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Credit Card Companies Willing to Deal Over Debt

By [ERIC DASH](#)

New York Times

January 3, 2009

Hard times are usually good times for debt collectors, who make their money morning and night with the incessant ring of a phone.

But in this recession, perhaps the deepest in decades, the unthinkable is happening: collectors, who usually do the squeezing, are getting squeezed a bit themselves. After helping to foster the explosive growth of consumer debt in recent years, credit card companies are realizing that some hard-pressed Americans will not be able to pay their bills as the economy deteriorates.

So lenders and their collectors are rushing to round up what money they can before things get worse, even if that means forgiving part of some borrowers' debts. Increasingly, they are stretching out payments and accepting dimes, if not pennies, on the dollar as payment in full.

"You can't squeeze blood out of a turnip," said Don Siler, the chief marketing officer at MRS Associates, a big collection company that works with seven of the 10 largest credit card companies. "The big settlements just aren't there anymore." Lenders are not being charitable. They are simply trying to protect themselves. Banks and card companies are bracing for a wave of defaults on credit card debt in early 2009, and they are vying with each other to get paid first. Besides, the sooner people get their financial houses in order, the sooner they can start borrowing again.

So even as many banks cut consumers' credit lines, raise card fees and generally pull back on lending, some lenders are trying to give customers a little wiggle room. [Bank of America](#), for instance, says it has waived late fees, lowered interest charges and, in some cases, reduced loan balances for more than 700,000 credit card holders in 2008.

[American Express](#) and Chase Card Services say they are taking similar actions as more customers fall behind on their bills. Every major credit card lender is giving its collection agents more leeway to make adjustments for consumers in financial distress.

Debt collectors, who are typically paid based on the amount of money they recover, report that the number of troubled borrowers getting payment extensions has at least doubled in the last six months. In other cases, borrowers who appear to be pushed to the brink are being offered deals that forgive 20 to 70 percent of credit card debt.

"Consumers have never been in a better position to negotiate a partial payment," said Robert D. Manning, the author of "Credit Card Nation" and a longtime critic of the credit card industry. "It's like that old movie 'Rosalie Goes Shopping.' When it's \$100,000 of debt, it's your problem. When it's a million dollars of debt, it's the bank's problem."

The recent wave of debt concessions is a reversal from only a few years ago, when consumers usually lost battles with their credit card companies. Now, as bad debts soar, it is the lenders who are crying mercy.

Credit card lenders expect to write off an unprecedented \$395 billion of soured loans over the next five years, according to projections from The Nilson Report, an industry newsletter. That compares with a total of about \$275 billion in the last five years.

All that bad debt is getting harder to collect. In the past, troubled borrowers might have been able to pay down card loans by tapping the equity in their homes, drawing on retirement savings, taking out a debt consolidation loan, or even calling a relative for help. But with credit tight, consumers are maxed out.

"Knowing that the sources of funding have dried up, having someone pay the balance in full isn't a viable strategy," said Tim Smith, a senior executive at Firstsource, one of the biggest debt collection companies.

Lenders are reluctant to admit they will accept less than full payment, lest they encourage good customers to stop paying what they can. Industrywide data is scarce.

Unlike the huge mortgage loan modification programs that are taking place, which address thousands of mortgages at once, workouts for credit card customers are still being handled on a case-by-case basis.

In addition to debt forgiveness, debt collectors are allowing many delinquent borrowers to pay down their debt over the course of a year rather than the standard six months.

Paul Hunziker, the chairman of Capital Management Services, said that before this downturn, his firm put only about a quarter of all borrowers into longer-term repayment plans. Now, it puts about half on such plans.

Some lenders are also reaching out to borrowers shortly after they fall behind on their payments to try to avoid having to write off the account. Others are reaching out to customers who seem likely to fall behind. Just as lenders competed for years to be the first card to be taken out of the wallet, they are now competing to be the first ones paid back.

And realizing that millions more consumers are likely to default on their credit card bills in the coming months, the banking industry has started lobbying regulators to make it more advantageous to lenders to extend payment terms or forgive debt.

In an unusual alliance, the Financial Services Roundtable, one of the industry's biggest lobbyists, and the Consumer Federation of America recently proposed a credit card loan modification program, which was rejected by regulators.

Under the plan, lenders would have forgiven about 40 percent of what was owed by individual borrowers over five years. Lenders could report the loss once whatever part of the debt was repaid, instead of shortly after default, as current accounting rules require. That would allow them to write off less later. Borrowers would have been allowed to defer any tax payments owed on the forgiven debt.

Landmark changes to bankruptcy legislation passed in 2005, for which the industry aggressively lobbied, seem to have hurt card debt collections. Credit card industry data indicate the average debt discharged in Chapter 7 bankruptcy has nearly tripled since 2004. And in Chapter 13 bankruptcies, secured lenders like auto finance companies routinely elbow out unsecured lenders like card companies, trends that have contributed to the card lenders' willingness to settle. Borrowers should not expect sweetheart deals. Card companies will offer loan modifications only to people who meet certain criteria. Most customers must be delinquent for 90 days or longer. Other considerations include the borrower's

income, existing bank relationships and a credit record that suggests missing a payment is an exception rather than the rule.

While a deal may help avoid credit card cancellation or bankruptcy, it will also lead to a sharp drop in the borrower's credit score for as long as seven years, making it far more difficult and expensive to obtain new loans. The average consumer's score will fall 70 to 130 points, on a scale where the strongest borrowers register 700 or more.

For the moment, it may be easier for troubled borrowers to start negotiating a modification by contacting the card company or collection agency directly. Credit counselors can help borrowers consolidate their debts and get card companies to lower their interest payments and other fees, but they currently cannot get the loan principal reduced.

Another option is for a borrower to sign up a debt settlement company to negotiate on her behalf. But regulation of this business is loose, and consumer advocacy groups warn that some firms prey on troubled borrowers with aggressive marketing tactics and exorbitant upfront fees.

More Banks May Become Private

By Kathy Chu

USA Today

January 5, 2009

The pending sale of IndyMac Bank to investment firms is likely the start of an era in which banks, generally considered the most public of institutions, will increasingly fall into private hands.

On Friday, regulators announced they had signed a letter of intent to sell the troubled mortgage lender for nearly \$14 billion to a group led by private-equity firm Dune Capital Management. The government has been searching for a buyer for IndyMac since July, when it collapsed after customers withdrew \$1.3 billion in 11 days on worries about the thrift's solvency.

Private-equity firms and hedge funds have long been able to own stakes in banks. But regulators' willingness to allow these entities to buy banks outright is "historic," says Scott Talbott, senior vice president of government affairs for the Financial Services Roundtable, which represents banks.

The deal "represents the economic pressure on banks, and the demand (on

regulators) by the extraordinary times," Talbott says.

As unemployment rises and more consumers struggle to pay bills, banks are faltering under ballooning losses on consumer loans such as mortgages and credit cards. In 2008, 25 financial institutions failed, compared with three in 2007.

The industry's troubles aren't expected to end soon. That's why more marriages between private investment firms and banks are likely.

Traditional suitors for troubled banks -- well-capitalized financial institutions -- are hard to find in this economic environment, says John Brunjes, a partner in the private investment funds group of Bracewell & Giuliani law firm in Hartford, Conn. Regulators have an incentive to seek non-traditional sources of funding.

The regulatory challenge, says Brunjes, is to balance "the need to attract large amounts of new private capital for faltering institutions, while at the same time imposing reasonable mechanisms concerning (banks') ownership."

In recent months, U.S. regulators have taken steps to encourage such investment. The Federal Reserve eased certain rules that made it difficult for private investors to take large stakes in banks. And the Federal Deposit Insurance Corp. expanded the pool of qualified bidders for troubled banks to include institutions that do not currently have a bank charter. (Investors must have conditional approval from the FDIC for a charter.)

Regulators seeking buyers for failed institutions also may be more willing to assume certain mortgage losses, making the banking sector more appealing. In the IndyMac deal, the buyers agreed to assume the first 20% of losses on certain mortgage loans. But the FDIC plans to take 80% of losses on the next 10% of bad loans, and 95% of loan losses thereafter.

