties to mitigate such effects and find alternative solutions for preventable foreclosures.[15] Unfortunately, homeowners and lenders are typically unable to agree on alternatives on their own, even when doing so is in the best interests of both parties.

This risk of impasse opens the door to foreclosure prevention programs and policies that can facilitate more desirable outcomes. As a last line of defense, such efforts can keep homes in productive use, mitigating both the direct effects on homeowners and lenders and the indirect effects on communities and governments. Measures may include modifying the terms of a mortgage, providing financial assistance to allow homeowners to stay in their home, or enabling them to exit the home without being foreclosed upon. The latter agreements are referred to as "graceful exits" and include options such as cash for keys, a short sale, or a deed in lieu of foreclosure.

However, policymakers face considerable constraints in funding foreclosure prevention efforts, given that the economic downturn has decimated state and local budgets. Policymakers must closely weigh the costs and benefits of foreclosure prevention efforts against those of other programs and services already on the chopping block. Still, recent foreclosure prevention efforts in New England and across the country show that states and municipalities can find effective ways to mitigate foreclosures.

Foreclosure mediation programs

Simply put, mediation is the process by which a neutral third party, a mediator, helps a homeowner and a lender in the foreclosure process try to negotiate a voluntary settlement. By getting both parties to talk, the mediation process provides a channel of communication that has eluded most borrowers who attempt to contact lenders on their own.[16] By providing this channel of communication, mediation programs try to find alternatives to foreclosure that are mutually beneficial to both parties, such as modifying the mortgage terms allowing the homeowners to stay in their home or allow the homeowners to vacate the home through a graceful exit. Mediators also review homeowners' eligibility for local, state, and federal foreclosure prevention resources.

Mediation programs have the potential to play a role in a majority of foreclosures and assist in nearly all residential cases, given that they typically mediate cases for any homeowner with a one- to four-unit primary residence that is at risk of foreclosure. This contrasts with more targeted foreclosure prevention programs that offer financial assistance to homeowners, which often set strict mortgage, credit, or income requirements (see the next section). Mediation programs also often incorporate many positive features that reduce foreclosure rates: they may try to intervene early, or to provide legal aid and counseling to homeowners, for example.[17]

Nationwide, only five states had some form of foreclosure mediation program in 2008—in some cases spearheaded by cities or counties. However, as early programs such as those in Connecticut and Philadelphia produced promising results, mediation became a popular prevention strategy, with 21 states and the District of Columbia having created a program by the start of 2011.[18]

Five of the six New England states have some form of mediation program—all except Massachusetts (see Table 2). Following Connecticut's program, New Hampshire and the city of Providence, Rhode Island, created mediation programs in 2009.[19] Maine, which had a pilot program in York County in the latter half of 2009, implemented a statewide program in early 2010. Vermont became the latest New England state to implement a statewide program in July 2010.

The foreclosure mediation process

Although all these programs share similar aspects, the mediation process varies significantly by state. Once a lender initiates a foreclosure in accordance with state law, homeowners receive information on the availability of mediation and other resources, such as housing counseling and pro bono legal services, along with the foreclosure notice. Information on the mediation process ranges from notification that a mediator will be contacting the homeowners (Providence), to forms that allow them to request mediation (Vermont), to requests for information so the state can screen the homeowners' eligibility for mediation (Connecticut and New Hampshire). Maine includes the foreclosure and mediation notice on the same form, thus minimizing paperwork.

Table 2. Foreclosure Mediation Programs in New England, as of 2011

	Judicial Foreclosure			Non-Judicial Foreclosure	
	Connecticut Foreclosure Mediation Program	**Maine Foreclosure Diversion Program**	**Vermont Foreclosure Mediation Program**	**New Hampshire Foreclosure Mediation Program**	**Providence[1] Foreclosure Ordinance**
Program administration	Judicial branch	Judicial branch	Judicial branch	Office of Mediation and Arbitration, judicial branch	Rhode Island Housing
Date program took effect	July 1, 2008	January 1, 2010	July 1, 2010	August 25, 2009	July 1, 2009
Homeowner enrollment	Automatic if homeowner returns form	Automatic if homeowner returns form; can opt out	Homeowner opts in	Voluntary	Automatic
Funding	$5 million from State Banking Fund	Administrative filing fee paid on all foreclosures	Lender pays mediation fee	Grant funds ($60,000)	Lender pays mediation fee
Length of mediation[2]	60 days[3]	90 days[4]	180 days	No time limit	60 days
NPV calculation[5]	No	FDIC	HAMP	No	No
Reporting of results	Periodic report on outcomes	Annual report to legislature	Participant survey	No	No

Source: Administrators of state foreclosure mediation programs

Notes:
[1] Cranston and Warwick, Rhode Island, have adopted ordinances similar to the one in Providence.
[2] From initiation of the mediation process to completion.
[3] The court may order a 30-day extension.
[4] Both parties can agree to an extension, or the court may order an extension owing to delays by lender.
[5] NPV = net present value. These calculations are used to determine if a modification that allows the homeowner to stay in their home is of benefit to a lender. Maine's mediation program uses the Federal Deposit Insurance Corporation's NPV calculation, while Vermont uses the HAMP calculation.

If homeowners respond to the foreclosure action or mediation forms, a mediator initiates the scheduling of the mediation proceedings (see Box 1 for information on state approaches to designating mediators). Providence automatically schedules all qualifying foreclosure actions for mediation, while Connecticut and Maine schedule all qualified homeowners who respond to the foreclosure action.[20] Maine goes a step further by requiring homeowners to sign a waiver if they want to opt out of mediation. In Vermont, homeowners opt in to the mediation program by returning the request to schedule mediation, and the lender must then participate.[21]

On the other end of the spectrum, New Hampshire requires both homeowners and lenders to voluntarily agree to participate for mediation to occur. The homeowners' request for mediation is sent to the lender, who evaluates their eligibility for federal foreclosure prevention programs and determines whether mediation is appropriate. If the lender finds that the borrowers are not eligible for mediation, it notifies them and the program administrator, and the process ends. If the lender deems the homeowners eligible, it notifies the state Office of Mediation and Arbitration—part of the judicial branch—which schedules the mediation. In New Hampshire, homeowners can also request mediation before receiving a foreclosure notice, which allows for earlier intervention than most programs.

Once mediation is scheduled, the parties agree to act in "good faith" by providing all the information the mediator requests in a timely fashion.[22] The mediator typically requests financial information from the borrowers, such as household income and expenses, and information on the terms of the mortgage and payments past due from the lender.[23]

Maine also requires lenders to prove their rights to the property by submitting copies of mortgage notes and deeds. In Vermont and Maine, mediators use information from borrowers and lenders to calculate the net present value (NPV) of a mortgage modification. These calculations compare the cost of various mortgage modifications that would allow the homeowners to stay in the home against the cost of the existing mortgage terms under a number of foreclosure scenarios to determine if a modification would be beneficial to the lender.[24] Such calculations provide mediators with a starting point to examine alternatives to foreclosure.

Before proceeding to mediation, some states and localities also require homeowners to participate in a pre-mediation meeting. In Providence, homeowners must meet with a housing counselor to review financial information and develop proposals for foreclosure alternatives to explore during mediation. Maine requires some homeowners to attend an informational court session to learn what to expect during the mediation process, and about counseling and legal resources.[25]

Box 1
Who mediates?

Although all foreclosure mediation programs rely on neutral third parties, who actually conducts the mediation varies greatly. In Connecticut, the mediation program is centralized in the judicial branch, and all mediators are judicial employees trained in mediation and foreclosure laws, and in local, state, and federal foreclosure resources and programs.

Maine, New Hampshire, and Vermont also administer their programs through the judiciary, but contract out mediation to individuals who meet certain standards, and who complete specialized state foreclosure training programs. In Maine and Vermont, these continuing education programs keep mediators up to date on the latest foreclosure prevention resources and methods.

Rhode Island relies on one mediator, referred to as a "conciliation coordinator," to mediate all cases.[A] The program can function with only one mediator because housing counselors play a larger role in the program and develop proposals for alternatives to foreclosure, lessening the need for constant oversight by the mediator.

Although no one approach is necessarily the best, all such programs should have enough trained and knowledgeable mediators to avoid forcing homeowners and lenders to wait for overbooked mediators, which bogs down the process.

After the mediator has gathered all required information, and the borrower and lender have completed any pre-mediation requirements, they meet for the mediation session(s) to consider alternatives to foreclosure. These solutions may allow homeowners to stay in their home, such as through a modified or refinanced mortgage, loan repayment plan, forbearance plan, or partial claim; provide a graceful exit, such as cash for keys, a short sale, or a deed in lieu of foreclosure; or qualify the homeowners for local, state, or federal financial assistance programs such as HAMP.

If both parties agree on a solution, the foreclosure proceeding is stopped. If the homeowners and lender fail to reach an agreement, the foreclosure process continues according to state law. In Connecticut, Maine, and Vermont the mediator files a report indicating the end result of mediation, and whether the parties complied with program requirements and acted in good faith. In Maine and Vermont, the mediator's report also includes results of the NPV calculations.

In Providence, if the parties do not agree on a solution, the lender must provide a written explanation showing that it complied with program requirements. If the mediator accepts the explanation, the lender receives a certificate of "good faith effort" to file with the recorder of deeds, and may proceed with foreclosure. In New Hampshire, the mediator files a report simply indicating whether the parties reached an agreement.

These state-to-state variations largely reflect differences in state foreclosure laws and resources. The next sections show how these programs arose, and how their structures may affect their outcomes (see Table 2).

State foreclosure laws: lender participation

A state's foreclosure law largely determines the structure of a state's foreclosure mediation program. Although foreclosure laws vary widely across states, these typically fall into one of two categories: judicial and statutory (also known as non-judicial). In judicial states, foreclosures proceed as civil lawsuits between lenders and homeowners, with a judge overseeing the proceedings and making a ruling. In a non-judicial process, lenders do not need to file a complaint with a court to foreclose: they simply need to follow state statutes.

