Joint Center for Housing Studies

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Protecting Homeowners Post-Purchase:

Lessons Learned from Engaging Distressed Homeowners

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For most families, a central part of the American Dream has been the goal of homeownership. Consumer attitudes, public policy, and the private sector were all integrally involved in driving the rate of homeownership to a record high of 69% in 2004[1]. The prevailing opinion of the day was that homeownership was a sound economic investment, built stronger families and enriched community life.

The Great Recession and lingering economic hardship afterward had a devastating effect on individuals, families, neighborhoods, and communities across our nation. The combination of record numbers of unemployed and underemployed, foreclosures, significant drops in home values, and loss of retirement savings and investments made this a complex and difficult problem to try to solve. Personally, most people know the story of at least one friend, family, neighbor, or coworker who struggled through this recession. However, these individual stories were often drowned out due to the sheer numbers of people in trouble, reducing people caught in this crisis to a statistic and making it easy to lose sight that these were people trying to survive and do the right thing through one of the most challenging times we have seen in the past 60 + years.

This paper will offer insights on individuals and families who sought help from housing counseling during this tumultuous period. Many factors and events can threaten the sustainability of homeownership, including income and budget shocks, life events, unexpected repair costs, falling home prices, and interest rate risk. These and other challenges encountered in the past few years have caused many to reassess the value of homeownership and forced everyone to reengineer how they engage with those facing the loss of their home. By assessing the data and performance from a variety of programs and services used by one of the nation's oldest and largest counseling agencies, we can gain insights and ideas about how to better help homeowners resolve mortgage delinquencies and ultimately achieve sustainable homeownership for more families in the future.

CredAbility is a full-service, nonprofit, financial counseling agency headquartered in Atlanta, formerly known as CCCS of Greater Atlanta. Founded in 1964, CredAbility provides 24/7 holistic

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[1] Joint Center for Housing Studies, *State of the Nation's Housing 2012.*

counseling in-person in five states in the Southeast and nationally in all 50 states via the telephone and Internet, in both English and Spanish. As one of the largest counseling agencies in the nation, CredAbility is a HUD-certified national intermediary and a member of both the National Foundation for Credit Counseling and the Homeownership Preservation Foundation. Our mission is to serve as a trusted advisor, helping people resolve financial challenges and build economic security for themselves and their families. We use comprehensive, holistic counseling to help clients assess their situation, set priorities and clear goals, and establish a realistic, written action plan to achieve them. We have helped more than 3 million households nationally since 2007 through our preventive and remedial services, which include Education and Public Outreach, Bankruptcy Counseling & Education, Housing Counseling, Budget & Credit Counseling, and Debt Management Plans.

While we conduct a broad range of education and counseling services with homeowners, this paper will focus on what we have learned about the challenges distressed homeowners face and how new methods of outreach and approaches to providing support are improving their likelihood of sustaining ownership and realizing positive outcomes from owning. Specifically, we will review:

- <u>Foreclosure Prevention Counseled Client Profiles</u>. Our counseling data offers a deeper, more comprehensive view of who is seeking help and the challenges they face in sustaining homeownership;
- <u>Early Intervention Outreach Program</u>. There is a significant group of delinquent homeowners who are hiding and/or discouraged from trying to resolve their delinquency, and early intervention by nonprofit counseling agencies can be a very effective tool to reach these families and encourage them to act; and
- <u>Post Modification Support Program</u>. It was not surprising that many attempts at loan modifications failed because they did not address the family's entire financial obligations. Ongoing engagement after a loan modification makes a significant difference for financially-fragile families as they recover and rebuild their financial lives.

The value of homeownership is deeply rooted in our personal and collective psyches. The data offered here represents the personal stories of millions of people who have faced the potential or actual loss of their home. As you read through this paper, we challenge you to ponder these two questions – "What should we – as counselors, policy makers, lenders, government, friends, and community leaders – do to help this person?" and "What should they do to address their situation?" Unfortunately the answers are not so clear or simple, but these are the questions we need to wrestle with and solve in order for us to close this chapter in our history, to aid the national economic recovery, and to protect communities from a repeat of this crisis again in the future.

The Historic Scope of the Problem

Before we review the data or explore the effectiveness of any of our programs, it is wise to stop and fully consider the depth and breadth of the challenges average families (low-to-moderate income and struggling middle class) faced during this time. Understanding the people and their situation is essential to crafting appropriate solutions. By any standard or measure, we know that the average family has struggled over the past few years. There are a variety of different tools and indices to assess individual components of this at a macroeconomic level, but none of these measures attempt to tell the whole story from the individual family's perspective and none of them look holistically at the key elements of what average families face. With nearly 50 years of experience and insight into helping consumers in financial distress, we know the biggest causes of distress, and how people react to financial challenges and proven strategies for regaining control. We applied this experience to build the CredAbility Consumer Distress Index (the "Index") to measure the financial condition of the average American household.

The Index is a quarterly, comprehensive picture of the average American household's financial condition. Built by assessing the key elements of financial health and distress, it converts a complex set of factors into a single, easy to understand number. The index measures the U.S., all 50 states and 77 of the largest metropolitan areas, with national and state reports dating back to 1980 and metropolitan reports dating back to 1990. We measure the five categories of personal finance that reflect or lead to a secure, stable financial life: Employment, Housing, Credit, Household Budget, and Net Worth. All are equally important, so each category is equally weighted. We use more than 65 data points from government, public and private data, and a proprietary methodology for compiling, combining, and evaluating data.[2] A sampling of key data points include: unemployment and under-employment, mortgage and rental delinquencies, housing cost as percentage of budget, credit scores, trade line utilization, credit delinquencies, per capita bankruptcies, disposable income, savings, consumer confidence, and household net worth.

Financial distress is measured on a 100 point scale and a score below 70 indicates financial distress. In general, lower Index scores equate to the presence of more household financial distress, a weaker financial position, the greater urgency to act, resolutions that will take longer and be harder to achieve, and the increased probability of needing a third party help to resolve. The Index score is tied to one of five general rating categories, which reflect the strength and stability of the consumer's position. The following table (Exhibit 1) shows the point values for each rating category and the distribution of quarterly ratings for the period 1980 Q1 to 2012 Q4.

