**Testimony of David Lowman**
**JPMorgan Chase**
**Committee on Financial Services**
**United States House of Representatives**
**April 13, 2010**

Chairman Frank, Ranking Member Bachus and Members of the Committee, thank you for the opportunity to appear before you today. JPMorgan Chase shares your commitment to helping homeowners and stabilizing our nation's housing market.

My name is Dave Lowman, and I am the Chief Executive Officer for Home Lending at JPMorgan Chase. Chase is one of the largest residential mortgage originators and servicers in the United States, serving more than 9 million customers in every state of the country with mortgage and home equity loans totaling about $1.4 trillion. We are proud to be part of one of this country's pre-eminent financial institutions with a heritage of over 200 years, but we do not rest on our record. We work very hard to help all of our customers during these challenging economic times, including those who joined us as a result of our acquisition of the mortgage and other assets of Washington Mutual from the FDIC.

We are here today to discuss with you how we can make foreclosure prevention solutions more effective for homeowners. Our initial efforts were focused on providing affordable payments. We believe these efforts have been most successful for homeowners with a desire to maintain their homes and a reasonable ability to make and sustain an affordable monthly mortgage payment. There are also homeowners unable or unwilling to maintain home ownership. For these borrowers, solutions have been designed to provide an orderly sale of the property. There is a third category of homeowners who have suffered significant home price depreciation as a result of the downturn in residential real property values over the last few years. This is arguably the most challenging group. The vast majority of these homeowners are meeting their mortgage obligations. But there are also homeowners with the ability but unwillingness to pay due to loss of equity, as well as homeowners for whom an affordable payment might be structured but not without additional tools, including principal reduction. These are some of the issues I will address in my testimony today.

## Chase is Committed to Keeping Families in Their Homes

At Chase we are working very hard to help families meet their mortgage obligations and keep them in their homes by making their home payments affordable. As a national leader in foreclosure prevention, we have continued to expand upon and improve our programs to keep families in their homes, and we have helped prevent over 965,000 foreclosures.

From the beginning of 2009 and through the end of February 2010, Chase offered over 731,000 modifications to struggling homeowners and has completed over 110,000 permanent modifications under the Home Affordable Modification Program (HAMP), Chase's own proprietary modification programs and modification programs offered by the Government Sponsored Enterprises (GSEs) and FHA/VA. Chase has consistently been among the leaders in implementation of HAMP and other modification solutions for homeowners. Homeowners seeking loan modifications are first considered for HAMP and then considered for other modifications programs available through Chase if they are ineligible for HAMP.

| *CHASE MODIFICATION VOLUMES, 2009-2010 YEAR TO DATE*[1] | | | | |
|---|---|---|---|---|
| ***Key statistics*** | ***HAMP*** | ***Chase programs*** | ***Agency*** | ***Total*** |
| *Modifications Offered* | *229,819* | *253,977* | *247,553* | *731,349* |
| *Approved for Permanent modifications*[2] | *57,177* | *80,827* | *28,748* | *166,752* |
| *Permanent Modifications Completed* | *19,470* | *67,999* | *22,706* | *110,175* |

*[1] Year-to-date as of February 28, 2010*

*[2] "Approved for Permanent Modifications" includes both modifications made permanent as well as borrowers who are approved for a permanent modification but for whom the permanent modification has not yet been completed.*

To achieve these results, we have initiated extensive outreach and made significant investments in people, technology and our infrastructure. In particular, we have:

