

March 16, 2011
Testimony before House Banking and Financial Services Committee
House Bill 4118

Good morning. Thank you for affording me the opportunity to comment on House Bill 4118. My name is David Brandt and I am the CFO of E&A Credit Union in Port Huron.

E&A is a part owner of The Mortgage Center, a Credit Union Service Organization that originates and services mortgage loans for credit unions throughout Michigan. As of February 28, 2011 over 14,300 mortgages are serviced through Mortgage Center.

In that portfolio there are more than 725 loans under modification agreements. Of those modifications one is the result of the current Public Act requiring pre-notification of foreclosure. We have found that successful modifications are the result of proactive communication long before the talk of foreclosure. Our experience has been that the pre-notification requirements add expenses and time to the foreclosure process and do not result in successful loan modification.

Currently, E&A begins to solicit modified payment arrangements no later than 35 days delinquent. By the time a loan is 50 days delinquent, the borrower has received three letters that solicit no less than four alternatives to foreclosure. This is in addition to phone calls and other communication. Notice of breach is sent no earlier than 61 -91 days delinquent. It is only after these efforts that the credit union sends the pre-notification letter of intent to foreclose. While many borrowers respond, our experience is that the response is not genuine and is used only to delay foreclosure.

It is important to remember that these are minimums. In one case we carried a borrower without payment for 15 months while waiting for his social security disability case to be settled. Our first choice is always to keep the borrower in their home.

Since this legislation was enacted E&A, has entered into 17 modification agreements. All were entered into prior to reaching the pre-foreclosure notification. Unfortunately, nine other homes have been foreclosed. At least three of those had been converted to rental property. Four additional properties were resolved through short sale and two were transferred by deed in lieu of foreclosure.

Foreclosure is expensive. The current process runs a minimum of 13 to 19 months. During that time payments are not received, the lender pays the property taxes, and the lender pays to insure the property. Attorney fees, publication costs, and the labor involved with sending notices and attempting to contact homeowners become very expensive.



The expenses only grow once the lender takes possession. It is now the norm for borrowers to remove plumbing, lighting, and other fixtures. More than half of our foreclosed properties could be sold only to cash buyers as the damage left by the homeowner disqualified the home for traditional financing.

While the home is on the market, taxes and insurance continue to be paid. The cost of upkeep includes lawn maintenance, snow removal, and regular inspections. Utility payments, local registration and permitting fees, marketing costs, and real estate commissions all erode the amount a lender will recover.

E&A's most recent foreclosure was a loan made in November of 2007. The loan had a principal balance of \$105,000 at foreclosure. At some point the borrower destroyed most of the floor coverings, punched holes in virtually every wall, and removed the sump pump leaving over a foot of water in the basement. The home is currently under contract for \$40,100. After costs associated with the sale, we will net \$20,000. We know that our best option for recovery is a homeowner paying us back.

Last summer this process became more personal for me. My next door neighbors decided foreclosure would be a great strategic option. They lived in their house for several months without paying their mortgage. Those savings gave them the money to put down on a bigger, nicer rent-to-own with the same payment as their old house. On the way out they removed landscaping, broke up concrete to get their basketball pole, and even took the central air unit. The house has been vacant now for seven months.

Comments on the Language of the Bill

No deadline is included for the borrower to attend a meeting with the mortgagor or to provide necessary documentation to the mortgagor. The request for a meeting adds 90 days to the foreclosure process. This period should end if the borrower does not provide requested documents within a reasonable time period.

Notification of pre-foreclosure is required by first-class mail, certified mail, and publication. Given that the bill is limited to the borrower's primary residence, this appears onerous.

The bill provides for virtually unlimited, repetitive modification. The borrower "earns" these protections by complying with a modification for only one year.

The bill requires that a housing counselor be involved in order for the borrower to exert these rights. A borrower should be able to take independent action should they so choose.

The required modification terms are unlikely to remain practical. They should be related to terms available in the marketplace, rather than requiring future legislation for



modification. For instance, a 3% mortgage is much more feasible when the market is at 5% than when it is at 8%. Accounting rules require recognition of the discount and lenders need to compensate for this risk.

Unintended Consequences

There are several side effects created with this legislation. Some have been realized, others are being discussed. They definitely merit consideration.

Breach letters that trigger foreclosure are being issued at earlier stages of delinquency. This is a direct result of the additional time added to the foreclosure process.

Credit standards may tighten. Borrowers with more colorful credit histories may find mortgages more difficult to obtain. Larger down payments, lower allowable debt ratios, and shorter repayment terms could all be anticipated.

Lenders may reduce the overall funds available for mortgage lending in Michigan. Lenders are effectively insuring borrower's future income. This liability will be considered in credit policies.

Consider the case of someone approaching retirement. One of the more common targets is to replace 60% of one's employment income in retirement. A very reasonable housing payment of 25% of gross income before retirement becomes 42% after retirement. Retirement should not trigger qualification for modification. Lenders will be forced to consider this risk.

Recommendations and Conclusion

In many ways the current housing marketing in Michigan makes this legislation unnecessary. Lenders are not able to recover mortgage balances through the sale of foreclosed property. Repayment by the borrower, even at a reduced level is often preferable.

Mortgage Center is a great example of this fact. More than 5% of the serviced portfolio is under modification. Less than 2% are in foreclosure. Moreover, the modifications are working. Of the 17 E&A loans under modification, none have gone to foreclosure and only one has required subsequent modification.

Legislation should be focused on delivering results. I believe this legislation was written with the best of intentions. However, it has not provided measurable benefit to Michigan's 4.5 million credit union members. In fact, as cooperative owners of their financial institution, Michigan's credit union members have subsidized the increased costs associated with complying with the act.



I believe it would be appropriate to allow the Public Act to expire in July as designed. If it is to be extended, it should be for a limited time only. Modifications should then be made to limit abuses of the provision. These modifications should include:

- Time limits for borrowers to perform their obligations
- Reduction to the redemption period after foreclosure
- Authority for lenders to compel a review of the borrower's financial condition after modification
- Modification terms that are tied to then current market terms

I appreciate the opportunity to provide testimony and am happy to provide further information or explanation.

Sincerely,

A handwritten signature in blue ink, appearing to read "DCB", is written over a faint blue line.

David C. Brandt, CPA
Chief Financial Officer