Exhibit 1: CredAbility Consumer Distress Index Rating Scale

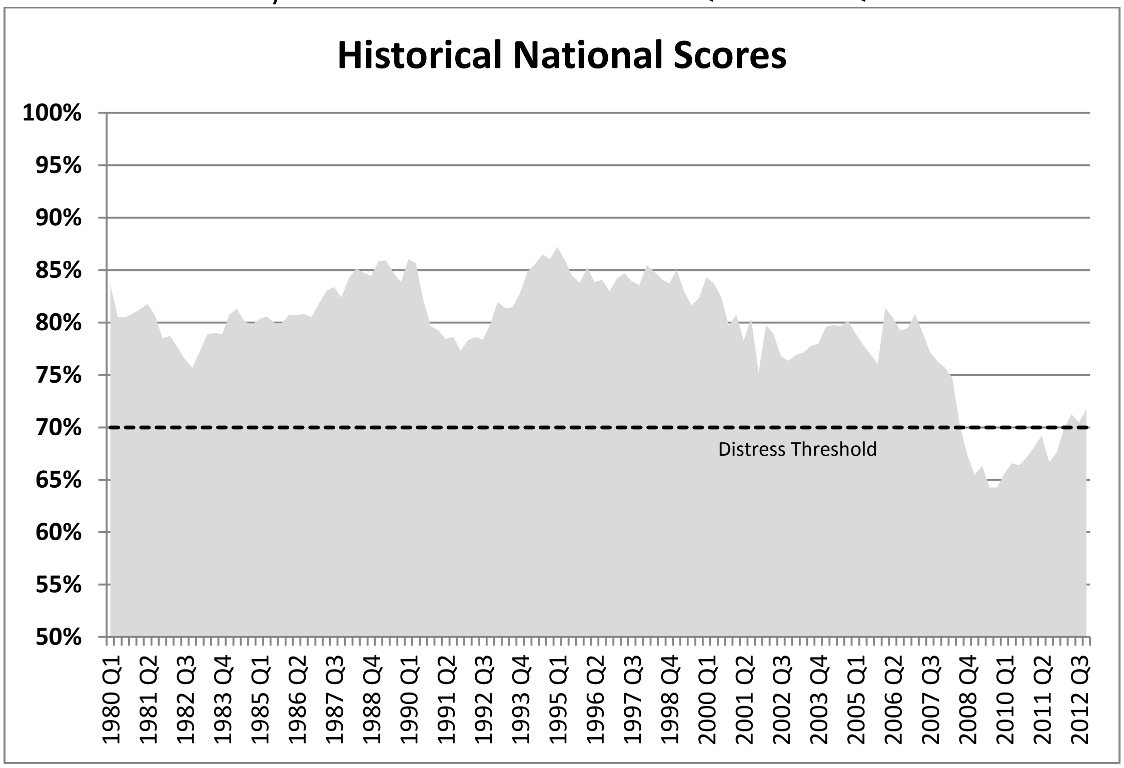
Rating	Score Range	Quarters Rated from 1980 to 2012	
		Number with Rating	Percent of Total
Secure	90 and Above	0	0%
Stable	80 – 89	68	51.5%
Weak	70 – 79	50	37.8%
Distressed	60 – 69	14	10.6%
Crisis	Less than 60	0	0%

Source: CredAbility, Consumer Distress Index 2007-2012

[2] CredAbility client data is not a data source for the Index. More information and historical data for the Index is available at *www.credability.org/consumerdistressindex*.

The following graph (Exhibit 2) offers a broad historical perspective of the National Index scores for the period from 1980 Q1 to 2012 Q4. The average quarterly score during this period was 79.3, with a high of 87.2 in 1995 Q1 and a low of 64.3 2009 Q4 64.3.

Exhibit 2: CredAbility Consumer Distress Index 1980 Q1 to 2012 Q4

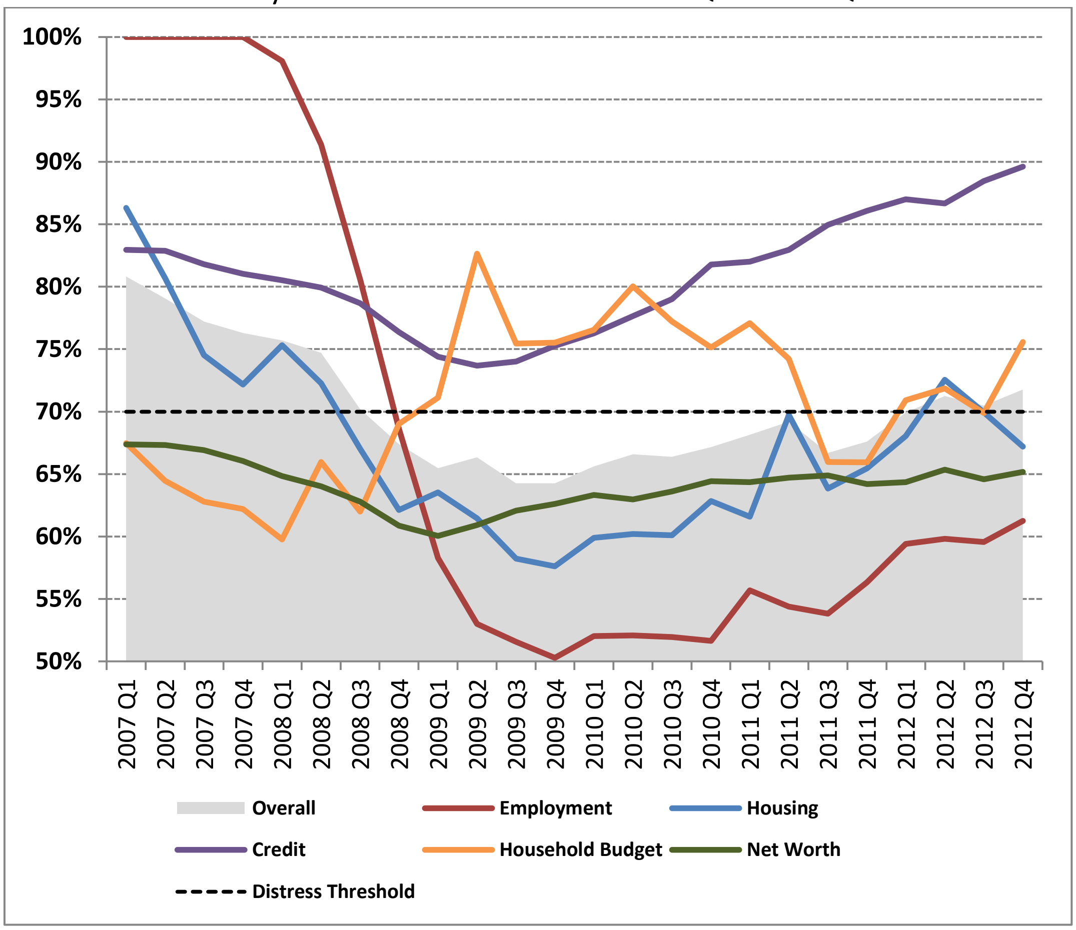


Source: CredAbility, Consumer Distress Index

The next chart (Exhibit 3) displays the National quarterly Index scores from the Great Recession of 2007 through the end of 2012. The overall score and the scores for each of the five elements are charted here to give you a sense of the drivers of the overall score and trends across time. Nationally, we were in a state of Distress from the 3rd quarter of 2008 to the 2nd quarter of 2012 – 14 consecutive quarters. Employment and Housing were the primary drivers of distress, but it also interesting to note how consistently strong and poor Credit and Net Worth were respectively and how Household Budgets fluctuated as families adjusted to their ever evolving situations.