**The Power Issue
On Wall Street
January 1, 2009**

This year's Power Issue is, of course, defined by the meltdown. The powerful players that we highlight in the next four pages are the people at the center of all the turmoil. They will have a direct impact on how this industry looks in the future. And some of them will define their legacies by how well they seize the day now.

Even if the industry has stepped back from the precipice and avoided a full implosion, it likely will still endure a slow, hard grind for most of this year. To be

sure, it remains to be seen which of the big companies will survive the year with their brands intact-if they survive at all. All the while, money will be made and lost, which is putting clients on edge and advisors on notice.

Some of our power brokers here aren't even in the industry. Sources who weighed in with ideas widely agreed that the real power affecting Wall Street won't be coming from Manhattan's skyscrapers, but rather from Washington.

In his role as President-elect Obama's Treasury Secretary-and heir to the financial mess-will Timothy Geithner be able to hold everything together? Will Rep. Barney Frank (D-Mass.) make major legislative change? We profile both men here.

But we certainly didn't ignore New York. Will John Mack keep Morgan Stanley on the straight and narrow path? How well will Wachovia be integrated into Wells Fargo? And how will Jamie Dimon manage his new, bigger empire? These are just some of the profiles you'll see here.

To build our list, we gathered names and talked to analysts and experts. In the end, it was a subjective call as to who made the cut and who didn't.

Let us know how your list would have been different.

Marten Hoekstra

Interim CEO, Global Wealth Management, UBS

It was quite a year for Marten Hoekstra. Following a deluge of negative headlines involving billion-dollar writedowns, the auction-rate securities blowup and allegations that UBS illegally helped clients avoid taxes, he ended 2008 as head of UBS' global wealth management business, which oversees CHF 2.9 trillion(US\$2.4 trillion) of client assets. Hoekstra was given the interim promotion after former chief Raoul Weil's indictment in connection with the U.S. Department of Justice's investigation into the firm's cross-border private banking operations.

Hoekstra, who now commutes each week between his New Jersey home and UBS corporate headquarters in Switzerland, acknowledges the firm's "heavy reputational damage" impeded recruiting and increased advisor attrition during the second and third quarters of 2008. But, he says, the surprising part was how quickly the trend turned around. By the fourth quarter, UBS was enjoying its best recruiting numbers ever. Granted, much of that turnaround can be attributed to the massive problems at some of the firm's competitors. But UBS also pulled off an impressive coup-capturing the cream of Lehman Brothers' advisory force by hiring

26 of its highest producers with combined assets of nearly \$11 billion.

While his outlook for 2009 is pessimistic in terms of revenues, Hoekstra sees opportunities for his team to capture assets in the down market as more clients seek to change advisors. "We need to make sure we don't switch to maintenance mode," he says. "We played defense with our clients for months. We've only recently been able to start with offense and rebuild."

To that end, Hoekstra believes both the firm and individual advisors need to own up to their mistakes. He says clients want to hear firms take responsibility for writedowns and the auction-rate securities issue. At the same time, advisors need to have "no denial" conversations and apologize to their clients if they didn't fully explain the portfolio risks.- -Helen Kearney

John Mack

CEO, Morgan Stanley

John Mack casts a long shadow over the brokerage and advisory world. Shortly after arriving at Morgan Stanley in 2005, he lured James Gorman from Merrill Lynch to turn around Morgan's dejected advisor force, a feat Gorman achieved efficiently during his two years on the job. And during last year's meltdown, Morgan was one of the two companies (along with Goldman Sachs) that soldiered through with the fewest chinks put in their armor. Not that the armor came away unscathed: Morgan seemed on its last legs in November when its share price bottomed at \$9.20. But what's one harrowing weekend time waiting for a cash infusion compared to a shotgun marriage with Treasury holding the shotgun and stockholders holding the bag?

Will it be enough to keep Morgan afloat? Many say yes. But more noteworthy is the fact that Mack likely will stay dry. Having led a famous turnaround of Credit Suisse First Boston (CSFB) as co-CEO, Morgan's current chairman and CEO long ago proved himself both a player and a survivor.

His style is not what many would call easy-going. At CSFB, Mack once threatened to tear up investment banker Frank Quattrone's contract if he wouldn't renegotiate, and got bankers to return hundreds of millions of dollars in compensation. More recently, in his September memo to the SEC, Mack asked to rein in the short sellers that he blamed for the freefall of Morgan's stock. That helped to push the regulators to issue the temporary ban on shorting financial services stocks. The result? Mack's move won Morgan room to breathe. But the firm may have lost billions in client assets from what managers perceived as Mack's influence on the ban. Still, Mack shows no sign of a furrowed brow.

Maybe he knows that, should Morgan flame, he will rise again. - -Lauren Barack

Timothy Geithner

Incoming U.S. Treasury Secretary

While this month brings the historic inauguration of President-elect Barack Obama, Wall Street is likely to pay closer attention to the new Treasury Secretary, Timothy Geithner. The day his appointment was announced, the Dow rose 4.9%. Geithner, 47, has played a key role in the financial industry bailout as president of the Federal Reserve Bank of New York, a post he held for five years. But his role is about to get much bigger. His challenge now-and it's a Herculean effort to be sure-is nothing less than continuing the rescue effort (in a newly proclaimed recession, thank you very much) while attempting to reshape the entire system.

Geithner was instrumental in last year's string of bailouts, and credited, in particular, with putting together the original rescue plan for American International Group. And while he has critics-primarily for his part in the decision to let Lehman Brothers fail-President-elect Obama has emphasized Geithner's ability to bring continuity to the rescue effort, citing an established relationship with Fed Chairman Ben Bernanke.

Geithner certainly knows the hallways of Washington. He spent 15 years at the Treasury Department including a two-year stint as Under Secretary of the Treasury for International Affairs in the Clinton administration.

Fred Joseph, president of the North American Securities Administrators Association, said, in a statement, that he hopes Geithner will create a "strong, comprehensive, collaborative and efficient" regulatory structure, with stronger enforcement and private remedies, as well as an emphasis on rules rather than the principles-based regulation that was proposed prior to the current crisis. - -Helen Kearney

Ken Lewis

President & CEO, Bank of America

In order for his \$50 billion purchase of Merrill Lynch & Co. to be deemed a success, Bank of America Chief Executive Officer Ken Lewis needs to make Merrill's "thundering herd" of advisors feel loved. When he and Merrill chief John Thain announced the deal, Lewis described the wealth management business as the firm's "crown jewel." But it was his subsequent interview on 60 Minutes, in which he said that financial services workers were overpaid, that caught the

attention of the herd. For advisors already wary of working for a bank, it did not bode well.

Still, by the Nov. 14 deadline, 93% of Merrill's top-producing advisors, of the 6,600 who were eligible, had signed the retention agreement from Bank of America. The deal was limited to advisors who brought in \$500,000 or more annually. "Bank of America gave the right people enough to stay," says industry recruiter Steve Rosen. "A lot of brokers are scared to move in this environment."

It's unclear whether Lewis will leave Merrill's wealth management business intact. Most advisors seem to be hoping for a hands-off approach and so far they've received assurances that nothing will change. Matt Bienfang, senior research director at TowerGroup, is confident Lewis will leave Merrill's brokerage unit alone. "The integration is going very fast and very hard. Most of the Bank of America folks will get pushed out of the way," he says. - -Helen Kearney

James Dimon

CEO, JPMorgan Chase

Jamie Dimon has long been one of the most-watched bankers in the U.S. With a career of heroic rises and falls, he has been called Shakespearean by no less an authority than New York City Mayor Michael Bloomberg.

Indeed, the feds turned to him when they needed a leading man to resolve the drama of the Wall Street meltdown. Last spring, the government tapped Dimon to clean up some of the mess by having JPMorgan buy the failing Bear Stearns and, later, Washington Mutual.

JPMorgan's strength stems from the fact that the firm had less exposure to the subprime mortgage market than most rivals. However, some observers suggest that the hard part is still to come. Brad Hintz, securities industry analyst at Bernstein Research, says, "Jamie's been very good-and he's also been very lucky." Hintz notes that Dimon had the savvy to tighten loose risk controls in JPMorgan's trading operation, but that he only dodged much of the subprime damage because he hadn't gotten around to pulling together the firm's warring mortgage teams.