Judicial foreclosure regimes are generally considered more borrower-friendly, as they give homeowners more time to correct a default and more opportunities to contest a foreclosure. In non-judicial states, defaulting homeowners can legally contest a foreclosure only by filing a lawsuit to stop the sale or filing for bankruptcy—both costly and unattractive options.[26] Across the country, states are split fairly evenly between judicial and non-judicial foreclosure regimes. However, 16 of the 21 states with mediation programs have a judicial process.[27]

New England's three judicial states—Connecticut, Maine and Vermont—all have mediation programs. As judicial foreclosures require court oversight, these programs capitalize on this legal infrastructure: foreclosures cannot proceed if lenders do not comply with mediation requirements. If participants do not reach an alternative to foreclosure, courts can review the mediator's report to ensure that they did comply. If a judge finds that a lender did not participate in good faith, the judge can impose sanctions ranging from fines and penalties to the dismissal of the foreclosure action. Dismissal is uncommon. However, in the first year of Maine's program, courts dismissed four foreclosures.[28]

Two of the three non-judicial New England states—New Hampshire and Rhode Island—also have foreclosure mediation programs. (See Box 2 for information on Massachusetts.) However, as noted, New Hampshire's program is completely voluntary, and provides little incentive for lenders to pursue alternatives to foreclosure more often than they did in the absence of the program.[29] In Providence, although the city automatically schedules mediation, lenders can foreclose without completing the mediation process by paying a $2,000 fine to the recorder of deeds.[30]

Although lenders' incentives to participate in such programs are somewhat limited, non-judicial states have used the threat of court

Box 2
The Massachusetts 150-day "Right-to-Cure" statute

The non-judicial foreclosure states of California, Michigan, and Oregon have created negotiation programs as an alternative to mediation.[B] Like mediation, these programs contact homeowners early in the foreclosure process, provide counseling and legal services, and facilitate conversations between lenders and homeowners. However, the negotiation process does not include a neutral third party. Foreclosures do not move forward until the lender files a statement of compliance with the negotiation process.

Massachusetts, also a non-judicial foreclosure state, has attempted a similar experiment. Before August 2010, delinquent homeowners had a 90-day "right to cure," during which they could prevent foreclosure by paying off all past-due mortgage amounts. If homeowners did not make the mortgage current after 90 days, the remaining principal and interest became due, and lenders could begin the foreclosure process. In August 2010, the legislature approved a 150-day right to cure, although lenders can reduce that to 90 days if they have at least one in-person or telephone meeting with homeowners to negotiate a reasonable alternative to foreclosure.[C] Lenders must also assess borrowers' income and expenses, and consider the costs and benefits of a loan modification by completing an NPV calculation.

To proceed with an early foreclosure, the lender must provide an affidavit to the homeowners and Massachusetts Land Court. The affidavit attests to the time and place of the meeting, participating parties, the relief (if any) offered to the borrowers, a summary of the NPV calculation, including the information used in the calculation, and certification that any offered options comply with federal law.

Although negotiation programs resemble mediation programs, it is unclear how successful they have been because most do not report on outcomes. However, given that a major barrier to finding alternatives to foreclosure has been a lack of communication between homeowners and lenders, a program that limits the length of the foreclosure process seems unlikely to spur lenders to communicate directly with borrowers to find such alternatives.

sanctions to ensure lender participation. For instance, in 2009 the Nevada legislature created a mediation program administered by the state judicial branch: if homeowners facing a foreclosure action request mediation, lenders must participate.[31] If they do not, the borrowers or the mediator can request a judicial review, which can lead to court sanctions.[32] This may partially explain why Nevada has reported more successful mediation outcomes than any other non-judicial foreclosure state.

Voluntary, opt-in, or automatic: homeowner participation rates

While ensuring that lenders participate is crucial to successful foreclosure mediation, so is convincing homeowners to join the process. Homeowner participation in opt-in programs across the country tops out at around 20 percent (Nevada), according to the Center for American Progress, while programs with automatic enrollment attain 70 percent participation (Philadelphia).[33]

These rates mirror those of well-documented programs in arenas other than foreclosures. For example, organ donation programs[34] and retirement accounts[35] that require individuals to opt in have participation rates well below 50 percent. Programs that automatically enroll participants but allow them to opt out have participation rates well above 50 percent.

The two mediation programs in New England that release data report similar levels of participation. Since the inception of Connecticut's program, the state has seen 46,425 foreclosure actions, of which 20,286 have proceeded to mediation, a 44 percent participation rate. However, the participation rate among qualifying residential households is estimated to be near 70 percent, as not all these actions involved one- to four-unit primary residences.[36]

The 2010 report on Maine's mediation program provides only total foreclosure filings (5,409) and the number of cases that engaged in mediation (983) from January 1, 2010 to December 31, 2010—a participation rate of 18 percent. However, the true participation rate likely is much higher, because some of the filings did not qualify for mediation. Further, there is an initial lag between the effective start date of a mediation program and when mediation sessions actually begin. In Maine, mediation sessions did not begin until May 2010. Maine's participation rate is also likely to improve over time, as participation rates tend to rise as programs overcome initial hurdles and become more entrenched in the foreclosure process.

If they do not bring homeowners to the table, it is difficult for mediation programs to prevent foreclosures. Designing mediation programs to ensure adequate homeowner participation is a key step. Beyond design, it is also important to accurately capture the participation rates of qualifying homeowners. By tracking such rates, policymakers can better understand a program's successes and shortcomings.

Length of mediation: striking a balance

If a mediation program is able to get both homeowners and lenders to participate, then the challenge becomes determining the correct length for the process.[37] The mediation timeline needs to be long enough to allow participants to provide and check financial information and explore alternatives. Yet if mediation simply prolongs the foreclosure process, it will burden lenders with the cost of forgone mortgage payments, households will be left in stressful limbo, courts will be backlogged with mediation cases that have not reached resolution, and financially strapped homeowners with limited ability and incentives to maintain their property will let property values decline.

Of course, mediation could also speed up the foreclosure process and reduce caseloads by shepherding cases out of the foreclosure pipeline and into alternatives that allow residents to stay in their home or make a graceful exit. The foreclosure mediation program of Cuyahoga County, Ohio, is the only one that reports on the impact of mediation on the duration of foreclosures. This program found that foreclosure cases in which borrowers participated in mediation lasted an average of slightly more than six months, while cases in which borrowers did not participate in mediation averaged nearly 12 months.[38]

In New England, the length of the mediation process appears to have little or no effect on the length of the foreclosure process. A drawn-out process is unlikely to occur in New Hampshire and Providence because lenders can leave the process at any time, and are unlikely to remain in mediation beyond the date on which foreclosure can legally proceed.[39]

In New England's judicial foreclosure states, the mediation process does not halt the foreclosure proceedings, as homeowners still need to respond to the foreclosure complaints. These states therefore require participants to complete mediation within the timeframe of the foreclosure process, ranging from 60 days in Connecticut to 180 days in Vermont.[40]

However, there are exceptions where mediation can be extended when necessary. For example, in Connecticut, the mediation process can be extended 30 days if the mediator files a report citing a need for more sessions. In Maine, mediation can be extended beyond the 90-day timeframe if both parties agree to such an extension, or if delays by the lender compel it.[41] By requiring participants to complete mediation within the state's legal framework but also allowing for extensions when needed, these states give participants time to explore alternatives without delaying the process unnecessarily.

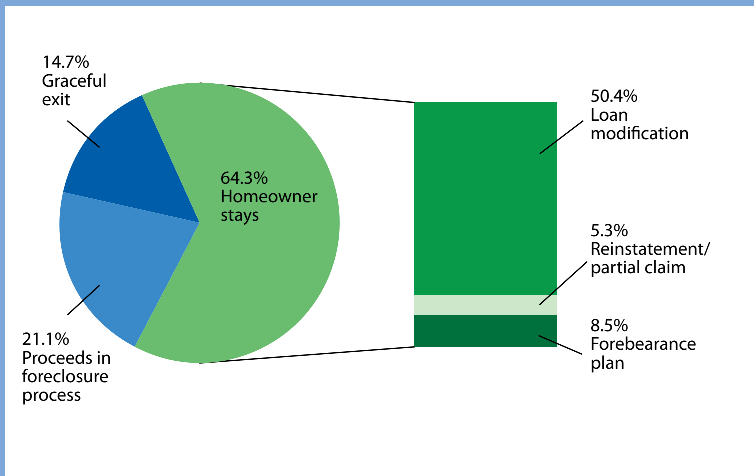
How is mediation funded?

Designing mediation programs to maximize homeowner and lender participation and proceed in a timely fashion will be for naught if the programs lack the funds to process eligible foreclosures and provide sessions. Mediation programs have developed a number of funding mechanisms to overcome that hurdle.

The most popular approach to funding these programs is through fees—most often charged to lenders, as occurs in Providence and Vermont. Maine also puts the onus on lenders by charging them a $200 administrative filing fee to initiate all foreclosure actions, regardless of whether they will proceed to mediation. Some states, such as Nevada, require homeowners to match the lenders' contribution. However, there are drawbacks to levying fees on lenders and borrowers to finance foreclosure mediation programs. By placing the burden on lenders, programs with inadequate incentives to secure their

Figure 3. Results of Connecticut's Foreclosure Mediation Program

As of January 31, 2011



Source: Connecticut Judicial Branch of Statistics
Note: For definitions of terms, see Appendix A.

participation provide further incentive not to participate. And programs that levy fees on homeowners may discourage those who are already financially drained from participating in voluntary or opt-in programs.

Although fees are the more common form of funding, a number of programs have found other sources. In Connecticut, where mediators are judiciary employees rather than contracted, the program has less need for mediation fees. Instead, the state finances its program with $5 million from the State Banking Fund. This fund, in turn, relies on annual assessment fees collected from Connecticut's banks and credit unions by the state banking commissioner, and appropriated by the general assembly. New Hampshire's small-scale program is funded with $60,000 in grants from the state Housing Finance Authority and a private trust. At a cost of $400 per case, the program can provide mediation for just 150 foreclosure cases. Although these programs minimize disincentives for participation, their funding caps also limit the number of mediations that can occur.[42]

Analyzing the outcomes of mediation

Although the goal of foreclosure mediation is to find alternatives to foreclosure when possible, few programs report their results, so it is difficult to accurately gauge their success. Still, Connecticut provides some of the best and most regularly updated information on the outcomes of mediation. These data show that the process can be quite successful in finding alternatives to foreclosure (see Figure 3).