The key takeaway here is that not only were average families in distress during this time, but by historical standards this has easily been the most stressed period in recent history and these 19 quarters were the worst 19 quarters in the past 31 years.

Exhibit 3: CredAbility Consumer Distress Index 2007 Q1 – 2012 Q4



Source: CredAbility, Consumer Distress Index

So, given this analysis as a backdrop, it should be no surprise that the families seeking help are facing some very difficult circumstances.

Faces of the Crisis: Overview of CredAbility's Counseling Client Profile

Before we can create a solution and action plan, we work with our clients to understand the individual or family's entire story. As a result, the depth of our engagement with those we counsel enables us to gather some unique data and insights. We must collect a comprehensive set of data to properly assess the client's situation and craft professional advice to help them implement a plan to achieve their goals. As a result, these 1:1 counseling sessions yield a rich data set that includes the following categories:

- Demographic – age, gender, marital status, ethnicity, and household size;
- Financial – income and expenses, assets and liabilities, and debt obligations;
- Credit – reports, credit and bankruptcy risk scores at counseling and one year later; and
- Cause of Problem – primary and secondary issues why they are seeking assistance.

We see a unique holistic view of clients' situations, as clients are willing to tell a neutral, non-judgmental third party much more about their true situation than they will to anyone else. We now host more than 3 million first counseling session records in our data warehouse and, because of our national work, affiliations, and partnerships, our data generally reflects the national geographic distribution of problems.

Overall, our data reveals a very financially fragile household. Since CredAbility serves people of all socio-economic levels and demographic groups, literally people from food stamps to those earning six-figure salaries, there is no simple answer as to who is our "typical" client. However, the average (mean) of all 1.6 million first counseling sessions completed across all of our lines of service from 2007 to 2012 looks like this:

- 46 year old, married Caucasian female
- 2.8 persons in household
- Homeowner (68%)
- 548 credit score, 137 Bankruptcy Navigator Index score
- $44,418 gross annual income
- ($1,441) monthly budget deficit (the amount of money left over after paying all scheduled bills)
- $30,134 unsecured debt
- 32.5% monthly housing costs to income ratio ("front-end ratio") / 54.1% total monthly recurring debt payments to income ratio ("back-end ratio")
- ($49,090) net worth

It is worth pausing for a moment to let the weight of that data sink in, because only by understanding the characteristics of those seeking help can we fully understand what happened and potentially how to prevent it in the future. This group would historically be in an asset accumulation phase of their lives to prepare for retirement in 20 or so years. Instead, they find themselves in a deep financial hole, saddled with a substantial negative net worth, troublesome levels of unsecured debt, ruined credit, difficult employment/income prospects, and serious questions about the value of homeownership. Historians will debate whether the Great Recession was the product of a housing bubble, subprime lending, government inaction, consumer greed, market failures, or some combination of these and/or other factors. What is beyond dispute is that this was much, much more than a housing crisis and that the impacts on spending and borrowing, perspectives on household income and employment, and the shattered dreams of this generation's retirement plans will reverberate for years in our national economy and psyche. Any serious discussion about long-term solutions must take these factors into consideration.

To help understand the specific challenges of homeowners who identified their mortgage delinquency as their primary financial problem, we will next look in-depth at a subset of these 1.6 million first counseling sessions. Data gathered from more than 422,000 foreclosure prevention clients through counseling sessions offers a unique perspective and better understanding of many of their specific issues.

Changing Demographics

As outlined in the following table (Exhibit 4), the demographic characteristics of those seeking help foreclosure prevention help changed dramatically across the past 6 years and some key observations about these trends and changes follow after the table.

Exhibit 4: CredAbility Foreclosure Prevention Client Demographics

Demographic Information	2007	2008	2009	2010	2011	2012
Age	44	44	46	48	49	51
Gender						
Female	61.3%	56.8%	52.3%	52.9%	53.5%	55.5%
Male	38.7%	43.2%	47.7%	47.1%	46.5%	44.5%
Marital Status						
Married	53.2%	57.7%	60.4%	56.9%	55.9%	53.9%
Divorced	14.7%	13.8%	13.3%	15.2%	15.7%	15.8%
Single	32.1%	28.6%	26.3%	27.9%	28.4%	30.3%
Female Headed Household	33.9%	27.8%	24.0%	25.9%	27.5%	30.1%
Ethnicity						
Caucasian	38.6%	42.2%	44.2%	49.1%	51.5%	50.9%
African American	39.8%	29.1%	19.9%	21.1%	20.6%	23.4%
Hispanic	15.8%	22.1%	29.4%	22.6%	20.5%	18.6%
Asian	1.3%	2.4%	3.0%	3.0%	2.7%	0.5%
Native American	0.4%	0.4%	0.4%	0.4%	0.3%	4.1%
Other	4.1%	3.8%	3.1%	3.8%	4.3%	2.6%
Household Size	3.2	3.3	3.2	3.0	3.0	2.9

Source: CredAbility, Foreclosure Prevention Client Profile 2007-2012

- Age. One of the most discouraging trends has been the steadily increasing age of our clients, moving from 44 in 2007 to 51 in 2012. Historically, our client has been a low-to-moderate family in their late 30s or early 40s. *Implication: People in their 40s and 50s traditionally have been stable financially, but this generation is dealing with employment issues and aging with unprecedented levels of debt. Most importantly, they have less time to recover from their current financial crisis. The cumulative impact of these challenges means they will face the most uncertain retirement in generations, one where they will be more responsible for and less prepared to handle their financial responsibilities.*

- Gender. Women have always been the majority of clients seeking counseling, but during this recession the percentage seeking help moved downward from 61.3% in 2007 to 52.3% in 2009 as more married couples and single men sought help.
- Ethnicity. In the early years of the housing crisis, we saw a disproportionate number of people of color seeking help. In the 2006-2008 time frame, the majority of people (between 57-61%) seeking assistance were from minority groups and most had nontraditional or subprime mortgage products. However, as the housing crisis has evolved and became an employment-driven problem versus a product-driven issue, the distribution of clients changed to mirror the nation's broader demographics, reaching a majority Caucasian (51.5%) client base by 2011.

