

February 19, 2013

**Testimony Before the Banks Committee  
On  
House Bill 6355  
An Act Concerning Homeowner Protection Rights**

**From: Chandler J. Howard, President & CEO  
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Chairman Leone, Chairman Tong and members of the Banks Committee, good afternoon.

My name is Chandler J. Howard and I am the President and CEO of Liberty Bank of Middletown, Connecticut.

I'm here to testify on House Bill 6355, An Act Concerning Homeowner Protection Rights.

**LIBERTY BANK BACKGROUND**

Liberty Bank is the third-largest Connecticut-based bank, with \$3.5 billion in assets. We are the ninth largest residential lender in the state, last year writing 2,000 first mortgages (for a total of \$401 million) – the second-highest level in our history.

We are an active and growing residential lender, committed to the Connecticut market. We have been awarded an outstanding CRA rating since 2001, and we also have a long-standing track record of serving first-time homebuyers.

Liberty Bank is dedicated to ensuring that all our homebuyers can afford their mortgages and that they will be successful homeowners. Our adherence to prudent underwriting standards allows us to keep our foreclosure rate at a minimum.

As a community bank, we prefer, whenever possible, to work personally and in good faith with homeowners in hardship to resolve their mortgage payment issues.

We also pride ourselves on making available local loan servicing representatives. In fact, we commonly read in our customer evaluations that local servicing is why a customer chose us.

#### RESIDENTIAL LENDING TODAY

In 2012, Liberty Bank sold approximately 80 percent of its residential first mortgages in the secondary market while retaining the servicing on most of those loans. Twenty percent of first mortgages were retained in our portfolio.

Our existing (1 to 4 family) property forecloses stand at just eight (or \$1.9 million) as of December 31, 2012; investor-held mortgage foreclosures number four (or \$750,000).

We are required to use Workout Prospector, an automated system (developed by Freddie Mac) for all of our loans serviced for Freddie Mac when determining if a homeowner qualifies for a loan modification. For our portfolio loans, we do not currently use an automated system, but follow our own internal policies and procedures.

We prefer to work personally and in good faith with homeowners having hardships to resolve their mortgage payment issues at the earliest stages of delinquency to try to prevent their entering mediation or foreclosure. We begin making calls at 16 days past due to ascertain the situation and can have an arrangement with the customer before the account reaches delinquency status.

In 2012, our average foreclosure took 14 months; our worst-case foreclosure is still in process, so far taking 38 months, including 10 mediation sessions and many delayed sessions.

We comply with current Connecticut laws governing foreclosures and mediation; however this puts us at risk of fines and penalties assessed by Freddie Mac and Fannie Mae for tardy foreclosure resolution.

We agree with the prevailing opinion that the mediation/foreclosure process in the state of Connecticut is broken.

#### OBSERVATIONS ON PROPOSED BILL 6355

We believe that, far from ameliorating the current mediation/foreclosure process, Bill 6355 will make the situation worse. Potentially, it can further lengthen the now-onerous foreclosure process for homeowners in hardship, while causing unintended financial and employment problems for lenders.

Virtually all of the proposed changes anticipate potential lender/servicer misconduct with nothing explicitly acknowledging the potential for homeowners who fail to cooperate.

While mediation sessions would theoretically be held to three, the bill gives judges sweeping latitude to prolong the mediation process indefinitely. In addition, the elimination of the eight-month deadline for the standstill period would render the lender unable to respond while the homeowner has unlimited time to make new assertions.

New requirements for mediation participants to have “full settlement authority” do not take into account the vast majority of mortgages that are tied to a second party – Freddie Mac/Fannie Mae, FHA, private mortgage insurers, or second lien holders. Ignoring the rights of these parties would expose first mortgage lenders to excessive risk.

The Bill would require lenders to use the FDIC model to determine qualification for a loan modification. While this tool may be useful, mandating its use may lead to unintended results.

Borrowers will have new special defenses and counterclaims to use against lenders in a foreclosure action that are related to an endless range of issues (including those outside the foreclosure process and out of the control of the lender). This will undoubtedly increase the time and cost of foreclosure.