"Was that a great skill, that he didn't address it until too late? Or was it luck?" Hintz asks. "We'll know for sure...as the economy begins to weaken. That's when retail businesses start to weaken. He missed the worst of the capital markets losses. Let's see how the portfolio holds up on retail side." - e_SRit-Elizabeth Wine

Tom James

CEO, Raymond James Financial

Consolidation and chaos: These two elements have helped Tom James boost the ranks-and assets-at Raymond James Financial. While the proud-of-their-heritage regionals were being swallowed by the big wirehouses earlier this decade, Raymond James positioned itself as the small-firm alternative. And with the current market crisis punishing share prices of big players, Raymond James has again emerged as the go-to option for many high-producers. The firm recruited more than 580 advisors last year, a nearly 42% increase from 2007. James, who, in 1966, joined the firm started by his father, credits a conservative philosophy and a focus on the private-client segment for insulating the company from the headline risk that engulfed larger competitors. "I can't remember a time I've received emails from advisors thanking me for being conservative, which is the case today," he says.

Still, the road ahead is rocky. The firm's stock price has seen its share of problems, plummeting below book value to \$13.02 in November. James says the firm has been unfairly penalized along with others, but acknowledges the outlook for 2009 is tough. Raymond James Bank is expected to write off more bad debts. James says he has applied for government assistance, which could potentially inject up to \$350 million into the firm, but insists it's more of an "insurance policy" against worsening markets than a current need for funding. Still, James sees an opportunity for his advisors to learn an important lesson in the turmoil: "Even when their clients are comfortable [again] with higher allocations to riskier investments, it is their job to supply discipline and remind [the clients] of the downside alternatives." -Helen Kearney

Mike Corbat

CEO, Global Wealth Management, Citigroup

Mike Corbat has his work cut out for him. As if it weren't bad enough to become head of global wealth management at Citigroup in the middle of an economic crisis that saw third-quarter pretax profit for the division fall by 30% year over year, he has to do so as the replacement for no less a luminary than Sallie Krawcheck. Worse, the first half of 2008 brought a net outflow of \$12 billion of client assets (before recovering slightly to attract \$3 billion in assets in the third quarter).

But overshadowing all of this is the trouble at the unit's parent. In November, Citigroup was staggering under the weight of bad assets until the government

agreed to guarantee \$306 billion of those risky assets, as well as inject \$20 billion in capital. Meanwhile, advisors saw the value of their deferred compensation fall through the floor as Citi's share price plunged to just \$3.77. "Smith Barney's biggest problem is that they are owned by Citi," says Matt Bienfang, senior research analyst at TowerGroup.

Corbat, an investment banker who joined Citi legacy firm Salomon Brothers, may struggle to convince brokers that he understands their business. He will report to John Havens, who heads the institutional client services group. The new reporting structure suggests that Citi is stepping back from its policy of separating the retail and investment units, which was put in place in 2002 after the research scandals. Not everyone sees the move as a positive for Smith Barney. "Cross-selling products and risking client relationships are some big hurdles," says Bienfang, adding that a Smith Barney client isn't really a Citi client. - -Helen Kearney

Danny Ludeman

President & CEO, Wachovia Securities

What bodes well for any advisor under Danny Ludeman's watch is his ability to focus on the important issues. "No matter whose logo or whose name is on the door, we all know it's all about doing the right thing for our clients," Ludeman told a group of branch associates recently. "We get it."

His words are especially apt these days for the 19,000 registered representatives in more than 4,000 locations working for St. Louis-based Wachovia Securities. And those sentiments get to the heart of the matter even more acutely for the A.G. Edwards brokers who joined Wachovia just a year ago and now face yet another takeover this year by Wells Fargo. While these mergers and acquisitions grab headlines, the deals' demands take time to reach fruition, say analysts who follow the industry. As an example, next month will finally mark the completion of Wachovia's integration of A.G. Edwards. According to Wachovia, the blended company will include both A.G. Edwards' revered rookie training and Wachovia's Envision program.

At press time, Wells Fargo was forming teams to tackle how it would dovetail its new Wachovia Securities division with its own operations. Decisions-including the combined company's name-will be made as the year progresses. Ludeman, for his part, brings it all back to the FA's key focus and how he "gets it." Since landing his first job in the industry in 1979 at Wheat First Securities, a small regional firm-and Wachovia predecessor-he's climbed the ranks ever since, without losing touch with the lower rungs. "We haven't forgotten that our success is driven by the special relationship FAs have with their clients," he says. - -Michelle Lodge

Meredith Whitney

Managing Director & Senior Analyst, Oppenheimer & Co.

Meredith Whitney rose from relative obscurity to make a daring call in October 2007: that Citigroup would cut its dividend to plug leaks in a weak balance sheet. She was proven right-the shares dropped sharply and CEO Charles Prince resigned within days. Ever since, she's been a full-fledged, high-flying bear who can move markets.

Her willingness to say what she thinks has garnered her an almost cult-like following among investors fed up with the near-nonexistence of sell ratings from other analysts. She had, for example, been predicting for months that the economy was headed for recession. And her most recent headline-grabber suggested that large banks will post \$44 billion in writedowns and credit-loss provisions, which will cause them to use recent government injections to boost reserves.

Even as Whitney enjoys her new celebrity, some observers wonder if she's in danger of sticking too long to her bearish guns when the market may be at the cusp of an upturn. Jeffrey Saut, chief investment strategist at Raymond James, says that Whitney's seemed brilliant recently because she's been right. That could change. "She needs to guard against overstaying the party," Saut says. "I've seen people blast into the public headlines and be superstars, only to fall to earth." - Elizabeth Wine

Barney Frank

U.S. House of Representatives

When Rep. Barney Frank (D-Mass.) unleashed his verbal smackdown against U.S. Treasury Secretary Henry Paulson in November, admonishing him for not coming to the aid of hobbled homeowners swiftly enough, industry onlookers wondered if the Chairman of the House Financial Services Committee could retain his mighty roar for regulation through the new year. Consensus? Absolutely.

In fact, with the changing of the guard in Washington, Frank at long last has an executive branch that will be more agreeable with his call for more oversight of the financial world. Frank has already held a number of hearings to grasp the specifics on the risks that brought about this current meltdown.

And he's never shied from voicing his opinion-not to mention anger-over recent actions in the financial community, including bank bailouts used for acquisitions,

or an apparent lack of oversight in the derivatives market. **"His role in oversight will multiply tenfold," says Scott Talbott, senior vice president of government affairs for the Financial Services Roundtable. "[Frank] will change the system to prevent this crisis from happening again."** - -Lauren Barack

Private equity group buying IndyMac assets
By Karey Wutkowski and Megan Davies
Reuters
January 2, 2009

WASHINGTON/NEW YORK (Reuters) - The assets of failed U.S. mortgage lender IndyMac are being bought by a group of private equity and hedge fund firms, including Dune Capital Management and J.C. Flowers & Co, which are putting up \$1.3 billion in cash.

The Federal Deposit Insurance Corp, which has run IndyMac since its failure on July 11, valued the sale to the IMB HoldCo consortium at \$13.9 billion.

Neither the investors nor the agency would provide immediate details on financing the rest of the deal, which the FDIC expects to close in late January or early February.

The investor group is led by Steve Mnuchin, the chairman of Dune Capital and a former Goldman Sachs executive; buyout artist Christopher Flowers, and hedge fund operator John Paulson, who gained billions of dollars betting that U.S. housing prices would slide and take mortgage-backed securities down with them.

Affiliates of billionaire investor George Soros and Michael Dell, the chief executive of computer maker Dell Inc, are also involved with the consortium buying IndyMac.

"We have assembled a group of experienced private investors in financial services to acquire the former IndyMac and operate it under new management with extensive banking experience," Mnuchin said in a statement on Friday.

The purchase will include IndyMac's 33 branches, mostly in the Los Angeles area, with about \$6.5 billion in deposits, as well as loan and securities portfolios of about \$23 billion. IMB HoldCo is also buying a mortgage servicing portfolio with unpaid principal balances of more than \$175 billion.

Terry Laughlin, who previously headed Merrill Lynch Bank & Trust, will serve as chief executive of IndyMac.