Of the 9,472 Connecticut homeowners who completed the mediation program as of January 31, 2011, 78.9 percent (7,478) avoided foreclosures.[43] Some 64.3 percent (6,086) stayed in their homes, and 50.4 percent (4,778) received a loan modification. Only 21.1 percent (1,994) of completed foreclosure mediation cases in Connecticut ended without a mutually beneficial alternative to foreclosure between borrowers and lenders, with these cases proceeding in the foreclosure process.

A number of other mediation programs have recorded similar success at finding alternatives to foreclosure, including those in Philadelphia (84 percent); Cuyahoga County, Ohio (61 percent); and Nevada (89 percent).[44] Of course, participation rates vary greatly across these programs, ranging from 20 percent in Nevada's non-judicial opt-in mediation program to 70 percent in Philadelphia's automatic-homeowner-enrollment program, which affects the number of cases that actually pursue alternatives to foreclosure.

Unfortunately, such high rates of success have not been universal. In the first 18 months of New Hampshire's program, participants have reached only 14 settlements among more than 100 mediation cases. This record mostly reflects the fact that mediation is voluntary: the program administrator has found it difficult to get lenders to participate.[45] In Maryland, also a non-judicial state, an opt-in program started in July 2010 has seen a participation rate of less than 10 percent. In that state, roughly one-third of cases that have completed mediation have found alternatives to foreclosure.[46] Many of Maryland's challenges also reflect its opt-in approach, as well as a lack of early intervention.[47]

The results from Maine's first year have been somewhat ambiguous. Of 505 cases that completed mediation, only 21 percent produced agreements for alternatives to foreclosure.[48] Nearly 55 percent failed to reach an agreement, and another 23 percent ended because homeowners did not attend mediation sessions. Further, only 98 foreclosure dismissals can be attributed to the mediation process, of which 62 (67 percent) were loan modifications (see Figure 4).

Unfortunately, Maine's program faces logistical hurdles in tracking whether mediation agreements lead to foreclosure dismissals.[49] For example, a loan modification typically goes through a trial period, during which the foreclosure action remains on the court docket. The foreclosure is dismissed only if the agreement leads to a permanent loan modification.

Mediation programs also tend to report lackluster results in their early stages—as is the case in both Maryland and Maine—as they deal with a backlog of foreclosures. Mediation program results tend to improve over time as they surmount initial challenges and become ingrained in the state foreclosure process.

Programs that track both participation rates and outcomes can better assess and expand their efforts. For example, as a result of tracking participation rates Connecticut changed its mediation program from allowing borrowers to opt in to automatically enrolling them in 2009 to improve participation rates as well as outcomes. As the program continued to report positive outcomes, the legislature allocated an additional $3 million on top of the initial $2 million from the State Banking Fund, and twice extended the program, first through July 1, 2012, and most recently through July 1, 2014.

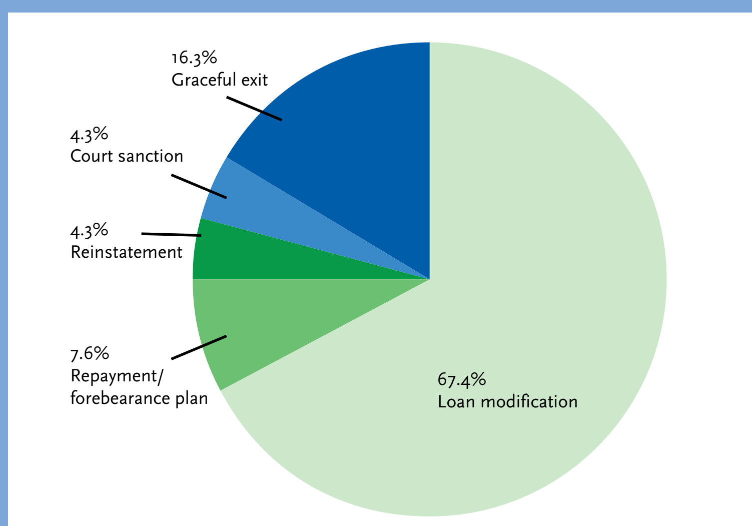
Results from mediation programs created early in the housing crisis have provided other states and cities with models, and allowed researchers to make policy recommendations. At a minimum, these programs reveal the importance of having a reporting requirement similar to Connecticut's to provide regularly updated data that allows officials to evaluate and adjust the programs as needed. Although officials need to weigh how best to use the limited funds devoted to mediation programs, dedicating a small portion to creating and updating a database would greatly enrich their ability to evaluate participation and outcomes—eventually producing better results.

Information on participation levels and outcomes also allows policymakers and researchers to assess how specific program attributes, such as opt-in provisions, affect the scale or effectiveness of foreclosure mediation. However, further information on the characteristics of homeowners and their mortgages, the types of loan modifications they receive, and what occurs after mediation are needed to better understand the long-term outcomes of agreements reached in mediation, such as which borrowers are likely to stay in their homes versus which are likely to default again and return to foreclosure.

Because programs lack such information, a number of questions remain regarding their success. Do most modifications that result from mediation occur through state programs or federal programs such as HAMP? As mediation results in a high rate of loan modifications, is it also leading to high redefault rate? Do homeowners who receive a modification, those who make a graceful exit, and those who proceed to foreclosure have different attributes?

Figure 4. Maine Foreclosure Dismissals as a Result of Mediation

As of December 31, 2010



Source: Maine Judicial Branch, Foreclosure Diversion Program
Note: This figure presents the outcomes of the 98 cases that completed mediation and had their foreclosure complaint dismissed. This does not represent the outcomes of all 107 cases that completed mediation with an agreement between parties, as an agreement does not guarantee foreclosure dismissal.

Some programs already have the tools to answer some of these questions, or have tried to do so. In Vermont, mediators report on the inputs used in NPV calculations, the outcomes of mediation, and the terms of any modification agreements. Because the NPV calculations require information on household income and expenses, and on the loan amount, interest rate, and amount past due, these calculations can shed light on who is benefiting from mediation. Reporting such inputs with mediation outcomes allows a richer understanding of who is benefiting from the program.

Philadelphia has actually reviewed the status of homeowners who reached an agreement with a lender to stay in their home as result of the city's foreclosure diversion program.[50] The review looked at the public record of agreements reached in the first 13 months of the program to see if homeowners still resided in their home 21 to 33 months later. The analysis found that more than 85 percent of homeowners who reached an agreement with their lender remained in their homes.

While this may not be the case for all programs, Philadelphia provides evidence that only a small number of homeowners who reach agreements in a mediation setting end up losing their homes. By pursuing similar evaluations, other mediation programs could obtain a richer picture of their long-term effectiveness in preventing foreclosures.

Foreclosure mediation summary

With many mediation programs reporting high levels of success in finding alternatives to foreclosure, these initiatives have become popular across the nation. The diverse funding options available to start such programs, their low cost relative to other foreclosure prevention programs, and their potential to reach nearly all homeowners at risk of foreclosure make them attractive options. A number of states and municipalities, including Massachusetts and Boston, are now considering creating such programs.[51]

The array of existing mediation efforts provides policymakers with models to consider when structuring their own programs. While states and municipalities have to work within their respective foreclosure processes and available resources, outcomes from existing programs point to designs that can lead to better outcomes.

Intervention: Programs should initiate the mediation process as early as possible, and complete it within existing legal timelines. This not only provides the maximum amount of time for parties to explore alternatives to foreclosure. By bolstering the chance that the mediation process will be completed in a timely manner, it mitigates many of the negative impacts of a drawn-out foreclosure process. However, programs should also allow mediation to be extended if needed, especially when lenders do not comply with the process. A combination of timeline-driven mediation and using extensions when warranted allows participants to explore alternatives while minimizing the chance of unduly prolonging the foreclosure process.

Participation: To ensure that all parties can explore alternatives to foreclosure, policymakers need to structure mediation programs to ensure their participation. A review of existing programs clearly shows that automatic enrollment or opt-out provisions for homeowners and threats of judicial oversight and sanctions for lenders improve participation rates. Because mediation is successful at finding alternatives to preventable foreclosures, maximizing participation among borrowers and lenders will likely mean avoiding more foreclosures.

Administration: Relying on the judicial branch in the foreclosure mediation process is an efficient use of resources, and an approach that most states, whether judicial or non-judicial, can replicate. Many mediation programs capitalize on a state's legal infrastructure to guide homeowners and lenders through the complicated foreclosure process and explore alternatives. While the judicial branch in non-judicial states does not play as integral a role in the foreclosure process, mediation programs in these states can still build on that resource, as New Hampshire and Nevada do.

Funding: States and municipalities need to carefully weigh the anticipated demand for mediation and the funding available to provide it. While the various sources used to fund mediation programs give policymakers options, they also impose a number of limitations. For example, a program that relies on fees from lenders, homeowners, or both can count on enough funding to provide mediation on the needed scale, as every foreclosure filing or mediation session provides revenue. However, if structured improperly, this fee-based approach can discourage lenders and homeowners from participating. Although programs that rely on special funds and grants minimize such disincentives, these constrained resources can limit the scale of mediation.

Results: To expand their impact, foreclosure mediation programs need to collect and report data on participation rates and outcomes. Programs that have done so have improved participation rates and results while gaining public support and additional funding. Most programs already require mediators to file reports on outcomes. These programs can simply dedicate a small percentage of their funding to a central authority to analyze and disseminate results, as Connecticut does. Another low-cost option is to require mediation to include NPV calculations. Such calculations would provide robust statistics on the program while ensuring a transparent starting point for mediation participants.