- Opened 37 Chase Homeownership Centers (CHOCs) in 15 states where struggling borrowers around the country can meet face to face with trained counselors, with 14 additional sites to be opened by the end of the April 2010, for a total of 51 centers
- Assisted more than 91,000 borrowers through our counselors at the CHOCs since their launch in early 2009
- Mailed over one million letters to invite Chase customers to discuss their situation or help them complete their HAMP documents
- Hired more than 3,580 loan modification counselors in 2009, bringing the total number of loan modification counselors to 6,258 in 15 sites in addition to the CHOC staff
- Hired additional mortgage operations employees, bringing the total number of Chase Home Lending employees dedicated to helping struggling customers to over 16,000 – nearly 50% of our total staff in Home Lending
- Handled over 12.8 million inbound calls to our call centers from homeowners seeking foreclosure prevention assistance in 2009 and through February 2010, including 2.4 million calls to our dedicated customer hotline for modification inquiries
- Launched a program for discounted sales and donations of foreclosed properties, through which we have completed over 530 transactions with non profit and state and local agencies in 24 states
- Hosted and participated in more than 471 homeowner events in 2009 and through February 2010 to educate and inform homeowners about the loan modification process and assist in the completion of required documents
- Instituted an independent foreclosure review process to avoid preventable foreclosure referrals and sales

**Chase Continues to Lend and Improve Affordability for Current Homeowners**

In addition to our programs to aid distressed homeowners, Chase has been active in continuing to provide mortgage credit and refinance opportunities to allow our borrowers to take advantage of historically low interest rates. In 2009 and through February 2010, Chase has originated more than $166 billion in residential mortgage credit. Of that amount:

- $15.7 billion in mortgage refinances have been originated through the Home Affordable Refinance Program (HARP).
- About 75% of HARP borrowers saved more than $100.00 on their monthly payments.
- $35.1 billion in new loans and refinances have been originated and insured through FHA/VA.

These programs offer high loan-to-value alternatives for borrowers who have good credit and mortgage payment history but may have experienced home price depreciation, making it difficult to qualify for a conventional mortgage loan.

The mortgage programs offered by Chase reflect our responsible lending principles. Chase did not originate, purchase or service Option ARMs but did acquire a portfolio of owned and serviced Option ARMs in 2008 when we acquired EMC (a subsidiary of Bear Stearns) and the mortgage assets of Washington Mutual Bank from the FDIC. Chase no longer originates subprime loans, or purchases mortgages originated by third party brokers (other than under the Rural Housing program). For loan originations to be sold to Fannie Mae or Freddie Mac or insured by FHA/VA, Chase has proactively established tighter credit criteria where it has observed poor historical borrower performance.

**Chase's Progress in Implementation of the MHA Modification Program**

Chase applauds the Department of Treasury's efforts to increase mortgage modifications industry-wide. Their efforts to standardize modification criteria through HAMP and publicize the program nationwide have benefited many struggling homeowners who would have otherwise faced foreclosure. The public response to the program was initially overwhelming and we have made significant investments to ramp up our modification capacity since our launch of the HAMP Program in April 2009.

As of February 2010, we estimate that we service approximately 437,000 loans that may be eligible for modification under the HAMP guidelines (about 50% of our total population of borrowers who are 60 days delinquent on their mortgage loans). On a weekly basis, Chase mails letters to borrowers with loans that become 50 days past due and meet basic HAMP eligibility criteria.

We have made solid progress in offering HAMP trial plans to about 230,000 homeowners and have over 150,000 homeowners in active trial plans through February 2010. We are now working very hard to convert homeowners to permanent HAMP modifications and have successfully converted about 20,000 homeowners but, like other servicers, we have faced challenges in getting borrowers to send in the documentation required to complete the modification.

We have added hundreds of employees in recent months who are dedicated to alerting customers and then collecting the documents needed to complete modifications. These initiatives have collectively increased the pace of HAMP modification completions at Chase from less than 1,000 a month in July and August 2009 to over 10,000 a month in January.

Very shortly, Chase will begin initiating trial plans under HAMP only after the borrower has provided the required documentation to support eligibility for the Program and will no longer commence trial plans based on stated information. This should greatly assist in shortening the period from initiation to permanent modification and increase our conversion rate, as borrowers should be motivated to provide the required documentation to receive the benefit of a reduced payment. As a result, failure to make timely payments should be the primary reason a borrower does not successfully convert from a trial plan to a permanent modification.