"The current economic climate is challenging for selling assets, but this agreement achieves the goals that were set out by the chairman and board when the FDIC was named conservator of IndyMac in July," FDIC Deputy Director James Wigand said in a statement.

IndyMac had had \$32 billion in assets when it was seized in July. At the time it was the third-largest U.S. bank failure until Washington Mutual's closure in September set a new record, with about \$307 billion of assets. In all, 25 U.S. banks failed in 2008.

IndyMac was the second-ranked publicly traded independent mortgage lender after Countrywide Financial Corp, which was acquired last year by Bank of America Corp.

Founded in 1985 by Angelo Mozilo and David Loeb, who also founded Countrywide, IndyMac once specialized in "Alt-A" home loans, which often didn't require borrowers to fully document income. It collapsed after loan defaults mounted, and tight capital markets caused losses on mortgages it could not sell.

SHARING THE LOSS

As part of the deal, the FDIC entered into a loss-sharing agreement with IMB HoldCo. IndyMac will assume the first 20 percent of losses on a portfolio of "qualifying loans," after which the FDIC will assume 80 percent on the next 10 percent of losses, and 95 percent on losses thereafter.

The resolution of IndyMac is expected to cost the FDIC's insurance fund between \$8.5 billion and \$9.4 billion. The industry-funded reserve to back deposits fell 24 percent in the third quarter of 2008 to \$34.6 billion, the latest fund total available.

The Office of Thrift Supervision said on Friday that it has given IMB HoldCo preliminary clearance to operate IndyMac as a federal savings association under OTS supervision.

After its failure, FDIC Chairman Sheila Bair used IndyMac as a test bed to demonstrate that lenders could modify distressed home loans in a way that benefits the financial institution, investors and homeowners. The new IndyMac will continue that modification program, the FDIC said.

Bair has urged the U.S. Treasury to use about \$24 billion in federal funds for incentives to get lenders to adopt similar loan modification plans nationally, but has been met with resistance from Bush administration officials.

The FDIC said the loan modification plan at IndyMac has provided total estimated savings of about \$423 million.

PRIVATE EQUITY DEAL

The FDIC said it was not the first time private equity firms have participated in acquiring failed banks. In the early 1990s, the FDIC tapped private equity sources when it sold New Bank of New England and CrossLand Federal Savings Bank.

"Allowing hedge funds to own a bank is a sign of the tough economic times and the need for creativity in turning the economy around," said Scott Talbott, chief of government affairs for the Financial Services Roundtable, an industry group. "Federal banking regulators will continue to consider hedge funds as possible buyers of other failing financial institutions."

The \$13.9 billion deal is also an indication that the private equity industry is finding ways to invest capital despite the lack of leverage. The industry has been hammered by the [credit crisis](#) which hit buyout firms' ability to buy companies through the traditional leveraged buyout structure.

Relaxation of some rules by U.S. regulators has made it easier for private equity firms to invest in banks, with Flowers being cleared in August by the Office of the Comptroller of the Currency to buy a small bank in Missouri.

Safety Handout: Identity Thieves Combine Offline And Online Options **SafetyHandout.com** **January 2, 2009**

Two out of five identity theft victims surveyed by the Identity Theft Assistance Center (ITAC, a nonprofit organization dedicated to fighting identity theft through victim assistance, research and law enforcement partnerships) know how their personal data was stolen. This knowledge provides valuable insight about how identity theft occurs.

When ITAC surveyed 275 identity theft victims who used the ITAC's free service over a one-month period, 160 consumers (58%) did not know the source of their **identity theft**. Another 115 consumers (42%) did know how their information was compromised. These 115 consumers attributed their identity theft to the following sources:

- * Friends, relatives, in-home employees - 26 cases, or 22.61%
- * Computer hacker/virus/phishing - 25 cases, or 21.74%
- * Mail (stolen or fraudulent address change) - 24 cases, or 20.87%
- * Lost/stolen wallet, checkbook or credit card - 15 cases, or 13.04%
- * Corrupt business or employee - 12 cases, or 10.43%
- * Data breach - 8 cases, or 6.96%
- * House burglarized - 4 cases, or 3.48%

* Instant credit - 1 case, or 0.87%

Getting accurate information about the sources of identity theft is difficult because identity theft - the opening of a fraudulent new account or account takeover - is often confused with other types of fraud, like the unauthorized use of a credit card. Nevertheless, it is up to each of us to be on guard against the possibility that our documents, or worst yet, our computers, could be compromised. Sometimes it may seem like a losing battle, but there are some steps we can take to prevent becoming the next victim. Here are some precautions:

* Do not keep your Social Security card in your wallet.

* If your Social Security number is on your driver's license, remove it. (In some states it is now illegal for a driver's license to be issued with a Social Security number.)

* When shredding important papers, make sure you use a cross-cut. "If it is shredded in strips and not cross-cut, I can put it down right in front of me and put it back together and there you have it," says "John", who uses his skills as a computer defense specialist to protect you, and is skilled in the ways of hackers and thieves and can ruin your credit and your life.

* "Don't use wireless for anything that you would not want put in a public newspaper. Though it's a nice convenience, your information is basically floating in mid-air. I could be two blocks away with a high-powered antenna picking up his information."

* The key is defense in depth or layers: Anti-virus, computer patches, and firewalls, and most importantly, updating them once a week. There are types of protection for wireless but they can be hacked in as little as twenty minutes. Because cybercriminals are becoming smarter and more sophisticated in their operations, they are real threats to your personal security and privacy. Your money, your computer, your family, and your business are all at risk.

To protect yourself, you need an Internet security team of experts making sure that you, your family, and your business computer are always safe and secure. The best protection you can have in today's rapidly changing world of cyber-attacks is to have expert support for all your Internet security needs that will provide technical support without any hassles and without charging you extra fees. It will become even more critical than it is today as time goes on. You need to find your own personal team of experts to rely on. If you ever have a security problem, you will want to have a trusted expert you can call for professional help, without any hassles and extra costs!

These cybercriminals leave you with three choices :

1. Do nothing and hope their attacks, risks, and threats don't occur on your computer.
2. Do research and get training to protect yourself, your family, and your business.
3. Get professional help to lockdown your system from all their attacks, risks, and threats.

Remember: When you say "No!" to hackers and spyware, everyone wins! When you don't, we all lose!

Banks Hoarding TARP Funds?

CNBC

January 5, 2009

VIDEO: <http://www.cnbc.com/id/15840232?video=985373987>

U.S. foreclosures keep coming - and for many, it's the second time around

Mary Delach Leonard

St. Louis Beacon

December 23, 2008

Posted 1:40 p.m. Tues., Dec. 23 - As 2008 ends, St. Louis housing counselor Eric Madkins, who counsels troubled borrowers facing foreclosure, says his phone is still ringing, and he's seeing firsthand evidence of a troubling trend: homeowners in trouble for a second time.

"We're seeing now people who may already be in a forbearance plan, but we're finding that we have to go back in and renegotiate with the lenders. Their financial circumstances may have changed again," said Madkins, director of housing and foreclosure intervention for the Urban League of Metropolitan St. Louis.

In many cases, these homeowners didn't have the assistance of a housing counselor and agreed to terms they cannot sustain, Madkins said.

On Monday, even as **Hope Now** -- a private-sector alliance of mortgage lenders, servicers and counselors -- was announcing in a media conference call that the industry had prevented 2.2 million foreclosures in 2008, the federal Office of the Comptroller of the Currency released its own bucket of ice-water statistics. Among them: 37 percent of loans modified in the first quarter of 2008 were 30 or more days delinquent after three months, and 55 percent were 30 days or more delinquent after six months.

"This trend of increasing delinquencies underscores the need to understand why these modifications have not been sustainable," noted comptroller John C. Dugan in the report.

Some of the re-defaults are simply the chickens coming home to roost, say industry critics who have been pushing lenders to negotiate real modifications that make long-term differences to homeowners, instead of demanding workout

repayment plans that simply rearrange debt with terms that homeowners can't sustain.

The Urban League is one of the local HUD-approved nonprofit agencies that provide free counseling to homeowners in the St. Louis region. While the agency's six counselors focus on St. Louis city and county, they also assist clients in the metro-east and have helped homeowners in St. Charles and Jefferson counties.