Financial assistance programs

Foreclosure prevention strategies have mainly focused on modifying mortgages to reduce homeowners' monthly payments to affordable levels. These modifications typically extend the term of the mortgage or reduce the interest rate, while adding missed payments, interest, and fees to the principal (a process known as capitalization).[52] This means that most loan modifications typically do little to reduce the actual amount owed. In fact, a majority of loan modifications actually increase the principal amount due.[53]

As home prices have declined steeply, the number of homeowners with negative equity—that is, a mortgage value greater than the value of their house—has skyrocketed. Some analysts suggest that nearly a quarter of all U.S. mortgages are underwater.[54] Research has shown that negative equity alone does not lead to foreclosure. However, underwater homeowners who face an adverse situation—such as unemployment, death, a health crisis, or a divorce—are more likely to experience foreclosure.[55] The combination of a large number of underwater mortgages with homeowners losing their jobs or experiencing cuts in hours and pay, diminishing their ability to pay a mortgage, has produced high levels of delinquencies and foreclosures from the "double trigger" effect. Lenders have been reluctant to reduce principal amounts to lessen negative equity, and guidelines for loan modifications usually preclude a homeowner from obtaining a reduction large enough to compensate for a significant loss of income.[56]

During the housing downturn, states have developed financial assistance programs to help troubled homeowners avoid foreclosure. These programs are typically run by state housing finance agencies (HFAs), which specialize in affordable housing, first-time homebuyer assistance, and community development. As the housing crisis dragged on, HFAs expanded their role in state housing markets to assist vulnerable homeowners.

Early programs targeted subprime borrowers and—like federal mortgage modification programs—focused on adjusting the terms of mortgages to reduce monthly payments. For example, in 2007 MassHousing, the HFA in Massachusetts, worked with Fannie Mae to start HomeSaver, a program targeting victims of predatory lending who meet strict income, mortgage, and credit qualifications.

However, as foreclosures on homes with prime mortgages surpassed those on homes

Table 3. State Financial Assistance Programs to Prevent Foreclosures in New England, as of 2011

	Refinancing	Mortgage assistance	
	Connecticut Fair Alternative Mortgage Lending Initiative and Education Services (CT FAMLIES)	**Connecticut Emergency Mortgage Assistance Program (EMAP)**	**MaineHousing Home Ownership Protection for unEmployment (HOPE)**
Date program took effect	July 1, 2008	July 1, 2008	January 1, 2008
Administrator	Connecticut Housing Finance Authority (CHFA)	Connecticut Housing Finance Authority (CHFA)	MaineHousing
Program	1) Refinances existing mortgage to 30-year fixed-rate mortgage. 2) Offers a second mortgage that homeowners can use to pay closing costs, back taxes, and other arrearages, or to reduce mortgage principal (by up to $25,000) if there is a gap between the appraised home value and mortgage amount. 3) Requires completion of a financial counseling course.	1) Assistance with monthly mortgage payments for up to five years for homeowners facing foreclosure owing to a financial hardship beyond their control, as determined by CHFA. 2) Assistance comes as a loan to be repaid as a 30-year fixed-rate mortgage. 3) Interest and repayment begin when homeowners' financial hardship is resolved.	1) Assistance with mortgage payments for up to four months to Maine Housing borrowers who become involuntarily unemployed. 2) Assistance comes as an interest-free loan. 3) Repayment is deferred until borrowers pay off the mortgage or stop using the home as their primary residence.
Homeowner qualification	1) Delinquent on mortgage payments, or anticipate becoming delinquent. 2) Delinquency stems from financial hardship beyond homeowners' control. 3) Demonstrate that their loan payment history was current for six months preceding the onset of their hardship. 4) Household income is within CHFA limits.	1) History of no more than three late mortgage payments in a 12-month period over two years. 2) Delinquent or anticipate becoming delinquent owing to financial hardship beyond their control. 3) Demonstrate an ability to repay loan. 4) Mortgage is not insured by the Federal Housing Administration.	1) Approved for state unemployment benefits. 2) Any delinquency is a direct result of unemployment. 3) Have made at least three consecutive on-time mortgage payments. 4) Home's loan-to-value ratio ≤ 100% 5) Unavailable for any job loss protection through private mortgage insurance or government insurers.
Funding	$50 million for first mortgages from tax-exempt bonds sold in 1980s, and $4 million for second mortgages from the Downpayment Assistance Program revolving loan fund.	$5 million from State Banking Fund, with another $2.5 million for debt servicing on up to $50 million in CHFA bonds.	Funding allocated from Maine HOME Fund on an annual basis, determined by state and county unemployment.
Reporting of results	Periodic reports to CHFA board of directors	Periodic reports to CHFA board of directors	Updates to governor on request

Source: Connecticut Housing Finance Authority and MaineHousing

with subprime mortgages, some HFAs expanded their refinancing programs to assist these borrowers.[57] Only a few states, including Connecticut and Maine, went a step further to work explicitly with homeowners facing the root causes of recent foreclosures: negative equity and unemployment (see Table 3).

Such assistance can range from modifying a mortgage to provide more favorable terms to homeowners and stabilize their living situation while providing a loan to pay down arrearages or reduce negative equity, to providing temporary assistance with mortgage payments to help homeowners overcome a short-term hardship. To provide such assistance, HFAs purchase mortgages or provide loans to homeowners directly, eliminating the need to negotiate directly with lenders.

These programs tend to require substantial funding—a significant barrier to implementation. What's more, unlike mediation programs, financial assistance programs focus on helping troubled homeowners deemed most likely to avoid foreclosure with assistance; that is, those borrowers who meet specific criteria or experience certain kinds of financial hardships. These programs therefore help only a select group of homeowners.

Connecticut

In 2008 Connecticut enacted aggressive legislation to mitigate the impact of foreclosures through a number of programs, including the state's mediation program.[58] Two major financial assistance programs emerged from An Act Concerning Responsible Lending and Economic Security (Public Act 08-176). These programs were the Connecticut Fair Alternative Mortgage Lending Initiative and Education Services (CT FAMLIES), and the Emergency Mortgage Assistance Program (EMAP).

Connecticut Fair Alternative Mortgage Lending Initiative and Education Services

Originally aimed at helping homeowners with adjustable-rate mortgages (ARMs), CT FAMLIES is similar in many ways to other state-run mortgage refinancing programs. Run by the Connecticut Housing Finance Authority (CHFA), the program originally offered a 30-year fixed-rate loan to owners of primary residences who are delinquent on their ARM and meet CHFA income limits. The homeowners must complete a three-hour financial counseling class before closing on the new loan, and complete further counseling if they later become 60-days' delinquent.

However, CT FAMLIES differed from other refinancing programs at the time in that it offered a second mortgage of $15,000 to homeowners with underwater mortgages who would normally have trouble refinancing. By helping to bridge the negative equity gap—and cover any other costs that could lead to default, such as overdue mortgage payments, fees, past-due utility bills, and taxes—CT FAMLIES allowed such homeowners to refinance and stay in their home. As prime foreclosures picked up, the CHFA expanded the program to allow homeowners to refinance fixed-rate mortgages, and to provide assistance before they became delinquent. To bridge larger equity gaps, the CHFA also increased second mortgage loan limits to $25,000.

HFAs typically fund their programs through tax-exempt bonds that carry restrictions. For example, such bonds may fund only first-time buyers and those who meet certain income guidelines and loan limits, and they cannot typically be used for refinancing or purchasing mortgages. However, Connecticut used unique funding sources to create a multimillion-dollar foreclosure prevention program in a time of tight budgets. The state allocated CT FAMLIES $50 million in tax-exempt bonds from the 1980s—known as Pre-Ullman bonds—which did not carry the restriction of current HFA bonds.[59] This allowed the CHFA to refinance and purchase existing mortgages under looser income and loan restrictions.[60] The state also tapped a revolving loan fund to provide a further $4 million for second mortgages used to bridge negative-equity problems.[61]

From July 1, 2008, to January 31, 2011, CT FAMLIES purchased 114 mortgages worth $22.9 million, or an average of slightly more than $200,000 per mortgage.[62] The program also provided 30 second mortgages totaling $384,000, for an average of $12,800.[63] The program essentially used half its funding during its first two and a half years.

The state initially relied on the Federal Housing Administration's Secure program to insure CT FAMLIES mortgages.[64] However, that program shut down at the end of 2008, significantly affecting the ability of CT FAMLIES to purchase mortgages. In 2009 the CHFA's board of directors authorized the agency to insure CT FAMLIES mortgages. The program purchased only 13 first mortgages and provided just 5 second mortgages during this transition period. However, later rule changes allowing the agency to refinance fixed-rate mortgages, remove the delinquency requirement for assistance, and increase second mortgages spurred a significant uptick in activity in 2010, when the agency recorded 39 first mortgages and 11 second mortgages.

As of January 2011, another 79 mortgages totaling $14.8 million were in the purchase pipeline. At this pace, the program could potentially commit all its funds by the end of 2011.

Emergency Mortgage Assistance Program

While CT FAMLIES was developed in response to the current housing crisis, EMAP is a revived and revamped mortgage assistance program originally created to help homeowners facing temporary financial hardship during the housing downturn in the early 1990s. The program was not funded from 1995 until 2008, when the Connecticut legislature refunded the program through Public Act 08-176.

EMAP now provides temporary assistance with monthly mortgage payments for up to five years to eligible homeowners who are facing foreclosure owing to financial hardship due to circumstances beyond their control. These can include a significant reduction in household income or an increase in expenses, as determined by CHFA.[65] As with CT FAMLIES, homeowners who anticipate becoming delinquent are eligible for EMAP. To receive assistance, homeowners must have a good credit history prior to their hardship, have made regular mortgage payments in the past, and show the ability to repay assistance in the future.[66]

Connecticut provided $7.5 million from the State Banking Fund to revive the program—the same source used to fund the state's foreclosure mediation program. Of this amount, the state earmarked $5 million for a revolving loan fund to provide assistance to homeowners. This assistance comes in the form of a 30-year fixed-rate mortgage to be repaid when the homeowners' financial condition improves or the house is sold. Homeowners who receive assistance are evaluated annually to determine whether they need continued assistance or if repayment should begin. The state allocated the remaining $2.5 million for debt service payments to the state treasurer, so CHFA could issue up to $50 million in bonds to keep the revolving loan fund capitalized.[67]

When the program resumed in 2008, EMAP defined financial hardship strictly: homeowners needed to have lost 25 percent of their income to qualify. Only 6.7 percent of applicants (36) were approved for assistance the first year. It quickly became apparent that a modest drop in income or a steep increase in housing expenses could lead to delinquency. Thus, in July 2009, the state loosened the restrictions to allow the CHFA to determine whether a financial hardship was the cause of a mortgage delinquency, including an unanticipated rise in housing expenses. The application approval rate rose to 17.6 percent over the next 12 months, and the number of loans quadrupled to 156.[68] As of January 31, 2011, EMAP had received 2,500 applications and made 342 loans.[69]

Among these borrowers, 41 did not need assistance with monthly payments: instead they used the funds to make their mortgage current, averaging $28,385 per loan. Another 183 homeowners received monthly mortgage assistance averaging $940 a month, and an initial disbursement averaging $20,204 to bring their mortgage current. After the annual recertification of 108 homeowners receiving monthly assistance, 68 saw their monthly assistance fall by an average of $303, 25 saw their assistance increase by an average of $216, eight began repaying their EMAP loans, and seven no longer required assistance but have not yet begun to repay their loan.

