

The Effects of Foreclosure Counseling for Distressed Homeowners



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Motivation



- Recent recession and financial crisis largely driven by housing market collapse
- Housing prices peaked in April 2006, have declined since (down over 32% nationally)
- Currently, over 4.5 million households are seriously (90+ days) delinquent on their mortgages or in the process of foreclosure

Motivation



- Programs have been implemented by the federal government to help homeowners avoid foreclosure and keep their homes
 - Making Home Affordable Program (MHA)
 - \$400+ million for National Foreclosure Mitigation Counseling (NFMC) Program
 - Home Affordable Mortgage Program (HAMP)

Motivation



- However...
- Despite huge funding allocation to counseling, no convincing evidence that counseling improves borrower outcomes
 - Data limitations
 - Endogeneity between a borrower seeking counseling and mortgage outcomes (motivation, financial knowledge, location, etc)
- Lack of evidence may have resulted in zeroing out of ongoing Federal funding for counseling in FY 2012 budget

Study Goals



1. Examine the effect of mortgage default counseling on borrower outcomes controlling for endogeneity/unobserved heterogeneity
2. Examine whether the timing of counseling receipt affects borrower outcomes

Roles & Rationales for Default Counseling



- Complex contracts that targeted populations fail to understand
- Lack of information about alternatives including public and private programs
- Emotional distress as a barrier to information processing
- Trusted 3rd party advisor in time of hardship
- But...
 - Limited potential if income reduced or eliminated
 - Not substitute for regulation or legal remedies
 - Quality and availability are uneven

Default Counseling



What Does Counselor Do?

- Diagnose payment problem
- Revise income and expenditures
- Prioritize non-mortgage debts
- Maximize potential income
- Form repayment strategies, including modification or selling the home

Research Design & Data



- Main limitations of previous research is lack of consistent, and extended, time series of observations on borrowers both before and after counseling
- Also lack of a viable control group in the data used
- We address this problem by relying on a very large data set with monthly observations on subprime borrowers and their mortgages

Data



- National CTS dataset – 3 million unique loans
- Counseling hotline dataset on 550,000 borrowers
- 13,515 counseled borrowers matched by loan #
- Random sample of 23,305 unmatched
- June 2007 through December 2009
- 1,195,401 borrower-month observations
 - 5.1 percent received modifications
 - 2.6 percent of homes were lost to REO

Table 2. Summary Statistics for Counseled and Uncounseled Borrowers

Variable	(1) June 2007 Uncounseled	(2) June 2007 Counseled	(3) December 2009 Uncounseled	(4) December 2009 Counseled
Homeowner has received counselling	0	0	0	1
				0.0000
Counseled when current				0.4591
				(0.4984)
Counseled at 30 days delinquent				0.1178
				(0.3224)
Counseled at 60 days delinquent				0.0905
				(0.2870)
Counseled at 90 days delinquent				0.3325
				(0.4712)
REO (lost home to foreclosure)	0.0166	0.0002	0.0314	0.0442
	(0.1276)	(0.0129)	(0.1743)	(0.2055)
Received a modification	0.0012	0.0050	0.0490	0.1784
	(0.0340)	(0.0703)	(0.2160)	(0.3829)
Number of Months Delinquent	0.2610	0.2739	0.5407	0.7011
	(0.7908)	(0.7533)	(0.1118)	(0.4016)
Adjustable rate mortgage (ARM)	0.6418	0.7744	0.6271	0.7418
	(0.4795)	(0.4180)	(0.4836)	(0.4377)
Current loan APR	7.9399	7.6077	7.4641	6.4033
	(1.9029)	(1.4540)	(2.1210)	(1.6990)
Current FICO score	667.3814	669.4346	660.8284	657.6039
	(69.6494)	(66.1573)	(77.0485)	(82.7812)
Loan-to-value (LTV) ratio	83.2329	85.9021	83.2480	85.9021
	(15.9520)	(11.6921)	(15.9436)	(11.6925)
Current payment & interest	\$1,420.23	\$1,628.18	\$1,417.40	\$1,677.30
	(1,032.15)	(897.33)	(1,038.06)	(927.41)
Original balance	\$235,097.10	\$314,928.20	\$234,943.00	\$314,980.30
	(181,890.90)	(178,118.90)	(181,765.50)	(178,131.90)
Current loan balance	\$233,331.90	\$318,807.40	\$231,430.10	\$323,047.20
	(183,764.60)	(183,672.90)	(183,028.90)	(187,412.30)
Observations	23305	6042	23305	6042

Source: CTS national data. Standard deviations in parentheses. Summary statistics only presented for loans available in both June 2007 and December 2009 with no missing values on key variables.