Madkins estimates that 35 to 40 percent of his clients have already worked out a plan with lenders that is not working. Sometimes, it's a case of homeowners who lacked the savvy to negotiate good deals in a complex financial maze. And some homeowners, he says, are so desperate to keep their homes they tell lenders what they think they want to hear.

Madkins says housing counselors are trained to ferret out accurate and realistic numbers.

"If homeowners are working with us, for example and they say they spend \$50 a month on utilities, I know that can't be right. We get realistic numbers. The numbers and financials have to be realistic. We try to drive that home," Madkins said. "If we see a budget - and a huge deficit - we see that this is why this person is struggling. Payments need to be adjusted. We make their case on the actual information we're given."

Good news, bad news

Foreclosure numbers released by the federal comptroller confirm what private fact-finders, such as RealtyTrac, have already been reporting: While delinquencies, foreclosures in process and other actions leading to home loss continue to rise, newly initiated foreclosures dropped by 2.6 percent between the second and third quarter of 2008. But delinquencies are now evident across all loan categories -- prime, subprime and alt-A, a category that encompasses a variety of "creative" adjustable rate mortgages.

The good news: Nine out of 10 U.S. mortgages remain current, according to the Office of the Comptroller of the Currency.

The bad news: One in 10 is in trouble.

Madkins isn't surprised by any of the end-of-year foreclosure statistics being released by national agencies.

The Urban League, which accepts referrals from the national hotline, can often provide troubled homeowners with local resources not available nationally, Madkins said. In limited cases, that might mean short-term monetary assistance, but it can also include help with home sales, employment assistance, or relocation, when a home can not be saved.

Increased media coverage of foreclosure has prodded some reluctant homeowners to step forward and ask for assistance, he said.

"They seem more confident now than in the past. Now, they see that it's not just them, it's other people -- and it's a nationwide problem," Madkins said. "Don't get me wrong. It's still hard to come forward, but now they're starting to see they aren't alone."

Modifications and re-defaults

The **Hope Now alliance** says the mortgage industry has been responding to calls for more loan modifications, citing a 29 percent increase, during the third quarter. The group's survey of re-defaults -- about 30 percent -- is lower than the federal number.

Steve Bartlett, president of Financial Services Roundtable, an alliance member, says the re-defaults are the product of a worsening economy, which, he says, is even forcing up the rate of default among prime loans, considered the safest segment of borrowers.

"Every single mortgage we re-modify and every single payment plan is designed to be permanent for the circumstances of that borrower at that time, based on their income," **Bartlett** said. "What we have discovered -- and this is more true now -- is the borrowers' circumstances change after they modify the mortgage, which is a way of saying, they lose additional income or lose their jobs. Then we have to go back and modify again."

Hope Now members in June agreed to a set of guidelines to streamline foreclosure prevention and also worked with Fannie Mae, Freddie Mac and the Federal Housing Agency to create the Streamlined Modification Program that took effect Dec. 15, said **Faith Schwartz**, executive director of **Hope Now**.

Madkins says the new guidelines are helpful to borrowers whose mortgages are held by a single lender but still don't address the loans that have been sold multiple times and divided into complex pools of mortgage securities. Those negotiations can take several months, which is crucial in a non-judicial state, such as Missouri, where the foreclosure process can take as little as 60 days.

"When there are multiple investors, that's when the turnaround times get longer," he said. "It really slows you down. The best reassurance we can give the borrower is when they suspend collection activity. As long as we know the sale date has been postponed, and they're going to review."

John Courson, chief operating officer of the Mortgage Bankers Association, an alliance member, acknowledged the complexity and limitations of modifying loans held in what he termed "private label securities."

"There is no question that private label securities are covered by contract. If you can structure something that is a deferral as opposed to an absolute, outright loss of principal, you have a greater chance of meeting the structure of the agreement," **Courson** said. "I think as we get more of a standardized modification program, generally accepted throughout the country, that we will see more servicers able to deal with loans inside those pools."

Calls for a moratorium

With the foreclosure crisis projected to last into 2010, Madkins says a national moratorium on foreclosures should be considered. Such action would give homeowners time to renegotiate loans, particularly when the mortgages are caught up in the complex web of securities pooling. Some states have taken the initiative and instituted their own moratoriums.

Although Fannie Mae and Freddie Mac made headlines when they announced a holiday moratorium on foreclosures, the majority of Madkins' clients weren't covered because the action didn't include private lenders.

"It should be across the board," Madkins said. "But it's going to take a change in public policy to slow things down."

Some critics have called for even more drastic efforts, including a ban on foreclosures similar to the action taken by the federal government during the Great Depression.

Bartlett dismissed that idea as no solution, adding that modifications won't work in every case.

"A mortgage modification for someone with income solves the problem. But someone who doesn't have any income, unless they have some other means of paying their mortgage, they can't keep their home," **Barlett** said. "This is a mortgage, not a gift. That is as it should be."

Courson noted that temporary moratoriums can give housing counselors the opportunity to work out solutions, but he added that growing unemployment is taking its toll.

"There are some situations that just can not be resolved, and we have to come to that reality and deal with that through the real estate and solving the issue for these borrowers," he said. "An outright ban on foreclosures is, frankly, not a permanent solution to what we're seeing."

Madkins estimates that his agency keeps 25 to 30 percent of clients in their homes.

"Income is the hurdle," he said.

by the numbers

2.2 million - number of foreclosure preventions for 2008 claimed by members of Hope Now, a private-sector alliance of mortgage lenders, servicers and housing counselors

1 million - estimated number of calls to the national Hope Hotline, operated by Hope Now, in 2008

7,000 - average calls a day to the hotline

950,000 - number of loan modifications completed in 2008, as projected by Hope Now members

133,000 - loan modifications completed in the third quarter of 2008, as reported by the Office of the Comptroller of the Currency

55 percent - number of loans that were modified in the first quarter of 2008 that were 30 or more days delinquent after six months, according to the federal Office of the Comptroller

Sources: Hope Now, Office of the Comptroller of the Currency and Office of Thrift Supervision [Link](#)

FREDDIE MAC; Fast Track Workouts for Delinquent Borrowers with Freddie Mac-Owned Mortgages Underway
Real Estate Business Journal
January 3, 2009

Seriously delinquent borrowers with mortgages owned by Freddie Mac (NYSE:FRE) or Fannie Mae can now take advantage of a new Streamlined Modification Program designed to make mortgage payments more affordable so more families can avoid foreclosure and stay in their homes. The Streamlined Mod Program officially went into effect on December 15, three days after Freddie Mac sent detailed implementation instructions to its servicers.

Announced on November 11, 2008 with the Federal Housing Finance Agency (FHFA), Fannie Mae and the **HOPE Now** Alliance, the Streamlined Modification Program replaces several time-consuming steps in a traditional loan modification with a faster uniform process that uses standard eligibility requirements and documents.

"This initiative builds on Freddie Mac's current loss mitigation efforts, which are on track to provide three out of five of our seriously delinquent borrowers with a workout this year," said David M. Moffett, Freddie Mac's Chief Executive Officer. "Our alliance with FHFA, Fannie Mae, and the **HOPE Now** Alliance will help our industry bring relief to thousands of distressed homeowners."

Under the Streamlined Modification Program, mortgage and escrow payments can be cut to 38 percent or less of an eligible borrower's gross monthly income by one or more of the following steps as necessary: reducing mortgage rates,

extending the mortgage term up to 40 years, or forbearing part of the principal. To be eligible, borrowers must own and occupy the property as a primary residence, have missed at least three mortgage payments and not filed for bankruptcy.

Borrowers should contact their servicers if they think they may qualify. At the same time, servicers will be identifying eligible borrowers and reaching out to them through the mail.

If an affordable payment cannot be achieved through the Streamlined Modification Program, servicers will evaluate borrowers through the traditional modification process. Servicers will also continue reaching out to distressed borrowers as early as possible to determine their eligibility for a workout or other foreclosure alternative.

Freddie Mac was established by Congress in 1970 to provide liquidity, stability and affordability to the nation's residential mortgage markets. Freddie Mac supports communities across the nation by providing mortgage capital to lenders. Over the years, Freddie Mac has made home possible for one in six homebuyers and more than five million renters.