Despite some reports to the contrary, HAMP modification performance has been strong, helping hundreds of thousands of homeowners achieve affordable mortgage payments. At Chase, on average, homeowners are receiving a monthly payment reduction of $548.00 through their HAMP modification. That represents an average payment decrease of 29%. Based on Chase data, HAMP modifications appear to be performing noticeably better than modifications the industry has performed in the past. While it is still early in the program, 88% of completed HAMP modifications to date are current after three months of completion.

**Chase is Implementing More Help for Homeowners Under HAMP**

Chase, along with the other major servicers, has continued to work with the Department of Treasury on a number of HAMP initiatives that have been announced in recent months. Chase believes the process of creating standardized and consistent approaches among servicers through these programs is a major benefit for both homeowners and servicers.

**HAFA** – The Home Affordable Foreclosure Alternatives Program is designed for non-retention foreclosure prevention solutions, including short sales and deeds in lieu. Chase recently began offering the HAFA Program.

**2MP** – Chase is scheduled to roll out the Treasury Department's Second Lien Modification Program (2MP) in the second quarter of 2010, though the Program will not be effective under Treasury's recently re-issued Supplemental Directive until August 1, 2010.

2MP is a systematic approach to modifying all second liens where the underlying first lien has been modified under HAMP. 2MP also provides for a lump sum payment to the second lien holder to partially write down or fully eliminate a second lien, if it is determined to be in the best interest of the investor. If a homeowner remains current on both their first and second mortgage loan, they will be able to qualify for success payments under 2MP. Chase supports 2MP because it appropriately balances the interests of first and second lien investors and facilitates more comprehensive modification solutions for homeowners. We also think it will result in more second lien modifications by establishing a consistent process and common database of information for servicers to access.

**Temporary Assistance for Unemployed Borrowers** – We actively utilize temporary forbearance agreements today for unemployed borrowers, similar to the program contemplated by the recent announcement. When the details of the new government program become available, we will implement the program within the timeline set forth by the Department of Treasury.

**HAMP Expansion to FHA Loans** – Chase currently offers a similar program for its own portfolio, facilitating FHA refinances for current borrowers who need help meeting FHA loan-to-value limits or debt-to-income ratios but otherwise meet FHA underwriting standards. We use principal adjustments or below market interest rates to assist these borrowers to refinance. We are pleased to see that FHA is expanding its product options to help underwater homeowners and we expect to offer the program to our customers once FHA issues the program parameters. While we believe this will be a beneficial program, our experience suggests there may be limited acceptance by consumers. Similar to the Chase program, only current borrowers can qualify.  We find many current homeowners are reluctant to participate in a program that may harm their credit record due to the principal reduction feature.

**Alternate Waterfall under HAMP for Earned Principal Reduction** – The Administration has released the broad outlines of this initiative to consider principal reduction higher up in the waterfall to encourage more principal reductions and more positive outcomes. However, a number of open issues remain, including how the Net Present Value (NPV) model will be re-calibrated, how the re-default assumptions will be changed, and the allocation of principal reduction amounts among lien holders.

With only a limited amount of information available, it is difficult at this time to quantify how many more homeowners will become eligible under the alternate waterfall or how many more homeowners will have an improved NPV.  Chase will continue to work with the Department of Treasury and other interested parties as it has throughout the development HAMP to help develop the detailed requirements needed to implement this aspect of HAMP.  Once these details are finalized, we will be able to better assess how effective the revised waterfall may be and whether it makes sense to use it.

**Chase and Second Liens**

The Committee has asked in particular about the role of second liens in foreclosure prevention.  It may be helpful to understand more about Chase's second lien portfolio.

Chase owns about $131 billion in Home Equity loans and lines as of February 28, 2010.