Changing Reasons for Distress

Exhibit 5: CredAbility Foreclosure Prevention Client Causes of Financial Problem

Cause of Financial Problem	2007	2008	2009	2010	2011	2012
Reduced Income / Unemployment	48.8%	47.7%	55.8%	52.9%	58.4%	43.8%
Over-Obligation / Over-Spending	29.9%	13.2%	7.0%	6.8%	8.5%	25.7%
Divorce / Separation / Death	8.7%	6.7%	9.3%	5.1%	7.5%	3.8%
Medical / Accident / Disability	2.0%	11.1%	6.9%	6.9%	10.1%	8.5%
Other / Not Provided	10.6%	21.4%	21.0%	28.2%	15.5%	18.2%

Source: CredAbility, Foreclosure Prevention Client Profile 2007-2012

While there may be significant volatility in the reasons cited for financial distress from year to year, people generally face financial distress for one of two basic reasons – the consequence of behavior or unpreparedness for unplanned circumstances. Traditionally, there are four major groups of causes of financial problems (1) reduced income from job loss, temporary under-employment, or cutbacks in hours worked, (2) changes in marital status, such as separation, divorce or becoming widowed, (3) medical issues, ranging from one-time events to chronic conditions or disability, and (4) overspending or accumulating too much debt. People get sick and divorced at roughly the same rates across all economic cycles. Historically, when the economy is good, people who get in trouble tend do so as a result of overspending and/or over-obligation. During recessions, it is job loss, temporary under-employment, and other reductions in hours or income that drive financial distress. This chart shows the clear shift away from behavior-based problems to income-related problems in the years 2007 to 2008 and the reverse trend in the years 2011 to 2012. This last shift has been driven as the unemployment rate has dropped and people have secured permanent work at lower rates of pay. This new reality of a permanently reduced income with significant financial obligations is part of the face of the current economic recovery. Interestingly, we are also seeing a rise in combination versus single problems, as well as the emergence of student loans as an issue, which appear in both the Other and Over-Obligation categories and is cited as a cause of distress by 8 to 13% of homeowners. *Implication: Jobs are the most critical factor in this recovery and for household financial stability, as it is difficult to pay a mortgage without one or with one that pays significantly less than when the home was purchased.*

Daunting Financial Picture

Average families use a limited number of relatively simple financial products in their financial lives, but these clients face a complicated situation. At the heart of every counseling session is a detailed review and frank conversation about their goals, habits, and overall financial picture. The following table (Exhibit 6) shows the financial information gathered from foreclosure prevention sessions:

Exhibit 6: CredAbility Foreclosure Prevention Client Financial Information

Financial Information	2007	2008	2009	2010	2011	2012
Gross Annual Income	**$45,423**	**$51,341**	**$50,520**	**$50,889**	**$51,081**	**$51,948**
Monthly Net Income	$3,097	$3,463	$3,464	$3,410	$3,376	$3,352
Monthly Living Expenses	$1,963	$2,154	$2,110	$2,108	$2,150	$2,178
Monthly Debt Payments	$2,289	$2,655	$2,601	$2,498	$2,420	$2,261
Monthly Surplus/Deficit	**($1,125)**	**($1,346)**	**($1,247)**	**($1,196)**	**($1,194)**	**($1,087)**
Surplus/Deficit as Percent of Gross Income	*-29.7%*	*-31.5%*	*-29.6%*	*-28.2%*	*-28.0%*	*-25.1%*
Surplus/Deficit as Percent of Net Income	*-36.3%*	*-38.9%*	*-36.0%*	*-35.1%*	*-35.4%*	*-32.4%*
Secured Debt Payments						
Housing Expense	$1,441	$1,671	$1,652	$1,568	$1,529	$1,444
Non-Mortgage Debt	$483	$507	$496	$475	$465	$457
Unsecured Debt						
Total Debt	$14,627	$19,091	$18,137	$18,321	$17,063	$14,412
Minimum Payment	$365	$477	$453	$455	$426	$360
# Creditors	5.0	5.3	4.6	4.6	4.4	3.9

Source: CredAbility, Foreclosure Prevention Client Profile 2007-2012

Key observations from this data include:

- Household Income. While we serve clients from all socio-economic groups, our work has historically been with low-to-moderate income families. However, this recession definitely impacted the middle class and above. We saw a huge jump in gross income from $40,534 in 2006 (not shown on this Exhibit 6) to $45,423 in 2007 to $51,341 in 2008, primarily as a result of higher income families dealing with job loss or under-employment issues. Our average client's income now mirrors that of the US median household income. It has become very common to see people who have previously supported the work of nonprofit and social service agencies and food banks to now be their clients. *Implication: Many people who traditionally had discretionary income or access to home equity are now struggling to keep their mortgage current. This change in income has also impacted their ability to refinance their mortgage and have funds available for upkeep, maintenance or repairs.*

- Household Expenses. As these clients sat around their kitchen table to work on their family budget, they faced a daunting challenge. The average starting budget for all Foreclosure Prevention clients from 2007 to 2012 is shown in the following table (Exhibit 7):

Exhibit 7: CredAbility Foreclosure Prevention Client Average Starting Monthly Budget

Monthly Take Home Pay	$3,400
Housing (mortgage, taxes, insurance)	$1,570
Living Expenses (food, gas, clothing, utilities)	$2,126
Non-Mortgage Secured Debt (auto)	$480
Unsecured Debt (credit cards)	$433
Monthly Surplus/(Deficit)	($1,209)

Source: CredAbility, Foreclosure Prevention Client Profile 2007-2012

Clearly, many of these family budgets were built on a different income level or were enabled by access to credit cards or home equity to deal with any budget shortfall. Instead, they found themselves forced to juggle their finances, deciding which bill to pay or whether to borrow and slip into deeper debt over time. *Implication: Credit cards have become critical to households' financial survival, as they provide needed cash flow for basic living expenses like gas and groceries and are the only shock absorbers for unexpected expenses, since most have little to no savings. As a result, many families have reprioritized payment of credit cards ahead of their mortgage. This picture may also explain why gasoline and food price swings are much more impactful on psychology and consumer spending than stock market volatility.*

- Unsecured Debt - One of the positive trends emerging over the past few years is that Americans have finally become serious about dealing with their unsecured debt. At the peak of the crisis in 2009, the average CredAbility client was carrying between 3.5 times to 7.7 times more credit card debt than the average American, depending on what type of counseling assistance they were seeking. For Foreclosure Prevention clients, credit card debt peaked in 2008 at $19,091 and has dropped steadily to $14,412 by 2012. *Implication: This deleveraging, first due to charge-offs and more recently by people paying down debt, is* *being driven by three factors: (1) people who are afraid of the stability of their job and/or have seen no real growth in wages are loathe to risk carrying unnecessary debt; (2) for consumers who have damaged credit or poor credit scores, the tightened credit standards mean that they can't get new credit and they must manage existing credit better in order to keep it; and (3) the psychology of people who have paid off debt and are now enjoying the flexibility of being debt-free and don't want to go back to the bondage of carrying too much debt.*