Maine

As the recession hit Maine and the state's employment situation deteriorated, MaineHousing, the state HFA, saw a rise in delinquencies owing to job loss and responded by creating the Home Ownership Protection for unEmployment (HOPE) program in January 2008. Modeled on North Carolina's Home Saver Program, Maine HOPE provides assistance for up to four monthly mortgage payments, including taxes and insurance, to MaineHousing borrowers whose delinquency is the direct result of involuntary unemployment.[70]

To qualify, homeowners also need to have received state approval for unemployment benefits, among other requirements (see Table 3). The program also essentially bars underwater homeowners by restricting assistance to those whose home has a loan-to-value ratio of less than 100.[71] This means Maine HOPE could potentially exclude the homeowners most likely to default on their mortgage: those subject to the "double trigger" effect.

Like other financial assistance programs, Maine HOPE relies on a unique funding source, the Housing Opportunities for Maine (HOME) Fund. To finance Maine's affordable housing initiatives, the legislature created the HOME Fund in 1983 by doubling the real estate transfer tax and dividing its revenues between the state's general fund and the HOME Fund.[72] MaineHousing used this funding to allow Maine HOPE to help MaineHousing borrowers survive tough economic times. Exact funding for the program is determined annually, based on the state and county employment situation.

Assistance comes in the form of an interest-free mortgage to be paid back when the primary mortgage matures or the homeowner sells the house. As of the end of 2010, Maine HOPE had assisted 257 borrowers with an average loan of $3,150. Nearly 232 borrowers—90 percent of those who received assistance—have resumed mortgage payments and avoided foreclosure.[73]

Financial assistance summary

By targeting a specific group of vulnerable homeowners, financial assistance programs directly help those borrowers most likely to be foreclosed upon in the current housing market. These programs circumvent the challenge of negotiating with lenders by purchasing mortgages or providing assistance directly to homeowners. Financial assistance programs can adjust the mortgage terms to make them more affordable to struggling homeowners while providing additional funding to allow those experiencing temporary hardship to get back on their feet. Although limited in number, financial assistance programs in New England provide key insights into effective foreclosure prevention strategies.

Intervention: Allow homeowners to apply for assistance before they become delinquent, to stop preventable foreclosures while preserving the program's funding. As with mediation, the key to preventing foreclosures is assisting borrowers as early as possible. Changes that allowed CT FAMLIES and EMAP to assist borrowers at risk of becoming delinquent have enabled these programs to help even more homeowners. Assisting borrowers before delinquency can also mitigate the long-run costs of the program, as getting to borrowers in more manageable financial conditions will require less financial assistance to get them back on sound footing.

Flexibility: Enable financial assistance programs to be flexible in responding to the causes of foreclosures. EMAP's initial strict income-loss provision of 25 percent was a major barrier to providing assistance to homeowners experiencing less severe but still serious financial hardship. Similarly the focus of CT FAMLIES on refinancing ARMs proved too narrow, as foreclosures on homes with fixed-rate mortgages soared. The flexibility built into these programs enabled them to adapt to the changing causes of foreclosure and assist troubled homeowners to avoid foreclosure.

Administration and results: The on-the-ground knowledge and ability of state HFAs to track results has allowed assistance programs to respond to the changing needs of the most vulnerable homeowners. By relying on established players in state housing and mortgage markets, financial assistance programs can monitor economic conditions closely, assess the challenges borrowers face, and determine the best course of action.

Challenge of funding: Although financial assistance programs have many positive attributes, states that lack unique funding sources are unlikely to create such programs in the current environment of fiscal austerity. The few states that have enacted financial assistance programs have tapped unique funding sources, such as the Maine HOME Fund and the Connecticut State Banking Fund. Although homeowners typically repay mortgage assistance over time, the initial challenge of providing funding for assistance programs has tended to outweigh their benefits. However, the federal government has shifted tactics in trying to prevent foreclosures, and is now providing funding directly to states to develop or sustain financial assistance programs, a move that may mitigate some of the concerns with implementing such policies (see Box 3).

Overall lessons for effective foreclosure prevention

The length and depth of the U.S. housing crisis has posed a broad set of challenges for policymakers. After a surge in subprime foreclosures in 2006, home foreclosures continue to weigh heavily on the housing market and affect the nation's economic recovery nearly five years later. With high rates of foreclosures expected to persist for at least several years, policymakers continue to look for solutions to this pervasive and corrosive

Box 3
Federal funding supplementing state mortgage assistance programs?

The federal government created two programs that provide funding directly to state HFAs, to help them develop foreclosure prevention programs or maintain financial assistance programs.

Hardest Hit Fund

To assist families in states hit hard by the housing and economic downturn, the Obama administration created the Housing Finance Agency Innovation Fund for the Hardest Hit Housing Markets (HHF) in February 2010. HHF provides $7.6 billion to HFAs in 18 states and the District of Columbia to design innovative, locally targeted foreclosure prevention programs. The hardest-hit states are those with unemployment rates at or above the national average, or whose housing prices have fallen more than 20 percent in the housing downturn.

With one of the nation's highest unemployment rates, Rhode Island received $80 million from HHF to develop a program administered by Rhode Island Housing. The agency created a mortgage assistance program for low- and moderate-income homeowners who experience financial hardship as result of unemployment or an unforeseen rise in expenses.[D]

Emergency Homeowners' Loan Program

To assist unemployed homeowners in the 32 states not covered by HHF, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 allocated $1 billion to the U.S. Department of Housing and Urban Development (HUD) to develop the Emergency Homeowners' Loan Program (EHLP). EHLP provides up to a $50,000, or up to 24 months of assistance, in the form of an interest-free loan to homeowners who experience a 15 percent or greater drop in income and are at risk of foreclosure.

HUD will provide assistance to homeowners relative to their state's share of unemployed homeowners, with homeowners in the five New England states eligible for assistance of up to $122 million.[E] In a limited number of cases, states with programs substantially similar to EHLP have received funding to provide emergency loans to borrowers and cover the cost of program administration. Connecticut—one of only five states to receive such funding—received $32.9 million to administer its own EHLP loans because EMAP is similar to EHLP.[F] Assuming similar need for EHLP loans to that of EMAP loans, the EHLP assistance could potentially help nearly 820 troubled homeowners.[G]

As HHF and EHLP are both in their early stages, the extent to which these programs will meet the demand for mortgage assistance across the states or supplement existing state mortgage assistance programs remains unclear. However, experience with Connecticut's EMAP program suggests that EHLP's strict income-loss provision may prevent states from assisting homeowners whose temporary financial hardship is not severe enough to qualify them but large enough to push them into delinquency. This shortcoming may be especially troublesome in states without a broader emergency assistance program, such as EMAP, to fall back on.

challenge. However, the economic downturn has left states with few resources to tackle the problem.

The most well-known efforts to prevent foreclosures have come at the federal level, as leaders have grappled with the changing scope of the crisis. However, while well intended, these efforts have fallen far short of the level needed, and have failed to curb the adverse effects of foreclosures on homeowners, lenders, communities, and local and state governments.

To further stem the foreclosure tide, many states have implemented their own prevention programs to help homeowners navigate the complicated and often convoluted foreclosure process, break down barriers to communication between homeowners and lenders, and target those most likely to face foreclosure. These programs provide important lessons for policymakers and administrators who create or oversee foreclosure prevention programs.

Intervene early. A key step in any successful foreclosure prevention strategy is reaching homeowners as early as possible. In the case of mediation, this means contacting homeowners when a foreclosure complaint is filed and facilitating conversations between lenders and borrowers early and often. Such efforts shepherd preventable foreclosures out of the pipeline, mitigating concerns about prolonging the foreclosure process.

Financial assistance programs should similarly allow homeowners to apply before their situation becomes dire. Adhering to that principle has allowed Connecticut's CT FAMLIES and EMAP to assist troubled homeowners before they no longer qualify for help while reducing the assistance they need to get back on their feet. ***Overall, by intervening early, prevention programs give homeowners, lenders, mediators, and HFAs time to explore alternatives to foreclosure, ultimately leading to better outcomes.***

Maximize participation. Experience with mediation programs clearly shows that successful policy prescriptions, such as opt-out provisions and automatic enrollment for homeowners and the threat of judicial oversight for lenders, bring homeowners and lenders to the negotiating table to find alternatives to foreclosure. In designing financial assistance programs, policymakers need to understand the circumstances that lead to delinquency and foreclosure. For example, a state seeking to provide mortgage assistance may want to evaluate the extent to which severe income shocks—as opposed to more modest shocks or rising housing expenses—are leading to foreclosures, before setting strict income-loss provisions, as Connecticut did with EMAP. ***To succeed, foreclosure prevention efforts must avoid creating barriers or disincentives to participation, and maximize the number of cases in which homeowners and lenders consider alternatives to foreclosure.***

Tap existing expertise. Given severe budget constraints, states have relied on existing resources to implement and administer their foreclosure prevention programs. Mediation programs have taken advantage of the judiciary's role in the foreclosure process, for example, while financial assistance programs have capitalized on the expertise of state HFAs in mortgage markets. ***Such efficient use of resources can help states launch effective programs quickly.***

Weigh funding strategies carefully. Foreclosure prevention programs that have emerged during today's housing downturn have relied on nontraditional funding sources, allowing states to take aggressive action despite severe budget constraints. For example, New England states have relied on lender fees, special funds, and public and private grants to implement an array of mediation and financial assistance programs. ***States and municipalities looking to develop or expand foreclosure prevention programs should carefully consider the benefits and costs of using a variety of funding options. These include the possible adverse incentives created by levying fees on homeowners and lenders, limits***

on program scale or design imposed by special funds and grants, and the availability of federal funding to supplement existing programs or create new ones.