- Approximately $25 billion are home equity loans and $106 billion are home equity lines of credit.
- Approximately $33 billion are in first lien position and $98 billion in second lien position.
- 5% of Chase's home equity portfolio is 30 days or more delinquent.  Total home equity line, home equity loan, first lien and second lien delinquency rates are within two percentage points of the overall total.
- About 50% of the total Chase second lien portfolio is underwater, and 95% of this portfolio is performing (less than 60 days past due).  30% of second lien mortgages have combined loan-to-value ratios over 125% and 94% of this portfolio is performing.
- For $40 billion of Chase-owned second lien mortgages, Chase also services a first lien mortgage:
    - 92% of these first lien mortgages are performing.
    - 28% of these first lien mortgages are by themselves underwater (loan- to-value ratio of over 100%).
    - 45% of first lien mortgages have a combined loan- to-value ratio of over 100%.
- About 10% of Chase's total serviced portfolio of first lien mortgage loans has a Chase-owned second lien.
- Our best estimate is that about 20% of Chase serviced first lien mortgages may have a second lien from another lender and about 70% *do not* have a second lien.

Chase uses appropriate and accepted accounting standards to value our second liens.  When a loan becomes more than 150 days delinquent, we write it down to its current fair market value.  This policy is applied consistently irrespective of whether the loan is in a first lien or second lien position and conforms to GAAP and regulatory accounting requirements which are closely supervised by the OCC and our independent auditors.

Struggling homeowners need help on more than their second mortgage. As the payments on the first mortgage tend to be far larger, the homeowner gets far less relief from a second lien modification than from a first mortgage modification. On average, pre-modification second lien mortgage payments are about 10% of a homeowner's monthly gross income compared to approximately 45% for the first mortgage payment and approximately 20% for credit card, auto and other debt. Chase believes both first and second liens need to be modified appropriately to achieve affordable payments.

It is important not to confuse *payment* priority with *lien* priority. In almost all scenarios, second lien holders have rights equal to a first lien holder with respect to a borrower's cash flow. The same is true with respect to other secured or unsecured debt, such as credit cards or car loans. Generally, consumers can decide how they want to manage their monthly payments. In fact, almost 64% of borrowers who are 30-59 days delinquent on a first lien serviced by Chase are current on their second lien. It is only at liquidation or property disposition that first lien investors have priority.

We routinely modify our second liens -- whether or not we own the first mortgage. We have offered almost 54,000 second lien modifications from 2009 through February 2010, 12,000 of which have been made permanent. Approximately 45% of second lien modifications were completed on loans where we do not service the first lien. We have the same economic incentive to help willing borrowers make their payments on second liens as on first liens.

Chase also has an established procedure to facilitate re-subordinations for any refinance that results in the borrower having an improved position through the refinance. In 2009 through February 2010, Chase received over 83,000 re-subordination requests and approved 82%.

Similarly, we have an established process to address requests we receive for the release of second liens we hold to facilitate a short sale by the homeowner. Also, as mentioned earlier, we have implemented the HAFA Program which will help facilitate the short sale process. We are committed to continuing to find the right balance for homeowners and investors in addressing second liens.

**Concerns about Broad Based Principal Reduction**

There are certainly individual cases or even segments of borrowers where a program that incorporates principal reduction is appropriate. For example,

- Certain Option ARM borrowers with very low payments may need some amount of principal reduction to achieve an affordable and sustainable monthly payment. We are in the process of finalizing the design and obtaining any required regulatory approvals for such a program for the Chase-owned portfolio.
- Current borrowers who otherwise are eligible under standard FHA underwriting guidelines may need some principal reduction to fit within FHA's loan-to-value or debt-to-income parameters. We currently offer this program for mortgage loans we own.
- Delinquent borrowers who qualify for FHA Hope for Homeowner loans may also need either principal reduction or a second lien extinguished. We plan to begin offering an H4H refinance option this summer.