Poor Debt-to-Income Ratios

From another angle, our clients have difficult debt-to-income ratios. For decades, mortgages were underwritten with a 28/36 rule, where borrowers were limited to a 28 percent front-end debt-to-income (DTI) ratio, calculated as the Mortgage Payment divided by Monthly Gross Income, and a 36 percent back-end DTI ratio, calculated as All Secured and Unsecured Debt Payments divide by Gross Income. The following table (Exhibit 8) outlines the DTIs for our clients:

Exhibit 8: CredAbility Foreclosure Prevention Client Debt-to-Income Ratios

Debt-to-Income Ratios	2007	2008	2009	2010	2011	2012
Housing as Percent of Gross Income	38.1%	39.1%	39.2%	37.0%	35.9%	33.4%
Housing as Percent of Net Income	46.5%	48.3%	47.7%	46.0%	45.3%	43.1%
Non-Mortgage Debt as Percent of Gross Income	22.4%	23.0%	22.6%	21.9%	20.9%	18.9%
Non-Mortgage Debt as Percent of Net Income	27.4%	28.4%	27.4%	27.3%	26.4%	24.4%
Combined as Percent of Gross Income	60.5%	62.1%	61.8%	58.9%	56.9%	52.2%
Combined as Percent of Net Income	73.9%	76.7%	75.1%	73.3%	71.7%	67.5%

Source: CredAbility, Foreclosure Prevention Client Profile 2007-2012

During this time period, the front-end ratios for clients in all of our other lines of service were not terrible, ranging from 23.8 percent to 32.8 percent. However, Foreclosure Prevention clients had front-end DTIs ranging from 33.4 percent to 39.2 percent and had back-end ratios, that fuller look at their obligations, ranging from 52.2 percent to 76.7 percent. It is very difficult to make housing sustainable with these kinds of ratios. *Implication: It was not surprising that early loan modification attempts failed at very high rates because these early efforts failed to look at the clients' entire financial picture and the problem was not solvable by adjusting a single payment or recapitalizing the arrearages. A second implication is that these Back-End ratios make for an interesting debate and difficult coordination between secured and unsecured creditors on who should take write-offs or make concessions to help homeowners succeed.*

Negative Net Worth

Calculating net worth for the average American family is a pretty simple exercise. Assets are composed primarily of their home, autos, checking account, savings account, and a very modest 401K. Liabilities include mortgages, auto loans, credit card debt, and some student loans. And while we stress to clients that their net worth does not define self-worth, it is still not a cheery exercise for most people to see where they stand. The following table (Exhibit 9) shows the net worth of the average client during this time period:

Exhibit 9: CredAbility Foreclosure Prevention Client Net Worth

Financial Information	2007	2008	2009	2010	2011	2012
Net Worth	**($8,168)**	**($72,630)**	**($88,936)**	**($64,923)**	**($44,388)**	**($20,029)**
Assets	$188,390	$173,460	$178,636	$202,080	$211,502	$210,561
Liabilities	$196,558	$246,090	$267,572	$267,003	$255,890	$230,590

Source: CredAbility, Foreclosure Prevention Client Profile 2007-2012

The impact of underwater homes weighed heavily on families' balance sheets. As net worth shifted from ($8K) in 2007 to ($89K) in 2009 to ($44K) in 2011, it was driven primarily by the declines in home value relative to the balances owed on mortgages. With these deficits, it would take many years of monthly payments for many homeowners to get back to just owing what the house is worth. *Implication: It is important to understand the homeowner's mindset, specifically, do they see their property a "house" or a "home"? A "house" is a place to live and a* *financial investment with limited emotional attachment. A "home" is a place for family with deep emotional meaning that offers social status and a connection to neighborhood, community, schools. As a result, the attitude and range of acceptance options for each group are quite different. In our own internal analyses of client performance, net worth has been consistently one of the best predictors of client success, as it impacts the willingness and capacity to implement and fight for the success of an action plan. This makes for interesting policy discussions around a variety of options and tools, from accelerated foreclosures to shared equity arrangements to principal write-downs.*

Distressed Credit Profile

One surprising, little known fact is that credit scores actually improved during the recession. While our clients' overall credit scores also rose steadily since 2007, it was more a reflection of the breadth the crisis, as more people with traditionally higher scores fell into distress rather than a broader recovery of low-to-moderate income families. The following table (Exhibit 10) shows the beginning credit profile of counseled clients:

Exhibit 10: CredAbility Foreclosure Prevention Client Credit Profile

Credit Scores	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**
Credit Risk Score	**511**	**519**	**546**	**561**	**564**	**576**
Bankruptcy Risk Score	114	113	133	145	154	180
- Probability of Bankruptcy	*77.9%*	*78.3%*	*70.0%*	*64.8%*	*61.1%*	*54.0%*

Source: CredAbility, Foreclosure Prevention Client Profile 2007-2012

- Credit Risk Score - For the past 10 years, the average credit score for clients across all other lines of services was in the high 520s to low 530s. Foreclosure Prevention clients were below that average during the 2007-2008 timeframe, but increased dramatically by 57 points from 2008 to 2012. This increase was primarily the result of people with traditionally higher credit scores seeking counseling after they encountered employment and income problems.

- Bankruptcy Risk Score- Another helpful tool in assessing the strength and future performance of clients are bankruptcy risk scores. While credit risk scores typically predict the chance a borrower will miss a payment in the next two years, bankruptcy risk scores predict the likelihood they will default entirely and file for a Chapter 7 liquidation or a Chapter 13 repayment plan. While dropping from a peak of 78.3 percent in 2008 to 54.0 percent in 2012, our clients had a very high statistical risk of failure.

  Implication: With these credit profiles, it is almost impossible for our clients to take advantage of refinancing at today's record low rates. And given the time it will take their credit to recover and in an era of significantly tougher underwriting, it will be a long time before they are likely to become homeowners again. Ironically, given the increased costs of filing after bankruptcy reform in 2005, some clients can't afford the filing fees and are too broke to file for bankruptcy.

Encouraging Results from Counseling

Despite all these dramatic shifts and significant challenges, foreclosure prevention counseling is a very effective tool. Once a person seeks help, a significant mindset shift occurs. With the full picture laid out, they can then decide on their goals and priorities and make the necessary choices in the proper context of priorities, trade-offs, and time frames. Over the last 6 years, we saw an average 40 point increase in the confidence to successfully reach their financial goals after counseling (from 37 percent to 77 percent).