Collect information and analyze results. Foreclosure mediation and financial assistance programs tend to be little understood. To quell concerns and gain public support, policymakers must provide concrete evidence of these program's effectiveness. Moreover, even the best-designed and implemented foreclosure prevention programs face unforeseen hurdles. Concrete evidence of their strengths and shortcomings, such as those provided by Connecticut's mediation and financial assistance program, can spur policymakers and administrators to make changes that produce better outcomes and lead to additional funding. ***Devising clear metrics for evaluating the success of foreclosure prevention programs—and an effective strategy for collecting and analyzing information on their outcomes—is essential to overcoming challenges.***

With the scale of foreclosures expected to remain at elevated levels, the need for an effective policy response remains urgent. Given tight fiscal conditions, policymakers will have to make tough decisions regarding the best options for addressing the challenges posed by foreclosures. By developing programs to find alternatives to preventable foreclosures, policymakers can attempt to mitigate some of the challenges foreclosures pose for homeowners, lenders, communities, and government. The policies reviewed here provide lessons that can help them design, implement, and administer successful programs. By applying these lessons—whether to mediation, financial assistance, or other foreclosure prevention programs—new and existing policies will be able to overcome many of the initial challenges that have hampered such efforts in the past and have a greater impact against the tide of foreclosures.

Endnotes

[1] In this report, "lenders" refers to entities with authority to modify the terms of mortgages, including banks and servicers.

[2] For a glossary of foreclosure terms and government programs mentioned in this report, see Appendix A.

[3] Eric S. Rosengren, "Asset Bubbles and Systemic Risk," remarks to the Global Interdependence Center's Conference on Financial Interdependence in the World's Post-Crisis Markets, Philadelphia, March 3, 2010.

[4] Realty Trac, "Record 2.9 Million U.S. Properties Receive Foreclosure Filing in 2010 Despite 30-Month Low In December," January 12, 2011.

[5] Sarah Bloom Raskin, "Problems in the Mortgage Servicing Industry," remarks to the National Consumer Law Center's Consumer Rights Litigation Conference, Board of Governors of the Federal Reserve System, Boston, November 12, 2010.

[6] Congressional Oversight Panel, *December Oversight Report: A Review of Treasury's Foreclosure Prevention Programs*, December 14, 2010.

[7] The report also identifies a number of other potential problems that would explain HAMP's shortcomings. These include the role of second mortgages; barriers that prevent homeowners from receiving modifications, such as unemployment and negative equity; and a failure to collect and analyze data that would explain HAMP's shortcomings.

[8] For an overview of state foreclosure prevention programs, see National Governors Association, "States' Foreclosure Response," http://www.nga.org/center/foreclosures.

[9] Kai-yan Lee, "Foreclosure Prevention and Intervention Efforts in New England," *New England Community Developments*, 2007 (4), Federal Reserve Bank of Boston.

[10] The data presented in this section are derived from the Mortgage Bankers Association's National Delinquency Survey. As of 2010:Q4, this data covered about 44 million first-lien mortgages on one- to four-unit residential properties. Based on analysis of Census Bureau and other industry data, the National Delinquency Survey is estimated to cover around 85 to 88 percent of the approximately 50 million loans outstanding in the market. Therefore, the information presented here is likely to understate the actual number of foreclosures. However, this data does allow for comparison of the scale of foreclosures across states. For further information on the National Delinquency Survey, see http://www.mbaa.org/ResearchandForecasts/ProductsandSurveys/NationalDelinquencySurvey.htm.

[11] For a discussion of the effects of foreclosure on families, see G. Thomas Kingsley, Robin Smith, and David Price, "The Impacts of Foreclosure on Families and Communities," Washington, DC: Urban Institute, May 2009; and Danne E. Davis and Minsun Shin, "The Lives of Sesame Street: The Impact of Foreclosure on Young Children and Families," *Contemporary Issues of Early Childhood* 10(2) (2009): 182–184.

[12] For a summary of the effects of foreclosures on lenders, see "Lenders' Cost of Foreclosure," Washington, DC: Mortgage Bankers Association, Congressional Education Series Briefing, May 28, 2008.

[13] For information on the effects of foreclosures on neighborhoods, see *REO & Vacant Properties: Strategies for Neighborhood Stabilization*, Federal Reserve Banks of Boston and Cleveland and the Federal Reserve Board, September 2010.

[14] For a discussion of the effects of foreclosure on state and local governments, see William C. Apgar, Mark Duda, and Rochelle Nawrocki Gorey, "The Municipal Costs of Foreclosures: A Chicago Case Study," Minneapolis: Homeownership Preservation Foundation, February 27, 2005.

[15] Preventable foreclosures are those foreclosures that can potentially be stopped through some alternative agreement. While not all foreclosures are preventable there is no exact definition of a preventable foreclosure. Some foreclosure prevention program explicitly target troubled homeowners that meet certain criteria as they believe with some assistance these foreclosures can be prevented. Examples of such are homeowners who become delinquent due to a temporary financial hardship beyond their control who could avoid foreclosure with limited financial assistance. Other preventable foreclosures can include situations where a homeowner and lender can find an agreement mutually beneficial to both parties. Sometimes a simple miscommunication between lenders and homeowners in the foreclosure process can be resolved by a conversation. Foreclosure prevention programs attempt to identify preventable foreclosures and facility alternative agreement when possible.

[16] For examples of the barriers facing homeowners, see William N. Lund, "Periodic Foreclosure Report Pursuant to PL 2009, Ch. 402," Gardiner: Maine Bureau of Consumer Credit Protection, October 15, 2010.

[17] J. Michael Collins and Maximillian D. Schmeiser, "Estimating the Effects of Foreclosure Counseling for Troubled Borrowers," Center for Financial Research, Federal Deposit Insurance Corporation, working paper no. 2010-06, June 2010.

[18] For a list of state and local foreclosure mediation programs, see Court ADR Resource Center's Foreclosure Mediation Program Models, at http://courtadr.org/files/ForeclosureMediationProgramModels.pdf; and the U.S. Department of Justice, Access to Justice Initiative, "Emerging Strategies for Effective Mediation Programs," http://www.justice.gov/atj/effective-mediation-prog-strategies.pdf.

[19] Providence created its mediation program by passing a city ordinance. In Rhode Island, Cranston and Warwick later adopted similar ordinances. This report focuses on the Providence program.

[20] Although these programs are automatic in essence, mediation is not automatically scheduled. If homeowners do not respond to the foreclosure complaint, they waive their right to mediation and judgment proceeds.

[21] In Vermont, mortgages subject to HAMP are eligible for mediation. Such mortgages are backed by Fannie Mae or Freddie Mac, or serviced by a lender participating in HAMP. A majority of mortgages qualify. HAMP also requires that qualifying mortgages apply to one- to four-unit homes that serve as homeowners' primary residence; that the homeowners received their mortgage on or before January 1, 2009; that their principal, interest, taxes, insurance, and homeowners' association dues total more than 31 percent of pre-tax monthly income; and that they owe $729,750 or less on their first mortgage for a one-unit property (limits are higher for two- to four-unit properties).

[22] Although definitions vary from state to state, "good faith" generally means that all parties comply with a mediator's requests in the allotted timeframe, provide information that is correct to the best of their knowledge, and do not intentionally delay or disrupt the mediation process.

[23] If loan servicing agreements or mortgage-backed securities (which pool mortgages, a process known as securitization) prohibit modifications, Vermont requires lenders to provide a copy of the agreement. Recent research has shown that securitization may not be impeding modifications as much as previously thought, given that modification rates for securitized and non-securitized mortgages are similar. See Sumit Agarwal, Gene Amromin, Itzhak Ben-David, Souphala Chomsisengphet, and Douglas D. Evanoff, "Market-Based Loss Mitigation Practices for Troubled Mortgages Following the Financial Crisis," Federal Reserve Bank of Chicago, WP 2011-03, 2011.

24 For an example of the inputs that NPV calculations require and how they work, see the Federal Deposit Insurance Corporation's NPV worksheet, http://www.fdic.gov/consumers/loans/loanmod/loanmodguide.html.

25 Other programs, such as the one in Philadelphia, hold a preliminary meeting to allow homeowners and lenders to work out a solution before they advance to third-party mediation.

26 In New Hampshire, if borrowers are granted an injunction to dispute a foreclosure, the judge can refer both the borrowers and lender to the mediation program.

27 Twenty states are considered judicial foreclosure states, while 29 plus the District of Columbia are considered non-judicial. Some states offer both judicial and non-judicial foreclosure, but they are typically assigned to the category that represents the majority of their foreclosures. Only North Carolina is not usually classified as either foreclosure regime, as its foreclosure procedure can have elements of both.

28 Maine Judicial Branch, Foreclosure Diversion Program, *Report to the Joint Standing Committee on Insurance and Financial Services*, 125th Legislature, February 7, 2011.

29 This design may be intentional, as funding for the program is limited, as discussed later in this report.

30 According to the Providence recorder of deeds, only one lender has paid a fine, and another is in litigation with the city over payment. E-mail correspondence with John A. Murray, recorder of deeds for the City of Providence, April 11, 2011.

31 For more information on Nevada's Foreclosure Mediation Program, visit the website at http://www.nevadajudiciary.us/index.php/foreclosuremediation.

32 For a discussion of state foreclosure laws and mediation programs, see Andrew Jakabovics and Alon Cohen, *It's Time We Talked: Mandatory Mediation in the Foreclosure Process*, Washington, DC: Center for American Progress, June 2009.

33 Alon Cohen and Andrew Jakabovics, *Now We're Talking: A Look at Current State-Based Foreclosure Mediation Program and How to Bring Them to Scale*, Washington, DC: Center for American Progress, June 2010.

34 Eric J. Johnson and Daniel Goldstein, "Do Defaults Save Lives?," Science 21(302) (2003): 1338–1339.

35 Brigitte C. Mandrain and Dennis Shea, "The Power of Suggestions: Inertia in 401(k) Participation and Savings Behavior," *Quarterly Journal of Economics* 116(4) (2001):1449–1187.