Fannie Mae Streamlined Modification Program
Group Marin's Blog
January 3, 2009

WASHINGTON, DC — Fannie Mae (FNM/NYSE), today said that the Streamlined Modification Program (SMP) announced by the Federal Housing Finance Agency (FHFA) in November is now available to Fannie Mae servicers and borrowers as an option to help prevent foreclosures. Fannie Mae on December 12, 2008, provided information and guidelines to its servicers regarding the implementation of the SMP.

The SMP is designed to be a streamlined process for modifying the loans of a large number of borrowers who are delinquent in their mortgage payment and may be able to avoid a foreclosure through the program. As FHFA has indicated, SMP was intended to help set standards in the mortgage servicing industry for conducting loan modification programs on a large scale as a foreclosure prevention measure

Fannie Mae has been working with FHFA and 27 lenders and servicers in the **HOPE NOW alliance** to implement the SMP. Under the program, borrowers who meet certain eligibility criteria and demonstrate financial hardship may be eligible for a loan modification that reduces their monthly principal and interest payment. The streamlined process allows a borrower to sign a single document at the outset of the workout process that both establishes a new monthly payment during a three-month trial period, and sets forth the modification terms that will take effect

if the borrower makes the new payments during the trial period. The program is available to borrowers who have missed at least three monthly payments on their existing mortgages.

“By bringing the collective efforts of FHFA, Treasury, **HOPE NOW**, Fannie Mae, Freddie Mac and other mortgage industry participants together through the SMP to confront the foreclosure challenge, we’ll be able to help more families across America stay in their homes,” said Herb Allison, Fannie Mae president and CEO. “Along with other recently announced initiatives by Fannie Mae to reach and help financially troubled borrowers earlier, including our Early Workout program, the SMP is a critical component of our company’s foreclosure prevention efforts. These efforts are helping more than 10,000 delinquent borrowers every month get back on track.”

Modification Options

Through the SMP, servicers may change the terms of a loan to reduce a borrower’s first lien monthly mortgage payment, including taxes, insurance and homeowners association payments, to an amount equal to 38 percent of gross monthly income. The changes in terms may include one or more of the following:

Adding the accrued interest, escrow advances and costs to the principal balance of the loan, if allowed by state law;

Extending the length of the mortgage loan as appropriate;

Reducing the mortgage loan interest rate in increments of 0.125 percent to an interest rate that is not less than 3 percent. If the new rate is set below the market interest rate, after five years it will step up in annual increments to either the original loan interest rate or the market interest rate at the time of the modification, whichever is lower;

Forbearing on a portion of the principal, which will require the borrower to make a balloon payment when the loan matures, is paid off, or is refinanced.

Eligibility

Highlights of the SMP’s eligibility requirements communicated to servicers include:

Conforming conventional and jumbo conforming mortgage loans originated on or before January 1, 2008;

Borrowers who are at least three or more payments past due and are not currently in bankruptcy;

Only one-unit, owner-occupied, primary residences; and

Current mark-to-market loan-to-value ratio of 90 percent or more.

Servicers will be sending modification solicitation letters beginning this month to thousands of borrowers believed to be eligible for the program. It is critical that eligible borrowers respond to these letters and reach out to their servicers to determine if they can receive SMP assistance. Also, borrowers who don't receive a letter are encouraged to contact their servicer to see if they may be eligible for SMP help. Fannie Mae will be working with servicers to monitor and improve implementation of the program as necessary.

This article was reprinted with permission from California Association of Realtors. For more information contact the

Fannie Mae Resource Center at 800-732-6643 [Link](#)

Home Sales Moving Into Digital Age

Jim Woodard

Copley News Service

January 4, 2009

The next high-tech development related to real estate sales will be truly paperless transactions, including the acceptance of digitized and encrypted signatures.

Closing of a home sale could be accomplished in less than 15 minutes when the entire processing is handled electronically, according to a report carried on the National Association of Realtors' website.

"Paperless transactions are growing in number and popularity with brokers and consumers," said Realtor and real estate educator Saul Klein. "They are particularly popular with younger brokers and consumers, those under age 40. However, considering the problems we now face with the economy, it will probably be five to 10 years before these systems will be universally used." Klein is a past president of NAR.

The most critical element in making a paperless online transaction is cooperation and coordination of all participants. This, of course, includes the lender and title company representatives who store legally binding documents, including all title, deed and loan instruments in digital form. Also, the system must allow all parties to the transaction to review and approve the documents through a

secure password-protected website in advance of the closing, the NAR report noted.

A digital transaction management system should allow the buyer and seller to affix a signature, or its equivalent, electronically. It's important to structure the system so documents and signatures are automatically encrypted so they can't be altered.

The current sticking point in many areas is the difficulty in getting all parties in the transaction to accept digitally signed documents. And they must comply with state laws. But general acceptance of the digitized signature is growing, along with the popularity of paperless transactions.

Most of the electronic closing procedures are already in place and are being used by a growing number of brokers. Several website platforms are now available to facilitate these procedures.

One particularly popular online management platform is called Relay, owned by NAR. It makes it possible for brokers, buyers and other participants to electronically track and retain transaction documents at any time. There is a growing number of other sites that offer similar services.

The computer continues to play an increasingly important role in the real estate buying and selling process.

Q: Why does it take so long to sell a house in today's market?

A: Home sellers are having a tough time these days, particularly those who insist on asking for an unrealistically high price. They often find themselves caught in a spiral of reduced prices over a period of several months, or even years.

The key problem is that initial high price. Brokers and prospective buyers in the area quickly identify the home as overpriced. Even with a succession of reduced prices, it's difficult to remove that stigma.

The best solution to the problem is to list the property at a price that's consistent with today's lower prices in your market, making it in line with recent sales prices of comparable homes in your area. Your broker can provide this information for you.

Also, if your home does not sell within a reasonable time span, reduce the price significantly, not bit by bit. Marketing a home that's overpriced, or reduced in price only slightly, can be a very lonely and agonizing process. The overpriced stigma becomes more firmly entrenched with every passing week.

In today's market, home buyers are extremely price conscious. In fact, many brokers won't even accept listings that are obviously overpriced. It just doesn't make business sense for them, considering the costs involved in professionally marketing the property.

Q: Are both closed and pending homes sales down?

A: While home sales are generally down in many areas, pending sales (before transactions are closed) are up, according to a recent survey. It also showed a decrease in the inventory of homes on the market.

The increase in pending sales is primarily due to lower home prices and historically low mortgage interest rates. The survey, conducted by Leading Real Estate Cos. of the World, showed a particularly large number of recent sales to first-time home buyers and investors.

Nearly half of the pending sales involved foreclosed properties, the survey report noted. And an increasing number of banks holding foreclosed properties are responding favorably to short-sale offers.

Q: What's being done to curb the number of home foreclosures?

A: More concerted efforts to reduce the number of home foreclosures are in the works. The **Hope Now** Alliance, a group created at the behest of the Treasury Department, expects to modify about 2 million mortgages in 2009. The group includes JP Morgan Chase & Co, Citigroup Inc. and Bank of America Corp.

The group estimates their efforts have resulted in preventing about 2.2 million foreclosures in 2008. They are now planning a new campaign to boost participation of more firms in the program.

To find out more about Jim Woodard and read features by other Creators Syndicate writers and cartoonists, visit the Creators Syndicate website at www.creators.com.

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How To Protect Your Personal Information

By: Anne Wallace

BusinessLife.com

January 5, 2009

Identity theft can happen to anyone and that's why it's so important to take steps to protect your personal information. One of the best ways to safeguard personal information--Social Security number PIN, account numbers, and date of birth--is to treat it like cash. Protect it and be careful how you use it.