Exhibit 11: CredAbility Foreclosure Prevention Client Survey Results

Survey Results	2007	2008	2009	2010	2011	2012
Confident in ability to reach goals - prior to service	34%	38%	37%	35%	39%	43%
Confident in ability to reach goals - after service	82%	78%	77%	75%	75%	73%
Net point increase in confidence	*48.0*	*40.7*	*39.7*	*40.3*	*36.9*	*30.0*
Would recommend our service	89%	88%	85%	85%	87%	82%

Source: CredAbility Annual Client Survey Summary

It is important to note that confidence levels and the net increase in confidence levels have dropped steadily across the period from 2007 to 2012. While this is may be a function of higher beginning confidence levels, it is also a reflection of the growing numbers of homeowners with very late stage delinquencies and others who are current but struggling with non-mortgage debts. These situations may well require new approaches and new tools to resolve their situations.

In addition to confidence gains, there have been a number recent studies that point to counseling's effectiveness, including Ding, Quercia, and Ratcliffe's (2008) study of outbound calls to mortgage borrowers 45 days delinquent, finding that the odds of curing the default are 50 percent higher for borrowers who accepted and received counseling than for non-counseled borrowers; Collins and Schmeiser's work (2013) find that counseling increases the probability of receiving a loan modification by 57.5 percent; and the Urban Institute's study on National Foreclosure Mitigation Counseling clients (2011) finds that counseled borrowers are more likely to cure (89-97 percent), received higher reductions in monthly payments ($176.00) and display lower re-default rates nine months after serious delinquency (67-70 percent).[3] CredAbility's

[3] Ding, Lei, Roberto G. Quercia, and Janneke Ratcliffe. "Post-purchase counseling and default resolutions among low-and moderate-income borrowers." *Journal of Real Estate Research* 30, no. 3 (2008): 315-344; Collins, J. Michael, and Maximilian D. Schmeiser. "The effects of foreclosure counseling for distressed homeowners." *Journal of Policy Analysis and Management* 32, no. 1 (2013): 83-106; Mayer, Neil, Peter A. Tatian, Kenneth Temkin, and Charles A. Calhoun, *National Foreclosure Mitigation Counseling Program Evaluation Final Report Rounds 1 and 2*, Washington, DC: NeighborWorks America, December 2011.

internal analysis of its foreclosure prevention counseling clients also showed that 81 percent were still in their home one year after counseling and 72 percent had no foreclosure activity on their credit report.

Outreach - Early Intervention

After seeing the level of financial distress experienced by many homeowners during the recession, it is easy to understand why one of the biggest challenges in dealing with individuals and families during this period was simply making contact with them. Whether as a result of feelings of shame or embarrassment or being paralyzed by misconceptions about the intentions of their servicer/investor, people often stop answering the telephone and/or opening their mail in a financial crisis. Given the traditionally low rate of mortgage delinquencies and defaults, the servicing world was equally unprepared from both a systems and staffing perspective to tackle this new world of double digit delinquencies. Freddie Mac estimated at one point that they had no contact with approximately 50 percent of homeowners that they had foreclosed on.

In late 2005, Freddie Mac engaged CredAbility and several other counseling agencies to determine if there was a way to reach and engage hiding and/or discouraged homeowners. This pilot kicked off in 2006 with three goals:

- Increase the contact rate with delinquent homeowners;
- Assess the efficacy of counseling at 45 days delinquency; and
- Decrease number of delinquent loans that result in foreclosure and prevent future delinquencies.

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http://www.nw.org/network/foreclosure/nfmcp/documents/NFMCEval_Rounds1-2_Final.pdf

Pilot Process

The pilot was designed to reach homeowners who were in the early stage of delinquency, primarily 45-60 days delinquent.

- Identifying Delinquent Borrowers. Individual companies servicing for Freddie Mac identified borrowers who were 45 days delinquent and who had no contact with the servicer since the delinquency began. Lists of these borrowers were sent to Freddie Mac, excluding certain types of loans such as FHA, VA, and those known to be in bankruptcy.
- Mailing the Offer. Upon receipt of the list, Freddie Mac mailed a solicitation letter to the homeowner on joint Freddie Mac/counseling agency letterhead that encouraged them to make contact with the servicer, offered free counseling, and informed them to expect a call from the counseling agency.
- Reaching Out. Within 5-7 days from the date of the solicitation mailing, if homeowners had not contacted the counseling agency or brought their account current, the counseling agency placed the first call in an attempt to reach the homeowner. The counseling agency made at least three attempts to reach the homeowner by calling at different hours and different days of the week.
- Encouraging Action. The content of the contact was simple and straightforward. Homeowners were encouraged to act—either by contacting the servicer directly or scheduling a counseling session—versus continuing to ignore the problem.

Pilot Results

The 2006 Pilot concluded at the end of 2007 and the results included:

- 16,751 letters mailed to delinquent homeowners, of which:
    - 10,738 homeowners made direct contact with the lender or brought the account current (62 percent of letters mailed)
    - 6,373 homeowner names and contact information were forwarded to the counseling agencies (38 percent of letters mailed)
- 4,840 homeowners made contact with or were contacted by the counseling agency (28.9 percent of letters mailed)

- 1,488 homeowners were counseled by the agency (30.7 percent of contacted by agency)
- Of the 4,840 homeowners that were in contact with the counseling agency, 2,556 (52.8 percent of those contacted by agency) avoided foreclosure via repayment plan, reinstatement, payoff, etc.
- 242 workout packages were created by counseling agencies (5.0 percent of those contacted by agency)

Broader Goals, Continuing Success

With these promising initial results, the pilot was moved into full program status in 2008 and the program goals expanded to five main goals for each contact:

- Reach the homeowner by phone;
- Establish homeowner's intention;
- Provide counseling (priority budget, importance of mortgage, options);
- Initiate a conversation between the homeowner and servicer; and
- When appropriate, complete workout package and forward to the servicer.

To date, the program has yielded some impressive results as outlined in the following table (Exhibit 12), including these program activity and success rates to-date:

Exhibit 12: CredAbility-Freddie Mac Early Intervention Program Data

Step	Number	Activity Explanation
Letters Mailed	955,768	Homeowners received letter with offer of assistance
Contacts by Agency	239,454	Right party contacts made by agency
Counseled by Agency	86,585	Completed a counseling session
Packages Submitted	17,660	Assembled and submitted a pack for decision
Delinquency Cured	59,265	Homeowner contacted who ultimately cured their delinquency
Foreclosure Avoided	64,922	Homeowner contact who avoided foreclosure
Contact Rate	25.1%	Agency made right party contact with homeowner receiving letter
Counsel Rate	36.2%	Agency counseled homeowner after contact
Delinquency Cure Rate	24.8%	Homeowners contacted by agency who cured their delinquency
Foreclosure Avoided Rate	27.1%	Homeowners contacted by agency who avoided foreclosure

Source: CredAbility, Freddie Mac EI Program Activity Report 2006-2012

Lessons Learned

In addition to these results, we have also learned some important lessons about how to make outreach contacts and engage homeowners through this process.