36 Anthony Klan, "States Try to Force Mortgage Workouts," *Wall Street Journal*, December 31, 2010.

37 The most common argument from lenders against foreclosure mediation programs is that mediation will further delay the foreclosure process. A prolonged process not only costs lenders missed mortgage payments, but the occupants' desire and ability to maintain the property while in foreclosure may be limited, so its value may deteriorate further. As the property is declining in value and delayed from returning to productive use, many of the negative side effects on communities may be exacerbated, making it difficult to sell the home when the foreclosure is completed.

38 Thomas J. Fitzpatrick IV and Joseph C. Ott, "Ohio and Pennsylvania: Two Approaches to Judicial Foreclosure Alternatives," *CR Report*, Federal Reserve Bank of Cleveland, Fall 2010. This estimate does not control for other factors that may affect the length of foreclosure proceedings.

39 The Providence program does have a 60-day timeline to ensure compliance with state foreclosure statutes.

40 Although Vermont has the longest mediation timeframe, it is the state's right-of-redemption period, during which borrowers can stop a foreclosure by paying off their obligations in full. Mediation therefore does not delay the foreclosure process.

41 Such extensions have produced more than 700 additional mediation sessions. See Maine Judicial Branch, Foreclosure Diversion Program, *Report to the Joint Standing Committee on Insurance and Financial Services*, 125th Legislature, February 7, 2011.

42 There are additional costs associated with foreclosure mediation that homeowners and lenders bear. This can include legal fees and services, time spent completing paperwork, attending court, and participating in mediation sessions. However, as the foreclosure process itself is somewhat costly, with many of these costs incurred in the foreclosure processes, the additional costs associated with mediation may be relatively small.

43 In the production of this report Connecticut released results for the mediation program through May 31, 2011. The results show similar success rates as those through January, with the May results showing slightly higher levels of success at finding alternatives to foreclosure as well as improvements in the participation rate.

44 Philadelphia VIP, "Mortgage Foreclosure Diversion Program: A VIP Case Study and Statistics," 2010; Thomas J. Fitzpatrick IV and Joseph C. Ott, "Ohio and Pennsylvania: Two Approaches to Judicial Foreclosure Alternatives," CR Report, Federal Reserve Bank of Cleveland, 2010; and Nevada Judiciary, "Number of Mediators Increased to Lead Foreclosure Mediations," October 28, 2010.

45 Shawne K. Wickham, "NH Foreclosure Mediation Program Sees Limited Success: 14 Settlements," *Union Leader*, July 16, 2011.

46 Gary Haber, "Few Marylanders Facing Foreclosure Seeking Mediation," *Baltimore Business Journal*, January 18, 2011.

47 Alan Cohen, "The Latest Mortgage Mediation Lesson: Maryland's Experience Points to the Way Forward," Washington, DC: Center for American Progress, January 19, 2011, http://www.americanprogress.org/issues/2011/01/mortgage_mediation_lesson.html.

48 Maine Judicial Branch, Foreclosure Diversion Program, *Report to the Joint Standing Committee on Insurance and Financial Services*, 125th Legislature, February 7, 2011.

49 To overcome such challenges, Maine is creating a database that will allow mediators to input information on each mediation case, giving the state up-to-date data and enabling it to better evaluate the program.

50 The Reinvestment Fund, "Philadelphia Residential Mortgage Foreclosure Diversion Program: Initial Report Findings," June 2011.

51 Legislators in Arizona, Hawaii, Missouri, Oregon, South Carolina, Tennessee, and Washington have also introduced bills proposing such programs.

52 For 2010:Q4, 91.6 percent of modifications involved capitalization, 84.1 percent involved reduced interest rates, and 56.1 percent extended the mortgage term. Only 2.7 percent reduced the mortgage principal, and 9.0 percent deferred a portion of the principal that incurs interest. See Office of the Comptroller of the Currency and Office of Thrift Supervision, *OCC and OTS Mortgage Metrics Report: Fourth Quarter 2010*, March 2011.

53 Conference of State Bank Supervisors, State Foreclosure Prevention Working Group, "Redefault Rates Improve for Recent Loan Modifications," Washington, DC: August 2010.

54 See CoreLogic, "U.S. Housing and Mortgage Trends," Santa Ana, CA: February 2011.

55 See Christopher Foote, Kristopher S. Gerardi, and Paul Willen, "Negative Equity and Foreclosure: Theory and Evidence," *Journal of Urban Economics* 64(2) (2008): 234–245.

56 Analysts are debating whether reducing the mortgage principal is an effective foreclosure prevention strategy. The 50 state attorneys general, working with federal agencies, have

proposed a settlement with major mortgage service providers regarding abusive foreclosure practices that would reduce the principal for underwater homeowners. For a discussion of the pros and cons of reducing principal, see Chris Foote, Kris Geradi, and Paul Willen, "The Seductive but Flawed Logic of Principal Reduction," *Real Estate Research Blog*, Federal Reserve Bank of Atlanta, March 9, 2011, http://realestateresearch.frbatlanta.org/rer/2011/03/seductive-but-flawed-logic-of-principal-reduction.html.

57 For a list of state financial assistance programs, see Tax Policy Center, "Mortgage Crisis: What Financial Assistance Have States Provided?," Washington, DC: http://www.taxpolicycenter.org/briefing-book/state-local/mortgage-crisis/financial.cfm.

58 This legislation also authorized the Home Equity Recovery (HERO) program, which refinances mortgages; and the Mortgage Crisis Job Training program, which provides employment services and job training to unemployed homeowners. For a review of programs in the legislation, see Soncia Coleman, "Foreclosure Prevention Programs in Public Act 08-176 and Public Law 110-289," Hartford: Connecticut Office of Legislative Research, September 9, 2008.

59 Pre-Ullman bonds are bonds issued prior to the date of enactment (April 24, 1979) or subject to a transition rule of the Mortgage Subsidy Bond Tax Act of 1979, the proceeds of which are used to make or finance mortgage loans for either owner-occupied single-family housing or residential rental housing for families. As a practical matter, these are housing bonds, issued, generally, before January 1, 1981 or the bonds issued to refund such bonds. As a result of being Pre-Ullman, single-family bonds do not have first-time homeowner, purchase price, income, targeted area, recapture, 10-year redemption, or many other requirements that otherwise apply to mortgage revenue bonds.

60 Some $70 million in these so-called pre-Ullman bonds initially seemed to be available: $40 million for CT FAMLIES, and $30 million for HERO. The state ended up allocating $40 million to CT FAMLIES and $20 million to HERO. After initial inactivity, the HERO program became HERO Expansion, a neighborhood stabilization program, with $10 million in pre-Ullman funding. CT FAMLIES has therefore used a majority of the funding allocated to the two programs.

61 The revolving loan fund is from CHFA's Downpayment Assistance Program, which is typically used to help first-time homebuyers.

62 Carol DeRosa, "CT FAMLIES, EMAP, & HERO Report to Mortgage & Board of Directors," Hartford: Connecticut Housing Finance Authority, February 24, 2010.

63 According to CHFA, as of December 31, 2010, 25 percent of borrowers with a first mortgage from CT FAMLIES had also received a second mortgage through the program.

64 FHA Secure allowed delinquent underwater borrowers to refinance if their delinquency stemmed from loan resets.

65 Qualifying reductions in income include: (1) unemployment or underemployment; (2) a loss, reduction, or delay in receipt of federal, state, or municipal benefits such as Social Security, Supplemental Security Income, public assistance, and government pensions; (3) a loss, reduction, or delay in receipt of private benefits, such as pension, disability, annuity, or retirement benefits; (4) a divorce or loss of support payments; and (5) disability, illness, or death. Qualifying increases in expenses include: (1) a significant increase in periodic payments required by the mortgage; (2) an unanticipated rise in housing expenses; and (3) expenses related to the disability, illness, or death of a family member.

66 Repayment begins when borrowers' total housing expenses, including the EMAP payment, equal 35 percent or less of monthly household income.

67 The program's finances are tied to state debt-servicing costs, and EMAP could be shut down if the state does not stay current on its debt payments.

68 Carol DeRosa, "CT FAMLIES, EMAP, & HERO Report to Mortgage & Board of Directors," Hartford: Connecticut Housing Finance Authority, July 20 and 29, 2010.

69 Of 340 loan approvals, 224 closed between July 1, 2008, and January 31, 2011.

70 MaineHousing borrowers are those with a mortgage through the Maine First Home Program. These are first-time homebuyers of one- to four-unit homes or condominiums who meet caps on income and loans.

71 The loan-to-value is based on the mortgage principal balance and the home's original purchase price or appraised value, whichever is lower.

72 The real estate transfer tax is split three ways: the county keeps 10 percent, and the remainder is split between the state's general fund and HOME Fund.

73 E-mail correspondence with Peter Merrill, director of the Communications and Planning Unit at Maine Housing, February 7, 2011.

Box endnotes

Box 1

A Rhode Island Housing, the state HFA, contracts with the conciliation coordinator, who has a mortgage-lending or servicing background and is knowledgeable about foreclosure laws, mediation, and resources.

Box 2

B In California, lenders must contact homeowners to initiate the first negotiation while advising them of their rights to request a second meeting. In Michigan and Oregon, lenders must notify homeowners of their right to discuss alternatives. If homeowners opt in to the negotiation process, lenders must participate.

C An Act Relative to Mortgage Foreclosure, passed August 7, 2010.

Box 3

D For an overview of Rhode Island's Hardest Hit Fund, see www.hhfri.org.

E Massachusetts is eligible for assistance totaling $61 million, Connecticut $32.9 million, New Hampshire $12.7 million, Maine $10.4 million, and Vermont $4.8 million.

F U.S. Department of Housing and Urban Development, "HUD Approves Connecticut's $33 Million Emergency Home Loan Program: State Expects to Take Applications in Early April," HUD No. 11-043, April 1, 2011.

G If demand for EHLP is similar to that for EMAP programs, some 150 homeowners would require an average initial payment of $28,385, for a total of $4.3 million. Another 670 homeowners would require an average initial payment of $20,204, plus average monthly assistance of $940, for a total of $28.6 million, if all borrowers required 24 months of assistance. The $32.9 million in EHLP funding would therefore assist a total of 820 borrowers.