Identification Strategy



- **Fixed Effects: time-invariant unobserved heterogeneity at the individual level**
 - affect both mortgage outcomes and the probability of seeking counseling (knowledge, motivation, social networks)
- **Instrumental Variables (IV)**
 - Decision to seek counseling is endogenous due to time-varying shocks or borrower characteristics that also affect mortgage outcomes.
 - Exploit exogenous variation in counseling by the timing and location of targeted citywide outreach events

Counseling Effects



Effects Vary Depending on When Counseling Occurs

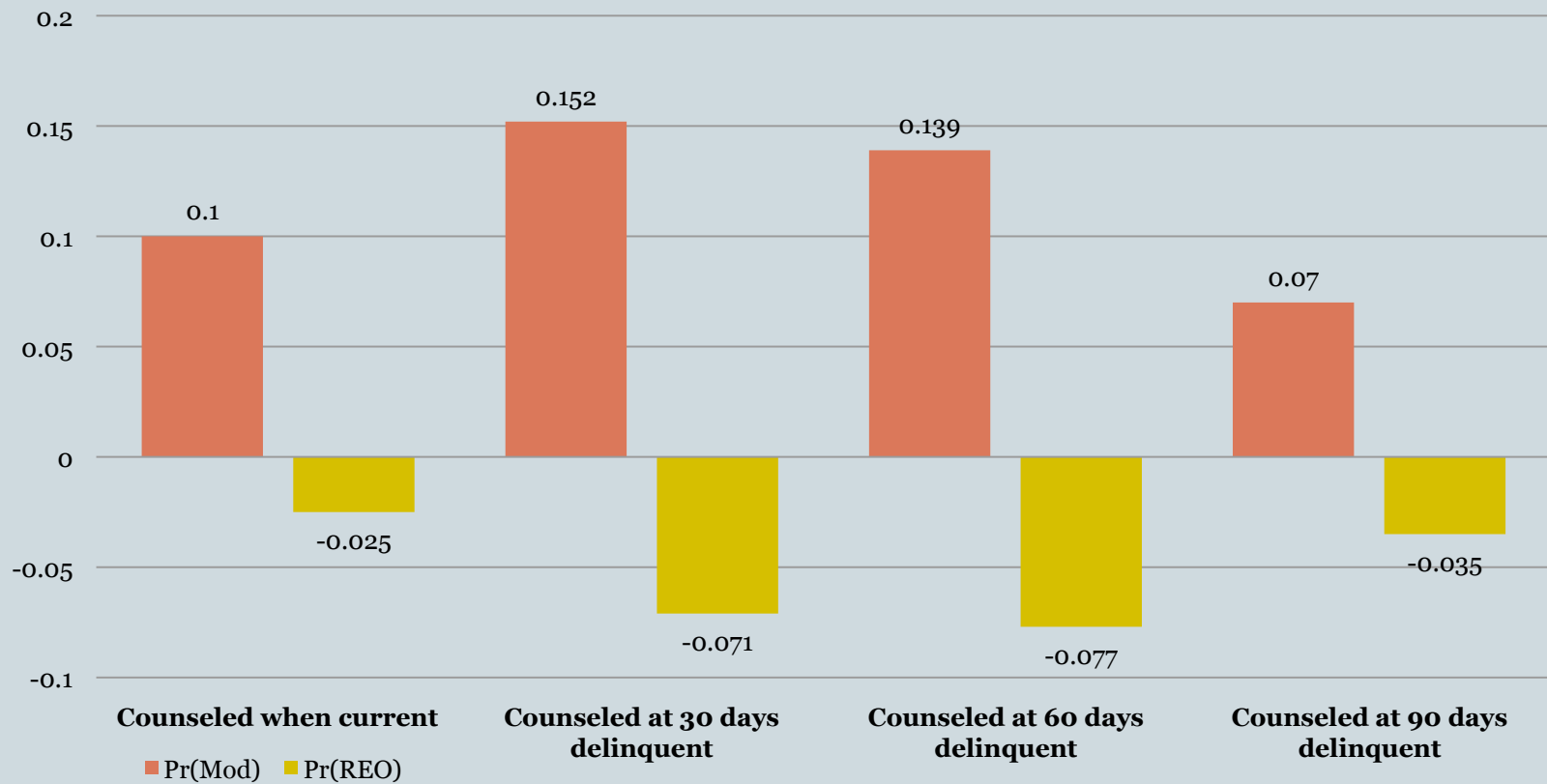


Table 5. LPM Versus IV Estimates of the Effect of Counseling on Receipt of a Loan Modification and Loss of Home to a REO Nationally

	(1) Received Loan Modification	(2) Received Loan Modification (IV)	(3) REO	(4) REO (IV)
Counseled	0.114*** (0.001)	0.575*** (0.074)	-0.040*** (0.001)	-0.004 (0.054)
Log current loan balance \$000	0.099*** (0.001)	0.273*** (0.033)	0.001 (0.001)	-0.015 (0.024)
Adjustable rate mortgage	-0.288*** (0.001)	-0.453*** (0.012)	0.004*** (0.001)	-0.004 (0.009)
Event city	0.114*** (0.001)	0.575*** (0.074)	-0.040*** (0.001)	-0.004 (0.054)
First-stage F-statistic		58.09		58.09
Num. obs	1195401	1195401	1195401	1195401

* p<0.05; ** p<0.01; *** p<0.001

Conclusions and Implications



- Selection into Counseling on Unobservable Characteristics
- Counseling increases likelihood of modification, some evidence that it reduces REO
- Timing Matters:
 - Early Intervention
 - ✦ Missed 1-2 payments
 - Late Intervention
 - ✦ Missed 3+ payments
- Transitional Support
 - Short sale or foreclosure auction

Thank You



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