We are also conducting targeted tests for other high risk borrowers to see if a principal reduction program is more effective and how those loans perform relative to other modification solutions we currently make available. Once we observe the results of these tests, we will be able to better evaluate the effectiveness of a broader principal reduction program.

We do think that large scale, broad–based principal reduction programs raise serious policy concerns, for both first and second lien mortgage loans, and particularly for current borrowers with an ability to repay their obligations. In Chase's view, such programs could be potentially very harmful to consumers, investors and future mortgage market conditions – and should not be undertaken without first attempting other solutions, including more targeted modification efforts.

Like all loans, mortgage contracts are based on a promise to repay money borrowed. Importantly, there is no provision in the mortgage contract, express or implied, that the lender will restore equity or reduce the repayment amount if the value of the collateral – be it a home, a car or a stock market investment – depreciates. If we re-write the mortgage contract retroactively to restore equity to any mortgage borrower because the value of his or her home declined, what responsible lender will take the equity risk of financing mortgages in the future? What responsible regulator would want lenders to take such risk?

We are also concerned that broad-based principal reduction could result in reduced access to credit and higher costs for consumers if market risk to lenders and investors materially increases. Borrowers likely will be required to increase their down payments, credit criteria will be further tightened and risk premiums for mortgage credit will increase and get passed on to consumers. Less affluent borrowers would likely be harmed disproportionately.

The benefits of a broad-based principal reduction program are to a large degree unknown and in Chase's view, outweighed by the risks and the facts that we do know.

- Our data show that our re-performance rates for first lien modifications based on verified income are performing reasonably well and perform without a strong correlation to loan-to-value (LTV) ratios. In fact, we see better performance in loans in the over 120% LTV band than the 90-120% band. This is because modification performance is correlated more strongly to affordability (i.e., payment reduction) than to LTV, which has little to do with affordability.

- Our data also show that second lien modifications are not an impediment to first lien modifications. Our HAMP first modification completion rate is virtually the same whether or not we are aware of the existence of a second lien.

- Moreover, it is unclear how much principal reduction would be required to reduce delinquencies among underwater borrowers, making it extremely difficult to measure the economic losses for investors, first or second, in following such an approach.

    - More than 70% of underwater borrowers are current on their mortgage obligations.
    - Academic research suggests borrowers' willingness to pay does not begin to erode until combined loan-to-values exceed 110%.[1]
    - Over 60% of Chase-serviced first mortgage borrowers who are underwater are higher credit quality GSE or prime loans and 78% of those are performing.

[1] Guiso, Luigi, Paolo Sapienza, and Luigi Zingales (2009). "Moral and Social Constraints to Strategic Default on Mortgages",Working Paper, European University Institute, University of Chicago, and Northwestern University.

- 43% of Chase-owned prime borrowers who are current but underwater have credit scores of 700 or more.

Many borrowers remain current on their home equity loans because they want to honor their obligations and protect their credit.[2] Our data show that 97% of borrowers in Chase's $98 billion second lien portfolio are performing on their loans (less than 60 days past due). For second liens that have a cumulative loan-to-value ratio greater than 100%, 95% of borrowers are performing. Regardless of loan-to-value, as long as borrowers continue to do the right thing and fulfill their contractual obligations, second liens that are current and producing cash flow to investors have value.

Additionally, a broad-based second-lien principal reduction plan would be forgiving past consumption by borrowers rather than housing investment. According to both internal Chase and Federal Reserve data, over 50% of borrowers used home equity loan proceeds for repayment of debt or personal consumption. No more than 15-20% used home equity proceeds to purchase a home. A broad-based program of principal reduction would be very expensive. To bring underwater borrowers "even" to a loan to value ratio of 100%, we estimate:

- It would have an industry-wide cost of $700 billion to $900 billion.
- The cost to Fannie Mae, Freddie Mac and FHA alone would be in the neighborhood of $150 billion.
- The Federal Reserve and Department of Treasury would have additional exposure through their ownership interests and risk guarantees of AIG, GMAC, and other institutions.
- Mortgage lenders would incur a significant reduction in capital now, potentially impairing their ability to extend future credit – mortgage or otherwise.
- And if house prices decline further, the costs would be even higher, representing the implicit "put" at 100% CLTV.