Here are some tips from the experts at ITAC, the Identity Theft Assistance Center, a nonprofit coalition of financial services companies committed to protecting customers from identity theft:

- Carry only necessary identification with you. Don't carry your Social Security card.
- Monitor your online and paper accounts. You can catch suspicious activity more quickly by monitoring your accounts online. Immediately report any unusual activity to your financial services company.
- Retrieve incoming mail as soon as possible and don't put outgoing mail in your mailbox.
- Manage how you "spend" your personal information by asking "why do you need it?" if asked for your Social Security number, driver's license number, date of birth, etc.
- Sadly, fraud and identity theft are often committed by people you know. Are you comfortable with the amount of personal information that friends, family and the people who work in and around your home or office have access to?
- Be wary of telephone requests for information. Unless you initiated the call, do not provide personal information over the telephone. The same rule applies to requests for information in e-mails and at your front door.
- When shopping online, use only secure Web sites. Look for online seals to make sure you are dealing with a reputable company. The seal verifies that a company is committed to its privacy policies.
- Beware of urgent e-mails asking you to disclose personal and financial information. These "phishing" schemes often use a bank or government logo to trick you into believing the e-mail is legitimate.
- You can check for suspicious or inaccurate account activity by reviewing your credit report. Or you can protect yourself by signing up with an identity theft prevention service such as ITAC Sentinel. You can learn more about ITAC Sentinel at www.itacsentinel.com or by calling (888) 283-1970.

Anne Wallace is president of ITAC, the Identity Theft Assistance Center (www.identitytheftassistance.org). ITAC is a nonprofit supported by financial services companies that protects consumers through partnerships with law enforcement, education and identity management services. (NAPSA)

Financial firms fight cyberthreats, brace for difficult year

By Marcia Savage

Information Security Magazine

December 23, 2008

After a year of turmoil and failure, the financial industry heads into 2009 facing the prospect of increased regulation while combating never-ending cyberthreats.

Experts expect lawmakers to create new operational risk regulations for the industry in the wake of a deepening recession triggered by the subprime mortgage debacle. A lack of fundamental business risk management led to the meltdown in the country's financial system, said Jonathan Gossels, president and CEO of security consulting firm SystemExperts Corp.

"There will be new regulations focusing on operational risk management, with compliance supported by IT infrastructure," he said. "All of this is in the context of extremely tight budgets."

While it will likely take a while for lawmakers to hammer out the new requirements, new personal data protection laws passed in 2008 will put pressure on the financial industry and other sectors. In Nevada, a law requiring encryption for transmission of personally identifiable information over public networks was enacted in October of this year. A Massachusetts law takes effect May 1 that requires businesses not only encrypt transmission of personal data, but also personal data stored on laptops and removable storage devices.

The Massachusetts law has a provision that organizations verify their service providers are compliant, which will continue to make third-party risk management a top issue for financial firms, said Mark Steinhoff, national financial services lead and principal at Deloitte & Touche LLP security and privacy services. The Red Flag regulation that took effect Jan. 1, 2008 also incorporates requirements for service providers.

Ron Woerner, a security officer at a large financial-services firm, expects other states will follow Massachusetts' lead and develop more stringent privacy and security laws, further muddying the regulatory waters.

"Financial companies will then need to spend more money ensuring compliance, taking money away from other needed security programs," he said.

Other new regulations financial institutions will face in 2009 include increased requirements for vetting commercial customers under a new federal rule that implements provisions of the Unlawful Internet Gambling

Enforcement Act of 2006, said John Carlson, senior vice president of regulatory affairs for BITS, a nonprofit financial-services industry consortium and division of The Financial Services Roundtable. Compliance will be challenging, he said, because gambling laws vary among states and countries.

In addition, the Federal Financial Institutions Examination Council was expected in December to release guidelines on managing risk associated with remote deposit capture.

As financial firms grapple with new regulatory requirements in 2009, they will face a continuing onslaught of cyberthreats. In fact, the upheaval in the market will likely fuel an increase in online attacks, some experts said.

"Cybercriminals will take advantage of the confusion related to mergers and failures," said David Pollino, an information security professional working with financial services companies.

Securing clients' systems will be a major focus for financial institutions in 2009 as they fight mounting losses due to insecurity on the customer side, Woerner said.

"While many clients' knowledge and ability with computer security continues to improve, many will continue to put pressure on financial institutions to provide the needed security for them," he said.

Paul Smocer, vice president of security at BITS, predicted application security will be a hot topic in 2009. Financial institutions have taken steps to improve secure coding practices internally, but will examine third-party software security more closely, he said.

Financial firms have implemented safeguards that make network-level attacks difficult, so attackers have shifted their focus to the application layer, he explained.

Also expect to see a lot of attention paid to authentication in 2009, Smocer said. "That's primarily due to the types of malware that we've been seeing lately -- malware that's not easily detectable on end users' PCs," he said. "I think that will cause questions to arise with regards to the authentication schemes that are in place today."

Another top issue will likely be strengthening email security to reduce phishing scams via implementation of DomainKeys and Sender Policy Framework, he said.

On the fraud front, identity theft will remain a top issue, Woerner said. The arms race will continue, with "the bad guys getting more organized and savvy on how to compromise financial systems," he added.

There's always increased concern about fraud in an economic downturn, but now there's particular concern about mortgage fraud, said Rodney Nelsestuen, a research director in TowerGroup's financial strategies and IT investments group. In fact, reported incidents of mortgage fraud were up 45% on fewer loan applications in the second quarter of 2008, compared to the second quarter of 2007, according to the Mortgage Asset Research Institute.

Even with the economic crisis, financial institutions are opening up new channels to their customers, such as mobile banking, which will bring new security risks, Nelsestuen said.

However, tight budgets will put added pressure on the professionals in charge of managing risk and information security. "Security professionals will be forced to do more with less, so focus must be given to automation and prioritization, based on reliable data," Pollino said.

Yet the economic crisis could help some companies resolve a difficult problem, Woerner said.

"The slow economy will increase the need for sound risk management practices to better prioritize security, privacy and compliance projects. Many companies have difficulty prioritizing risk decisions," he said. "The economic downturn may finally provide the impetus to fix the eternal problem of security prioritization."

With Billions at Stake, Business Lobbyists Vie for a Piece
By [ELIZABETH WILLIAMSON](#) and [BRODY MULLINS](#)
Wall Street Journal
January 6, 2009

WASHINGTON -- President-elect Barack Obama's stimulus plan aims to help Main Street, but it is already sparking boom times on K Street as lobbyists from a host of U.S. industries seek a share of the projected \$800 billion package.

Wind farms want permanent tax credits. The steel industry wants "Buy American" protection for infrastructure projects in the bill. Home builders want a national low mortgage rate, guaranteed by Uncle Sam. Universities want money for campus repairs, as well as \$700 more per student in federal grants.

The spending requests total many times the likely size of the package. Environmentalists alone put together a wish list of 80 projects that add up to \$405 billion.

With a fight likely over a pie that, however large, isn't big enough for all, industries are crafting creative pitches to show that assistance to them would provide the fastest, broadest or most comprehensive stimulus.

The U.S. Travel Association, which represents hotel, resort and theme-park operators, wants the stimulus package to include a measure they have pushed for years, establishing a government office to pitch American tourism to foreigners.

"When you're looking at stimulating the American economy, it doesn't get any better than bringing people into the country," said Geoff Freeman, senior vice president of the association. "They come, they leave their money, and they go home with a better impression of the United States."

Although the financial sector has received more than \$1 trillion in federal rescue money over the past year, its lobbyists are pushing for more.

The Financial Services Roundtable, a coalition of the 100 largest financial-services companies, sent a letter to congressional leaders Monday asking for several tax breaks, including the doubling of the mortgage-interest deduction for first-time home buyers, and allowing companies to accelerate deductions for bad debt.

The National Association of Federal Credit Unions is looking to extend its reach with an aggressive push for Congress to lift limits on credit unions' business loans in the bill. The powerful group wants the limit raised from the current 12.25% to 20% of a credit union's total assets -- or lifted entirely.

The measure, said chief lobbyist Dan Berger, is "a way to provide small businesses access to much-needed credit without costing the taxpayer a dime."

The Securities Industry and Financial Markets Association wants to exempt private-activity bonds from the alternative minimum tax, and relax rules that discourage banks from owning municipal bonds.

The U.S. Chamber of Commerce, the nation's largest business lobby, has written a letter asking for lower tax rates for companies that buy back their own debt. The National Association of Manufacturers has joined with the National Association of Home Builders in a coalition called Fix Housing First. They are pushing for an

extension of home-purchase credits and a federally supported national mortgage rate of 3%.

