U.S. Department of the Treasury
Federal Deposit Insurance Corporation

December 21, 2007

Honorable Barney Frank
Chairman
Committee on Financial Services
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

Thank you for your letter of December 11th. We appreciate the opportunity to clarify our understanding of some of the key details of the American Securitization Forum's (ASF) Streamlined Foreclosure and Loss Avoidance Framework for Securitized Subprime Adjustable Rate Mortgage Loans.

The goal of the plan announced on December 6th is to streamline the processes used by servicers to reach out to borrowers to avoid unnecessary foreclosures. The ASF Framework provides guidelines which the servicing industry may use to systematize the processes for identifying which borrowers can be fast-tracked into an extension of their starter rate for five years or longer and which borrowers will require more extensive loss-mitigation efforts to avoid unnecessary loss of their home. This Framework should make servicers more efficient and effective and free up resources so they can focus on those borrowers who need the most help. We hope that systematic modifications will be adopted as the standard practice across the entire industry.

It is important to view the ASF Framework as a tool to streamline the processes used to help distressed borrowers given the escalating volume of unaffordable resets occurring in the next 18 months. The ASF Framework is an initial step, and it will be evaluated in the coming months based on its success in achieving this goal.

The questions that you have posed involve many of the key aspects of the ASF Framework. While the industry developed this Framework and will be responsible for implementing it, the following is our understanding of its application based on extensive discussions and representations by ASF and its member institutions.

- **Five-Year Extension of the Initial Rate.** The ASF Framework describes three segments of borrowers. The first segment includes current borrowers who are likely to be able to refinance through FHA, FHASecure, or private mortgage products. The third segment includes borrowers who are delinquent at the starter rate. The second segment of borrowers -- those who are current but who are unlikely to make the reset payments and cannot obtain refinancing -- are the focus of the streamlined modification processes identified in the Framework.

For borrowers within segment two, the ASF Framework provides for a five-year or longer extension of the starter rate. By its terms, it does not preclude longer or shorter extensions. However, Treasury and the FDIC, along with other federal banking regulators, believe that a minimum of five years is essential to provide sustainable payments for the borrowers, to allow time for borrowers to refinance already expensive mortgage obligations, and to create predictability in the mortgage markets. We believe there is an emerging consensus within the industry that shorter extensions are not productive in today's environment. We will insist that ASF closely monitor implementation through reporting under the ASF Framework's Investor Reporting Standards to guard against unsustainable, short-term modifications.

- **Amortization.** The ASF Framework does not directly address whether interest could accrue at the higher reset rates during the period of the loan modification. However, we have been strongly assured by ASF and its member institutions that no interest at the higher rate would accrue against borrowers during the period of any modification. A borrower's obligation would be limited to the amortizing principal and interest at the starter rate during the modification period.

- **Will There Be Additional Consumer Costs.** While the Framework does not directly address this issue, ASF and its members have assured us that no costs will be imposed on consumers.

- **Prepayment Penalties.** The ASF Framework does not address the treatment of prepayment penalties that are part of substantial proportions of 2/28 and 3/27 subprime hybrid adjustable rate mortgages. However, by contract, prepayment penalties do not apply to modifications of existing loans to extend the starter rates. Such penalties only apply to the prepayment of the loan through sale or refinancing. The ASF Framework would only modify the interest rate. Most prepayment penalties expire concurrent with the interest rate reset. Thus, if the starter rate for a 2/28 loan were extended for five years, the prepayment penalty would expire at the original 2-year reset date, and no prepayment penalty would apply at any point during that subsequent five-year period. As a result, the borrower could prepay the loan without penalty at any time during the extended period.

  Any extension of the prepayment penalty would require a specific agreement with the borrower, and we have been assured by ASF that its members have no intention of seeking such extended prepayment penalties.

- **FICO Test.** The ASF Framework provides for an immediate fast-track modification for borrowers who cannot refinance and who have FICO scores below 660 and whose FICO scores did not increase more than 10% after origination. For these borrowers there would be no need to document the borrowers' income and, assuming they met the other segment two criteria, they would be fast-tracked into a loan modification at the starter rate. Borrowers with higher FICO scores *would still be eligible for a fast-track loan modification,* but it would require verification of their income in order to meet the servicer's duty to confirm that the borrower could not make his or her reset payments.

FICO scores have the advantage of allowing for verification without the need to contact the borrower. Thus, many of those homeowners who meet the FICO test can have their loans automatically modified without having to make contact with the servicer. While we are mindful of your concerns regarding incentives, we think the limited use of FICO scores -- designed to further speed up the process of providing loan modifications to subprime borrowers -- is acceptable.

- **Going Forward.** The ASF Framework is designed to speed up the process of providing appropriate loan modifications. It must be judged by its success in accomplishing this goal. We are committed to measuring progress and will ensure that these metrics are made public. While the ASF Framework is an initial step forward, we will continue to review its progress and work to make any necessary adjustments.

  One of the benefits of a streamlined process for borrowers with resetting loans who are currently paying the starter rate, but who cannot make the reset payments or obtain refinancing, is that it will free up resources to help servicers deal with the more difficult loans, such as those that are delinquent or are already struggling to make higher reset payments. These borrowers, described as part of segment three, will require more customized solutions if foreclosure can be avoided. Freeing servicer resources to respond to these borrowers is a critical part of an effective response.

We believe that servicers have the flexibility to respond to rising borrower stress. It is essential that they use this flexibility to respond in a systematic way to the volume of resetting loans through 2009. Some servicers have expressed concern about the potential for litigation by some investors. The ASF Framework, as the industry best practice, should help alleviate those concerns.

Thank you once again for the opportunity to address your questions about the ASF Framework. We look forward to continuing to work with you and the Committee to facilitate an effective response that avoids unnecessary foreclosures.

Sincerely,

Robert K. Steel
Under Secretary for Domestic Finance
U.S. Department of the Treasury

Sheila C. Bair
Chairman
Federal Deposit Insurance Corporation

cc: Honorable Spencer Bachus