Given all these uncertainties and the potential magnitude of economic losses, Chase believes the proper balance among the interests of all the parties is achieved through the basic HAMP waterfall and perhaps the new alternate HAMP waterfall, once it is finalized and evaluated, combined with 2MP. These programs are specifically designed for homeowners who are either already delinquent on their first mortgage loan or where default is reasonably foreseeable based on the borrower's demonstrated risk characteristics.

Under HAMP, the consumer gets the same affordable monthly payment through principal deferral, with the potential under the alternate waterfall to earn equity over time. To the extent the borrower has both a first and second lien, a second lien modification under 2MP will create a more comprehensive solution. If home prices appreciate over time, the first and second lien investors appropriately retain the ability to benefit. Meanwhile, 2MP provides a mechanism for the second lien investor to share appropriately in the modification process so it does not disproportionately impact the first lien investor.

Finally, responsible lenders and major servicers are offering programs that incorporate principal reduction features for borrowers who most need that type of assistance, based on the characteristics of their particular portfolio of loans. We believe these types of targeted solutions are more appropriate.

[2] According to a recent survey conducted by Fannie Mae, "Respondents ranked negative impact on credit score (35 percent) and moral qualms (33 percent) as more likely factors for motivating them to pay their mortgage." *Fannie Mae National Housing Survey Fact Sheet, dated April 8, 2010*, p.4

**Principal Reductions in Securitized Transactions**

A program of systematic principal reductions would require investors in these securitized pools of first mortgage loans to approve principal reductions. Investors have generally not directed Chase to make these principal reductions, which is not surprising because 78% of the underwater loans that we service in prime private label securitized transactions are performing.

Additionally, as these loans are pooled in securities, principal reductions are generally not permitted without specific instructions. That's because modifications, as contemplated under most Pooling and Servicing Agreements (PSAs), do not include and may even prohibit a permanent reduction in principal. We do service some transactions that specifically permit principal reduction for delinquent loans or loans in imminent default, if the NPV of the principal reduction is greater than the anticipated foreclosure recovery, but this is not typical and there are usually limitations on the percentage of loans in the pool that can be modified. We also service transactions where the servicer is required to absorb any deficiency caused by accepting a principal reduction in liquidation. We would be concerned that this same approach would be applied to principal reductions accepted by the servicer in a modification without investor consent, transferring an unanticipated loss to the servicer.

The process to change a private label PSA to permit principal reductions would require an amendment to the Agreement to be executed by all the parties (depositor, trustee, servicer, master servicer and insurer, if applicable) and, in some cases, 51% or more of the certificate holders. In our experience, amending a PSA is a very difficult process.

Similarly, to date, we have not been permitted to reduce principal on loans in Fannie Mac or Freddie Mac securities. As we understand it, under their securitization documents, they would be required to first buy a loan out of a pool and make the investors whole before principal could be reduced. This would cause Fannie Mae and Freddie Mac to incur significant losses for loans that may be current and producing cash flow to investors.

**We Focus on Making the Monthly Payments Affordable**

The cornerstone of HAMP, as well as other modification programs available through Chase, is to achieve an affordable monthly payment for homeowners who have demonstrated a willingness to stay in their homes and an ability to make a reasonable monthly housing payment. We focus on affordability because it is, by far, the largest issue driving mortgage delinquency today. There are many reasons borrowers face affordability issues. In our experience, the number one reason is a recession-driven decline in income, whether it is a spouse losing a job, fewer hours at work, underemployment, or finding a new job that pays less than the previous one. Data from Federal Housing Finance Agency suggest that 75% of mortgage defaults nationwide are caused by issues of affordability: borrowers default when a life event (or a cumulative set of life events) causes them not to be able to pay their mortgage with income and savings.