- Value of an Endorsed, Neutral Third Party. Homeowners who are hiding from their servicer are very skeptical of third parties. They are often bombarded with a variety of calls and solicitations from organizations that purport to want to help, but it is difficult to tell legitimate organizations from potential scams. Homeowners liked receiving a letter to introduce the counseling agency and to see the endorsement of the financial institution, even though they were afraid to speak directly to the financial institution themselves. By endorsing free access to a trustworthy nonprofit agency, the servicer showed that their true intent was to work with the homeowner to find a solution, not just to foreclose on the property.

- <u>Less Demand for Counseling than Expected</u>. While we were successful in contacting 25 percent of these delinquent borrowers, the rate of those agreeing to counseling was just 36 percent of the contacted group. Perhaps this low demand for counseling is the result of not wanting to interject a third party into the process or otherwise complicate working with the servicer. But it is unfortunate that these families missed out on an opportunity to address their entire financial picture and challenges and to take advantage of a wider variety of tools and programs versus just changing their monthly mortgage payment amount.
- <u>Cures from a Single Phone Contact</u>. We were surprised to see how many homeowners required just the nudge of call from a counseling agency to get them to act, resulting in a cured delinquency. This represents a remarkable return on investment and mission for counseling agencies, servicers, and homeowners alike.
- <u>Packages Remain Problematic</u>. The rate of document collection and submission is 20.3 percent for counseled clients, a rate for delinquent loans that is just too low to impact the overall problem. Financially distressed people are notoriously poor record-keepers and changing requirements during the early years of the crisis made it tough to pull together a package and get a decision within the allotted time frames. Progress continues and third parties like CredAbility are critical to this effort, but better systems (like the emergence of Hope LoanPort) and streamlining the movement of homeowners through a full range of retention and exit options needs more attention.

<u>Post Loan Modification (Post Mod) Support Program</u>

Since the early days of the housing crisis, when counseling was almost exclusively offered in person by most housing counseling agencies, engagement models with homeowners have been forced to evolve. From offering counseling via a national hotline to connecting homeowners with servicers to gathering documentation for decisions on workouts, counseling agencies have continued to adapt to the changing needs of the families we serve. The launch of Post Mod Support Program is just one of the latest examples of this continuing innovation.

Loan modifications quickly became the preferred tool in the attempt to keep homeowners in their homes, with more than 6 million government and private modifications completed since 2007. However, in the first wave of loan modifications redefault rates of 50-60 percent were common due to the focus on lowering mortgage payments or recapitalizing arrearages versus dealing with the client's whole range of financial problems and the lack of ongoing support for financially fragile homeowners. Many homeowners who have experienced delinquency on their mortgage need ongoing education, counseling, and coaching to successfully maintain homeownership. In our experience, it takes a family between 9 to 18 months to get into financial problems before they reach out for help and it takes 2-3 times that long to work out of the problem. In light of the client profile outlined earlier in this paper, it is clear that these families' financial challenges will not go away overnight.

Process

Started in 2009, our Post Mod Support Program is designed to engage and coach homeowners about how to manage their priorities and finances in order to maintain homeownership. After a loan modification is established, whether a trial or permanent mod, CredAbility provides outreach, counseling, education, and follow-up coaching to homeowners identified by an investor and/or servicer, following the process outlined below.

- Identifying Homeowners. The servicer sends to CredAbility a list of homeowners who have entered into a loan modification agreement and who have been targeted to receive the offer of ongoing support. This homeowner contact information includes: homeowner's name, phone number(s), street address, city of residence, zip code, investor and servicer loan number, payment amount (PITI), and payment due date.
- Extending the Offer. The homeowner receives a letter from the Investor or servicer, introducing CredAbility, describing the services available, and alerting the homeowner of CredAbility's intent to place an outbound call to the homeowner. The letter also includes a dedicated toll free number and dedicated web address that homeowners can use to contact CredAbility directly to get more information or to opt out of the program.
- Making Initial Contact. CredAbility makes at least three outbound call attempts per homeowner at three different times of day and on different days within a 30 day period. The conversation with the homeowner includes a live exchange of information (not just a

series of messages or voicemails) and information about the availability of free education and counseling resources. Having the homeowner agree to participate in ongoing outreach and/or a counseling session is targeted outcome.

- Counseling the Homeowner. For borrowers who accept the offer of free service, CredAbility schedules a telephone counseling session to be held as soon as possible and no more than 30 days following the date of the initial conversation with the homeowner. The first counseling session consists of a comprehensive review of the homeowner's current financial situation including:
  - A review and discussion of current debt payment obligations, including mortgage payments, with attention to trial modifications that could help the homeowner successfully achieve a permanent modification;
  - A review and discussion of credit report and score;
  - Creation of a budget designed to enable the homeowner to manage regular monthly obligations and household expenses and establish the foundation for long-term financial stability;
  - Identification of unsecured debt that may be compromising their financial situation and develop strategies to address it, including creation of a debt management plan or other debt reduction strategies;
  - Development of a personalized action plan for the individual/family to follow; and
  - Sending the homeowner a written summary of the session, including the action plan, educational materials, and additional resources.
- Offering a Second Counseling Session. The second counseling session consists of:
  - Education on how to maintain stable finances for the longer-term by addressing a broad range of financial concepts, remedial and preventive strategies and personal goals;
  - A review of credit report to ensure accurate reporting and address any issues; and
  - Modifications to the budget to achieve longer term goals such as: planning for expenses related to maintaining the home; establishing adequate emergency

savings; saving for retirement, education and other needs; and repayment of unsecured debts

- Ongoing Outreach. At the heart of the Post Mod Support Program is a regular series of contacts and conversations designed to build a relationship with the homeowner. CredAbility makes up to 10 monthly education and coaching check-in contacts to homeowners to offer additional assistance, including online educational resources and coaching on the action plan and budget during the 12 month period following initial acceptance of assistance. Contacts are broken up into three four month segments with specific content designed for each period. The goal of these scheduled contacts is to build a relationship with the homeowner by imparting relevant information to the homeowner in small doses at teachable moments. These periodic contacts are designed to not be too intense or intrusive and we employ a variety of methods, including telephone calls, emails, and texts. Counseling is always available as needed and these regular contacts offer a non-threatening way for homeowners to discuss emerging problems or recent events that might otherwise jeopardize the stability of their situation. This is important because it is typically four to six months after the modification is started that the first serious problem arises.