New proposed good faith standards are complex, encompass “any” applicable rule or guidance (which can be contradictory), and are simply unattainable. Yet, a finding that a party did not act in good faith does not require proof of malice, intent to injure, or bad faith, and may result in fines or sanctions.

## UNINTENDED CONSEQUENCES

With nearly five years passed since the financial crisis, it is safe to say that the vast majority of dishonest lenders are out of business. What remain are conscientious banks that have money to lend, want to lend, and that want to stimulate their local housing markets.

Yet, Bill 6355 imposes numerous one-sided, short-sighted provisions that clearly disincent banks from lending in their communities.

While we prefer to work one-on-one with homeowners in hardship for loans in our portfolio, mandated use of the FDIC model, as required by the bill, would clearly mean that those who fail would need to immediately enter the mediation/foreclosure process. Because a “regulation,” as the bill states, would also include “guidelines” that the FDIC has issued on loan modifications, this would create a black-and-white proposition and tie our hands for working with borrowers on loans held in our own portfolio.

As an experiment, Liberty Bank tested five of our mortgages currently in hardship. While in all cases, we modified their loans resulting in reduced payments, four of the five failed the FDIC test as required by the bill. Under the test, we would not have been able to offer a modification and, overall, this would limit the number of borrowers we could help.

Mandating the FDIC model would mean that we would no longer have any latitude to intercede, and that if we did, even in good faith, we would potentially be violating Fair Lending practices and open up the possibility that borrowers could raise claims in foreclosure if we deviated from the FDIC model.

Further delays in the mediation/foreclosure process will mean more fines, fees and penalties for lenders. Banks, already facing the thinnest profit margins in history (due to unprecedented low interest rates), will need to pass the cost onto the customer in the form of higher interest rates.

Connecticut home prices are already among the highest in the nation, while our housing market remains stagnant. Higher mortgage interest rates will be one more roadblock to stimulating home sales in the state.

In addition, higher interest rates would negatively impact first-time homebuyers and a portion of current refinance customers. They will not be able to afford loans.

Fear of resorting to a foreclosure – because the process is so onerous and one-sided – could also cause banks to re-price their products accordingly to offset the risk and to raise their underwriting standards to a level that only the most affluent or creditworthy could meet.

Many banks, including Liberty Bank, continue to service most of their loans so that our customers can contact someone locally if they have questions, need help, or have a hardship and get immediate answers or action.

When Liberty sells loans in the secondary market, a significant portion of our gain on sale comes from the present value of the loan servicing. Accounting rules require us to record this value on our balance sheet as an asset. We believe that this proposed legislation will result in Connecticut servicing rights being less valuable in the market and with regulators. If the value of those assets declines, we must write them down. Not an attractive outcome from a safety and soundness standpoint.

The consequence is an immediate hit to our earnings and to our capital. Every dollar of that capital equals ten dollars of loans to our customers. Less capital reduces the number of loans we can originate.

In addition, the depressed value of servicing will reduce our gain on sale for future originations requiring a higher interest rate to attain adequate profitability.

An additional unintended consequence may be for lenders to change their business models to sell their loans as “service released” to out-of-state companies to mitigate the risk to their balance sheets. While Liberty’s intention is to retain servicing, we expect that others may see this as a viable alternative.

This will result in a loss of jobs in Connecticut as banks outsource this important service in order to reduce risk and control costs. One more blow for an already too high unemployment rate.

## CONCLUSION

Liberty Bank is a community bank and, as such, a proponent of strong healthy communities. Homeownership and employment are the first building blocks of prosperous cities and towns.

We do not want to foreclosure on a property – except as a last resort – and we do not want to own property. A lengthy mediation and foreclosure process benefits no one, the banks, homeowners, neighborhoods, home values, or home sales.

We agree with the Bill’s proponents that the efficiency of the foreclosure process needs to be increased. However, the bill as drafted would only cause more delays and costs.

We are committed to working with the Banks Committee through the Connecticut Bankers Association to accomplish the objective of speeding the mediation and foreclosure process while protecting the interest of all parties.

Thank you for the opportunity to testify today and I’d be happy to answer any questions you may have.