As servicer, we have a contractual obligation to our investors, a social responsibility to our borrowers and an economic incentive to make loan modifications available when a modification incurs a smaller loss than a foreclosure. To achieve an affordable payment, we have been following the year-old HAMP waterfall of reducing the interest rate, extending the term and, where needed, deferring principal into a non-interest bearing final payment. As noted above, these modifications have resulted in an average monthly payment reduction of 29%, or $548.00, for our borrowers.

Recently, the Administration announced an alternate HAMP waterfall that will factor earned principal reduction into the NPV calculation for a modification. We know this will be surprising to some, but we have found that rate reductions and term extensions – not principal reductions – have the largest impact in achieving payment affordability and result in more modifications.

When the NPV calculation rules out a modification or when the homeowner has insufficient means to make a reasonable monthly payment, we try to determine whether the family's challenges are temporary. If so, we may offer a forbearance plan, similar to the Temporary Assistance Program for the unemployed recently announced by the Administration. If not, we will act in the best interest of the investor and consider solutions such as short sales or deeds in lieu of foreclosure.

**Looking Ahead**

Many new tools have been developed in recent months to help address lessons we have learned through the HAMP roll out as to where gaps existed in helping more homeowners. As with the basic HAMP Program, which has now gathered significant momentum, it will take some time to get the new initiatives up and running smoothly but Chase believes these are the right steps to be taking now and will benefit many homeowners.

Additionally, Chase continues to believe there are opportunities to refinance some borrowers into more sustainable FHA mortgages – including some with principal reduction – through the Hope for Homeowners program and potentially the recently announced FHA initiatives. These programs require an individual review of each borrower's situation to make sure the new mortgage is affordable and sustainable and the principal reduction is justified by the benefits of the transaction.

There are still some borrower segments that will require more customized solutions, such as the unemployed, borrowers with very low initial payments or borrowers with affordable mortgage payments that are highly leveraged with other debt. Chase continues to work to find solutions for all its borrowers who can show reasonable ability and willingness to sustain a mortgage loan, including principal reduction where appropriate.

We are pleased to have this opportunity to share our progress with you. We look forward to continuing to work with the members of Congress, the Administration, our federal banking regulators and our community partners in implementing these initiatives to help families and to stabilize neighborhoods and the U.S. economy.

## APPENDIX: Chase Loan Modification Programs

In October 2008, we expanded the loan modification alternatives Chase already offered as part of our proprietary Foreclosure Prevention program. The enhanced modification tools allow for more flexibility based on the borrower's current loan type and the borrower's specific financial situation.

### Proactive Outreach for ARM borrowers

Chase-owned subprime hybrid Adjustable Rate Mortgages (ARMs) scheduled to reset for the first time are being modified to remain at the initial interest rate for the life of the loan. Borrowers qualify for this program if they have a clean payment history on a hybrid ARM with an interest rate that adjusts after the first two or three years. Borrowers do not need to contact Chase to benefit from this program – the rate lock is implemented automatically – and borrowers are so advised.

We use the ASF Fast Track program to reduce payment shock for subprime hybrid ARMs serviced but not owned by Chase and scheduled to reset for the first time. Qualifying borrowers will have their initial ARM rate frozen for five years.

Chase did not originate or purchase Pay Option ARM loans itself but does own and service a portfolio of Pay Option ARM loans as a result of the 2008 acquisitions of the mortgage assets of Washington Mutual from the FDIC and EMC, a subsidiary of Bear Stearns.