Promising Results

Early results are promising, with contact made with 49.7 percent of homeowners targeted and 85.9 percent accepting the offer for ongoing support. Additional results are shown in the following table (Exhibit 13) include:

Exhibit 13: CredAbility Post Modification Support Program Activity

Step	Activity	Percent	
Referrals Received	26,152		
Made Right Part Contact	13,005	49.7%	*of referrals*
- Opt Out	*1,833*	*14.1%*	*of contacted*
Entered Ongoing Support	11,172	85.9%	*of contacted*
Remained in Ongoing Support after 4 months	*6,012*	*62.7%*	*continued to next 4 month cycle*
Chose a Counseling Session	2,435	21.8%	*of participants*
- Second Session	*1,170*	*48.0%*	*of counseled*

Source: CredAbility, Post Modification Support Program Activity Report 2010-2012

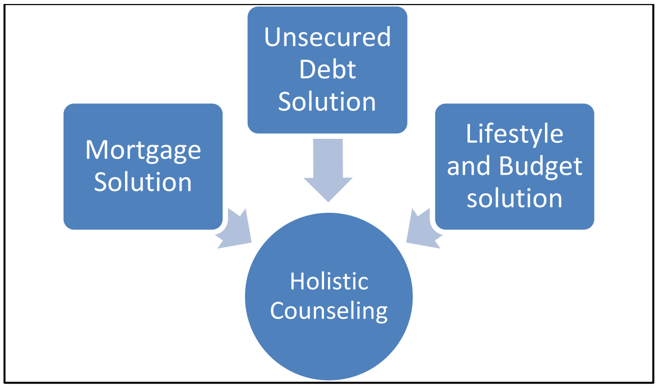
While loan performance for this group appears to be strong, results versus a randomized control group have not been released and we are not at liberty to discuss any results yet.

Other Models Emerging

We have recently started working on a new version of the Post Mod model developed by the Homeownership Preservation Foundation (HPF). The engagement strategy in this model is a deep, intense counseling-centered interaction. This model is designed to support the homeowner exclusively through a series of three focused, scheduled counseling sessions versus the ongoing outreach contacts in CredAbility's existing program. The core of these HPF counseling sessions includes:

- Extending borrower/counselor engagement to reinforce actions;
- Focusing on borrowers' total financial situation;
- Ensuring homeowners understand the terms of mortgage modification;
- Establishing realistic and specific action steps; and
- Offering financial education.

Exhibit 14: HPF Post Modification Support Program



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Source: Homeownership Preservation Foundation

The Four Stages of Treatment reflect include:

- Identifying consumer challenges and developing an action plan;
- Delivering accountability and progress reports;
- Creating sustainable habits; and
- Ensuring a final review and graduation from the program.

So while the outcome goals of both post mod programs are the same, namely creating sustainable homeownership, we are anxious to see how well this new approach increases homeowner success and long-term economic stability over the next few years. By comparing it with the CredAbility model, we will also learn more about the characteristics of homeowners who are most likely to engage and succeed in each particular model.

Lessons Learned

- Homeowners Like Regular Contacts. While we have a specific topic or agenda item to cover in each contact, these cumulative engagements build a relationship. Listening to recorded interactions between counselors and the homeowner show how quickly this rapport can be built and how appreciative they are of the continued support.
- Changing Habits Takes Time. Setting new goals and starting a new plan is always exciting, but sticking with it as life happens is hard. Being seen as a trusted third-party advisor opens

the door to offer suggestions and have tough conversations about the consequences of bad choices.

- Problems Will Happen. The fragile nature of homeowners' finances almost makes it inevitable that they will experience financial challenges in the first year of a modification. We see problems typically arise four to six months into the plan, which is why it is critical to have an established line of communication and access to a trusted advisor so that a homeowner can act quickly to address any problem before it spirals out of control.
- It Works. While we are not at liberty to share specific outcome data yet, our internal models show a sustained, positive benefit from this work to helping homeowners succeed.

Conclusion

At the beginning of this paper we challenged you to ponder these two questions – "What should we do to help this person?" and "What should they do to address their situation?" Unfortunately, even at this point, the answers are still not so clear or simple, but they are answers we need to find in order for us to move on and not repeat this crisis again. So instead of policy recommendations, we offer seven practical parting thoughts and observations for you to consider as we move forward:

1. **Reexamine conventional wisdom periodically**. Homeownership is not for everyone and our historical views of the value and benefits of homeownership proved to be false and damaging to many families. We need thought leaders to regularly and publicly examine and debate conventional views to ensure their validity in a rapidly changing world.
2. **Build margin into our lives**. We cannot make lending or borrowing decisions based on the assumption that things will always go well. We believe that consumers must be encouraged and required to maintain breathing room in their financial lives if they are to succeed in the uncertain world they will navigate in the years ahead.
3. **Understand that bad things happen to good people**. We must find ways to discern between sweeping events beyond an individual's control and poor personal choices. It seems obvious to most people that there are clear differences between an irresponsible real

estate speculator and a person who always paid their bills until being laid off and now cannot find another job, but designing an objective system to identify and rehabilitate such people on a continuum is very difficult.

4. **Engage overwhelmed and paralyzed people**. We must find new ways to communicate and engage with people struggling through a personal crisis. Crises take time to develop and even longer to resolve. Throughout that time frame, families remain very financially fragile and are almost guaranteed to face setbacks along the way. We must find simple ways for these people to have endorsed access to a neutral, trusted advisor and easier access to the tools and services that will enable them to resolve their situation.
5. **Require a comprehensive view**. We must view family finances through a holistic lens and fashion goals and solutions accordingly. In this crisis, housing debt often surfaced as the problem both because it is the single largest bill people face and because failing to pay has such dire consequences. However, at the heart of the problem was the layering of multiple risks and the mass of other debts that made the family's position untenable. Every lender needs to worry about these other debts because it affects their returns and losses.
6. **Understand that distressed people act perfectly "rational."** No one wants to be in trouble and it is a very hard mindset to understand unless you have experienced it. Homeowners observe their environment and act within this current context by focusing on what they can control. We saw this multiple times, from homeowners asking for a specific type of modification or principal reduction that a friend received to homeowners in judicial foreclosure states that stopped mortgage payments and refused very generous relocation or non-retention incentives because they understand the state's foreclosure timelines.
7. **Acknowledge there are no quick or easy solutions**. Like losing weight or staying healthy, it is not knowledge, but rather the willingness and discipline to do apply that knowledge that ultimately yields results. It requires time, support and the proper motivation to tackle and resolve the complicated financial problems that people in a crisis face. Unfortunately the money and resources for third-party counselors and advisors to assist in these types of situations always arrives late and leaves too early. We need sustainable fee-for-service funding models and infrastructure for those critical financial first-responders.