Appendix A
Glossary of foreclosure terms

Adjustable rate mortgage (ARM)

A mortgage where the interest rate changes based on movements in an index rate, such as the interest rate on Treasury securities or the cost of funds index. ARMs usually carry a lower initial interest rate than fixed-rate loans, and have minimum and maximum rates. When interest rates rise, loan payments usually increase; and when interest rates fall, monthly payments may decrease. For further details, see *Consumer Handbook on Adjustable-Rate Mortgages,* Federal Reserve Board of Governors, http://www.federalreserve.gov/pubs/arms/arms_english.htm#arm.

Cash for keys

Homeowners agree to sign over ownership of their property and vacate it immediately in exchange for a cash settlement from the lender. This resolution prevents the lender from pursuing foreclosure.

Deed in lieu of foreclosure

Homeowners convey ownership of their property to the lender, which typically forgives some or all of their debt. This agreement allows the lender to avoid the cost of foreclosure and sell the property more quickly.

Emergency Homeowners' Loan Program (EHLP)

The Dodd-Frank Wall Street Reform and Consumer Protection Act provided $1 billion to the U.S. Department of Housing and Urban Development (HUD) to implement EHLP, which assists homeowners in states not covered by the Hardest Hit Fund (see Hardest Hit Fund). Under the program, state agencies and nonprofits offer eligible borrowers a zero-percent-interest "bridge loan" of up to $50,000, to help them pay the mortgage principal, interest, insurance, and taxes for up to 24 months. HFAs that run assistance programs determined by HUD to be substantially similar to EHLP receive funds to make emergency loans to borrowers and cover administrative costs. See http://www.hud.gov/offices/hsg/sfh/hcc/ehlp/ehlphome.cfm.

FHA Secure

A program designed to help homeowners lower their monthly payments, avoid default, and protect their investment. The program targeted homeowners with current or delinquent adjustable-rate mortgages not issued by the Federal Housing Administration (FHA). Homeowners had to show that their delinquency stemmed from rising interest rates, and that they had dependable income and could make mortgage payments. The program ended in 2008.

Forbearance plan

An agreement that allows homeowners to make less than the full monthly mortgage payment, or to pay nothing at all, for a given period. A lender may consider forbearance when homeowners can show that a bonus, tax refund, or other future income will allow them to make their mortgage current, or qualify them for a repayment plan or loan modification.

Graceful exit

An agreement in which the lender allows a delinquent homeowner to exit the home without going through foreclosure. Such agreements include cash for keys, a short sale, or a deed in lieu of foreclosure.

Hardest Hit Fund (HHF)

Established in February 2010, HHF provides targeted aid to families in states with unemployment rates at or above the national average, or in states where home prices have dropped more than 20 percent. Each state housing agency gathered public input to devise programs designed to meet distinct challenges facing struggling homeowners. Funding comes from the federal Troubled Asset Relief Program (TARP), and all funded programs must satisfy requirements of the

Emergency Economic Stabilization Act of 2008. For a list of HHF states and their foreclosure prevention strategies, see http://www.treasury.gov/initiatives/financial-stability/housing-programs/hhf.

Home Affordable Modification Program (HAMP)

Created by the U.S. Treasury in February 2009 with $50 billion in TARP funding, HAMP is designed to encourage lenders to modify the terms of mortgages to make monthly payments affordable for delinquent borrowers. HAMP encourages lenders to participate by making incentive payments for permanent modifications that allow homeowners to stay in their homes. Lenders and mortgage servicers sign a servicer participation agreement requiring them to offer HAMP modifications to all eligible borrowers. See www.hmpadmin.com.

Loan-to-value ratio (LTV)

The amount due on a mortgage divided by the assessed value of the property. If homeowners owe more than the assessed value, their LTV is greater than 100 percent.

Mortgage-backed securities

An ownership interest in mortgages created when issuers package them for sale to investors. As homeowners pay off the loans, investors receive interest and principal. For a primer on these securities, see *An Investor's Guide to Mortgage Securities*, Freddie Mac, http://www.freddiemac.com/mbs/docs/about_MBS.pdf.

Net present value (NPV) calculation

Uses information on homeowners and their mortgage to determine whether they are eligible for a mortgage modification, and whether the lender would benefit from modifying the loan. If the total discounted value of expected cash flows from the modified loan is higher than that from the unmodified loan, the result is positive, or passes the calculation test, and the lender would benefit from modifying the loan. If the discounted value of the cash flows from the modified loan is lower than that from an unmodified loan, the result is negative, or the NPV calculation fails, and the lender would not benefit from modifying the loan.

Partial claim

A HUD program that helps homeowners make past-due payments on FHA mortgages. Borrowers must be at least four months behind on payments on their primary residence and prove that a financial hardship caused their delinquency.

Prime borrowers

Those with a good credit history and adequate income who qualify for the lowest-interest, fixed-term mortgages—typically 30 years.

Reinstatement

The amount—including mortgage payments, late fees, and legal costs—that will bring an overdue mortgage current and prevent foreclosure. Under a mortgage reinstatement plan, the lender agrees to allow homeowners to pay the total amount due in one lump sum by a specific date.

Short sale

An agreement between homeowners and lender to allow the sale of a home at less than the value of the mortgage, as an alternative to foreclosure (see LTV and underwater mortgage). Lenders typically—but not always—forgive the difference between the value of the loan and the sales price of the home.

Subprime borrowers

Typically those with a poor credit history who do not qualify for a conventional mortgage and receive riskier mortgages, such as adjustable-rate mortgages, and whose lenders require little or no documentation or no downpayment.

Troubled Asset Relief Program (TARP)

Under the Emergency Economic Stabilization Act of 2008, the Treasury Department received $700 billion to promote stability in financial markets by purchasing and insuring "troubled assets." The Treasury used some of this authority to create programs designed to stabilize the housing market, such as HAMP and HFF. See http://www.financialstability.gov.

Underwater mortgage

The amount due on the mortgage is greater than the value of the house—also called negative equity.

Appendix B
Foreclosure mediation programs in New England

Connecticut's Foreclosure Mediation Program

Website: http://www.jud.ct.gov/foreclosure/

Results: http://www.jud.ct.gov/statistics/FMP/

Legislation:
2008: http://www.cga.ct.gov/2008/SUM/2008SUM00176-R02HB-05577-SUM.htm
2009: http://www.cga.ct.gov/2009/ba/2009HB-06481-R000200-BA.htm
http://www.cga.ct.gov/2009/sum/2009SUM00209-R04SB-00948-SUM.htm
2010: http://www.cga.ct.gov/2010/sum/2010SUM00181-R02HB-05270-SUM.htm
2011: http://www.cga.ct.gov/2011/ACT/PA/2011PA-00201-R00HB-06351-PA.htm

Maine's Foreclosure Diversion Program

Website: http://www.courts.state.me.us/court_info/fdp/index.html

Results: http://www.courts.state.me.us/publications_other/fdp_2010_ar.pdf

Legislation: http://www.mainelegislature.org/legis/bills/bills_124th/chapters/PUBLIC402.asp

New Hampshire's Mediation Program

Website: http://www.courts.state.nh.us/adrp/foreclosure

Legislation: http://www.gencourt.state.nh.us/legislation/2009/SB0070.html

Rhode Island City Ordinances

Providence: http://cityof.providenceri.com/deeds

Cranston: http://www.cranstonri.com/pdf/FOI2.pdf

Warwick: http://www.warwickri.gov/pdfs/cityclerk/2010/PCO-7-10.pdf

Vermont's Foreclosure Mediation Program

Information: http://www.uvm.edu/consumer/?Page=foreclosure.html

Legislation: http://www.leg.state.vt.us/docs/2010/Acts/ACT132.pdf

Appendix C
State housing finance agencies and financial assistance programs in New England

Connecticut Housing Finance Authority

http://www.chfa.org

CHFA Financial Assistance Programs (CT FAMLIES and EMAP)

http://www.chfa.org/Homeownership/for%20Homeowners%20at%20Risk%20of%2
Foreclosure/default.aspx

Legislation: 2008: http://www.cga.ct.gov/2008/SUM/2008SUM00176-R02HB-05577-SUM.htm
2009: http://www.cga.ct.gov/2009/ACT/PA/2009PA-00209-R00SB-00948-PA.htm
2010: http://www.cga.ct.gov/2010/ACT/PA/2010PA-00002-R00SB-00502SS1-PA.htm

MaineHousing

http://www.mainehousing.org

Maine HOPE

http://www.mainehousing.org/Documents/Brochures/Brochure-HOPEFlyer.pdf

MassHousing

http://www.masshousing.com

New Hampshire Housing Finance Authority

http://www.nhhfa.org

Rhode Island Housing

http://www.rhodeislandhousing.org

R.I. Hardest Hit Fund

http://www.hhfri.org

Vermont Housing Finance Agency

http://www.vhfa.org

Appendix D
Websites with foreclosure resources in New England states

Connecticut

Judicial branch, state law on foreclosures

http://www.jud.ct.gov/LawLib/Law/foreclosure.htm

Maine

Bureau of Consumer Credit

http://www.maine.gov/pfr/consumercredit/foreclosure_resources.html

Massachusetts

Office of Consumer Affairs & Business Regulation

http://www.mass.gov/foreclosure

New Hampshire

Help for New Hampshire Homeowners

http://www.homehelpnh.org

Vermont

Mortgage Assistance Program,
Department of Banking, Insurance, Securities, & Health Care Administration

http://www.bishca.state.vt.us/banking/consumer-resources/mortgage-assistance-program-map

New England Public Policy Center
Federal Reserve Bank of Boston
600 Atlantic Avenue
Boston, MA 02210

PRSRT STD
U.S. Postage Paid
New Bedford, MA
Permit No. 450

The New England Public Policy Center was established by the Federal Reserve Bank of Boston in January 2005. The Boston Fed has provided support to the public policy community of New England for many years; NEPPC institutionalizes and expands on this tradition. The Center's mission is to promote better public policy in New England by conducting and disseminating objective, high-quality research and analysis of strategically identified regional economic and policy issues. When appropriate, the Center works with regional and Bank partners to advance identified policy options.

You can learn more about the Center by contacting us or visiting our website:

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