To help borrowers with Pay Option ARMs, Chase makes available loan modifications through HAMP and its own proprietary modification programs. In 2009 and 2010, we also offered a proactive program for Chase-owned loans, developed specifically to assist current Option ARM borrowers who may be at higher risk of default due to a scheduled recast in the next 12 months that could significantly increase their monthly payment. To minimize any potential payment shock, we made the borrower a pre-approved offer to modify their loan to a lower fixed rate loan that keeps their payment at its current amount, which they have already demonstrated the ability to pay. If this payment amount results in a lower-than-market interest rate, the rate can step up to market over time, subject to certain limits to avoid payment shock. High risk borrowers due to recast in 2009 were mailed proactive outreach offers starting in the first quarter of 2009, to which over 85% responded. In the last quarter of 2009, we began mailing pre-approved modification offers to about 5,000 additional borrowers whose loans were due to recast this year. In total, we have completed nearly 5,000 modifications for Option ARM borrowers under this program since 2009.

Under our various programs, Chase has completed modifications of over $7 billion of Pay Option ARMs (over 16,000 units) since 2009 through rate reduction, term extension or proactive outreach. In addition to completed modifications, there are customers active in trial modifications under HAMP and Chase modification programs (to the extent they are ineligible under HAMP) that are not yet included in the completed modification figure.

### Chase Custom Modifications

Borrowers not eligible for HAMP or any of the systematic Chase modification programs described above are reviewed on a case-by-case basis to determine the suitability of a modification or other foreclosure prevention approach.

Chase custom loan modifications for first liens are evaluated by developing an estimated target affordable payment of 31% to 40% of the borrower's gross income. We use the lowest percentage for borrowers with the lowest incomes. Once the target payment is calculated for the borrower, we will test each modification option to see if it will get the borrower to an affordable payment. Concurrently, we apply a net present value (NPV) analysis to each option to determine whether the value of the modification exceeds the value expected through foreclosure. We recommend the modification option that produces both an affordable payment and a positive NPV result. In addition, Chase custom loan modifications offer broader eligibility and payment flexibility compared to HAMP.

**Other Foreclosure Prevention Options**

In addition, Chase offers other foreclosure prevention options, such as:

- Payment plans (where a borrower agrees to pay back arrearages over time),
- Deferments (where a borrower agrees to make late payments in the future),
- Borrower stipulations (where a borrower agrees to make a set of payments, often as a prelude to a modification), and
- Short-sales / settlements (a form of principal forgiveness where Chase agrees to accept less than the amount of the mortgage in exchange for the underlying property or the proceeds of the sale of the underlying property).

Although borrowers do not keep their homes in short sales and settlements, these may be appropriate solutions when the borrower has no interest in remaining in the home or simply cannot afford the home over the long term, even if payments are reduced by a modification.

**Our Community Stabilization Initiatives**

Not every foreclosure can be prevented, so it is vital to our communities to look beyond foreclosure prevention to deal with the impact of foreclosed properties on neighborhoods. In 2008, Chase established a dedicated unit under its Homeownership Preservation Office to develop strategies to deal with foreclosed properties, working with our partners in the community and our banking regulators.

As part of our announcement in 2008, Chase committed to donations or discounted sales of 500 foreclosed properties over the next 2-3 years. In just a little over one year, we met our goal of 500 completed transactions. Through February 2010, we have donated or sold at a discount over 530 properties to non-profit organizations in 24 states.

We know that the HAMP program has been difficult for servicers to implement and that has affected our customers' experience. We know that we are accountable to help our borrowers and work to make HAMP a success, but we should also remember that a significant amount of progress has been made in a very short period of time. Right now, among all the HAMP participants, nearly 1.1 million homeowners are benefiting from more affordable monthly mortgage payments by entering into HAMP trial plans – and the number continues to grow. We are working very hard to convert trial plans to permanent modifications and help make HAMP a success. At Chase alone, over 110,000 homeowners have been approved for or entered into permanent modifications under HAMP or the other loan modification alternatives we make available to homeowners.