In a conference call with Obama officials two weeks ago, executives from [International Business Machines](#) Corp., [Cisco Systems](#) Inc. and the Information Technology Industry Council outlined a six-point plan dubbed "Investing in Digital Infrastructure to Jump-start the Economy." The companies are part of a tech-industry coalition that wants to dip into the stimulus pot to upgrade and expand telephone lines for broadband Internet service, increase tax incentives for research and development and allow companies to return overseas profits to the U.S. at reduced tax rates.

At the request of Congress and the Obama transition team, the Natural Resources Defense Council has compiled a list of more than 80 projects, including \$18 billion for a state energy-efficiency grant program and \$6 billion for water infrastructure projects.

"It's been portrayed by some as wildly outrageous...here go the environmentalists again," said Karen Wayland, legislative director for the NRDC. "What we were suggesting are authorized programs where an injection of quick cash will create jobs."

The United States Association of Importers of Textiles and Apparel -- which includes such major retailers as [Target](#) Corp., [J.C. Penney](#) Co., [Kohl's](#) Corp. and [Macy's](#) Inc. -- wants a total repeal of import tariffs on clothing. The logic for tying this long-sought change to the stimulus package: the import tax falls disproportionately on those hardest hit by the downturn.

The tax makes up about \$5 of the cost of shoes that retail for \$15 and therefore "parents are trying to keep shoes on their children's feet and this regressive tax is making that more difficult," said Matt Rubel, the chairman and CEO of [Collective Brands](#) Inc., the parent company of Payless ShoeSource and several low-cost brands. "We are working very hard to make sure [that the removal of] this tax on American working families is included with the stimulus," he said.

Obama Supports Corporate Tax Refund That Was Rejected Twice in 2008
By Richard Rubin
Congressional Quarterly
January 6, 2009

Some of the biggest winners in the economic stimulus package might be the biggest money losers in corporate America.

President-elect [Barack Obama](#) is resurrecting an idea that fell short of enactment twice in 2008: allowing companies a speedier recovery of their current losses through refunds of taxes they paid on earnings in previous years.

The extension of net operating loss carryback from two years to five, which is favored by Republicans, would provide instant refunds to some of the firms that have been hit hardest by the recession, including large portions of the financial services and real estate industries.

That's welcome news to companies that would otherwise face the prospect of gradually using those losses over the next 20 years to offset taxes on future profits.

The provision would “strengthen the balance sheet and strengthen current lending programs,” said Scott Talbott, senior vice president for government affairs at the Financial Services Roundtable. “That’s the heart of what we’re talking about here.”

But it's also far from certain that the provision would stimulate the economy as intended, said James Horney, director of federal fiscal policy at the Center on Budget and Policy Priorities, which advocates for low-income workers.

“If you just provide more money to businesses in general, that doesn't necessarily mean they're going to do any more investments or hire any more employees,” he said, adding that getting money to people who are likely to spend it is a more effective approach to spurring demand and corporate investment.

Some companies being affected by tightening credit would spend any new tax refund, Horney said, but others could just sit on it until the economy gets better.

And the fact that the likely beneficiaries of the carryback provision include companies that profited from the housing bubble earlier this decade is likely to rankle some lawmakers. Last year, when the Senate considered a similar proposal, [Judd Gregg](#), R-N.H., called it “modified socialism,” arguing that the housing industry was asking the government to insure companies against their own risks.

“It's a lot like that story of the fellow who shot both his parents and then threw himself on the court and asked for mercy because he was an orphan,” he said on the Senate floor.

[Accelerating Benefits](#)

Lawmakers have not yet released legislative text or a revenue estimate for the plan, but a similar proposal considered in 2008 by the Senate Finance Committee would have cost \$23.1 billion over the first two years and \$10.4 billion over 10 years.

Here's how loss carryback works: Assume that a company made \$1 million a year in 2004, 2005, 2006 and 2007, then lost \$2 million in 2008 and another \$2 million in 2009. Under current law, the company would have paid income taxes on its profits in those first four years. Then, because it lost money in 2008, it could get a refund for the taxes it paid on the \$2 million in profits from 2006 and 2007, its most recent profitable years.

When it rang up another \$2 million in losses in 2009, the company could not get back any money immediately, but it would be allowed to use those losses to offset \$2 million worth of profits over the next 20 years.

Under the expected Obama proposal, however, the company could look back five years and get a refund equal to the taxes it paid in 2004 and 2005 when filing its taxes for 2009.

The proposal would help many companies across the economy, except perhaps in still-profitable sectors such as pharmaceuticals and consumer products, said Robert Willens, a corporate tax expert in New York.

“All you're doing is accelerating the use of the losses,” he said. “It's not as if you're allowing people to use losses they wouldn't otherwise be able to use.”

Idea Had Been Shunned

Homebuilders and others tried in 2008 to get Congress to enact a similar extension, but they fell short, particularly in the House. In January, the Senate Finance Committee added the provision by voice vote to last year's stimulus bill, but the package died on the floor, one member shy of the 60 votes needed to add it to the narrower House stimulus plan (PL 110-185).

Then, in April, the Senate added the loss-carryback provision to a housing bill (PL 110-289). House Democrats immediately resisted the move, and Ways and Means Chairman [Charles B. Rangel](#), D-N.Y., announced that he would not include it and took a shot at the Senate bill as he introduced his own version.

“We need to provide relief to the [home] buyers and families themselves, not just the banks and builders,” he said.

But just nine months later, House Democrats may turn around and embrace the provision. That may be a signal of bipartisanship, and Republican leaders have said that they are more likely to support a stimulus bill that contains GOP ideas.

Among the array of Republican-favored tax proposals, such as a tax holiday for repatriating income earned overseas, the extension of loss carryback is the most palatable, a House Democratic aide said.

That logic, however, has just emboldened Republicans, said Steve Wamhoff, legislative director at the liberal Citizens for Tax Justice, who cited a proposal to reduce the 25 percent income tax bracket to 15 percent as a particularly bad idea because its benefits would flow to wealthier taxpayers.

“They’ve already been given goodies to buy them off,” he said, “so they’re moving on to crazier things.”

Cyber security for the banking and finance sector
Wiley Handbook of Science and Technology for Homeland Security
January 6, 2009

See link for article:

<http://www.fsround.org/hyperlink/hhs460.pdf>

Banks, Homebuilders May Convert Losses Into Cash With Tax Break
By Ryan J. Donmoyer
Bloomberg
January 6, 2009

Jan. 6 (Bloomberg) -- Investment banks, homebuilders and manufacturers who failed to win passage of a tax break in last year’s stimulus that would convert losses into cash have persuaded President-elect [Barack Obama](#) to back their cause.

A provision in a fiscal stimulus measure being crafted by Obama and congressional leaders would let businesses use operating losses in 2008 and 2009 to claim a refund of taxes paid in the previous five years, according to transition officials and congressional aides familiar with the talks.

Without the provision, companies would have to wait years to apply those losses against future profits.

“We need to speed stimulus to all sectors, especially the financial services sector, which provides the oil for the economic engine,” [Scott Talbott](#), senior vice president of government affairs at the Financial Services Roundtable, said today. The proposal “is a broad-based measure that will help restart all sectors of the economy at the same time,” he said.

Current law lets businesses use operating losses to claim refunds for the prior two years. Losses that aren't carried back can be used to reduce taxes on future profits.

Expanding the provision, known as a “net-operating loss carryback,” to five years would refund more than \$14 billion to U.S. companies this year, according to estimates by the nonpartisan Joint Committee on Taxation. It has long been a staple in fiscal stimulus bills and was last enacted temporarily in 2002.

The change would be a boon to banks, which have posted hundreds of billions in writedowns and credit losses tied to the falling value of mortgage securities since the subprime crisis began. It also would help homebuilders who enjoyed large profits until 2006 when the housing market began to implode.

‘Not Offensive’

“It’s definitely controversial but is probably a good policy,” said [Robert Willens](#), a certified public accountant who advises clients on how accounting and tax rules affect Wall Street. “In these times, it’s not offensive to extend the period to five years for recovery and rehabilitation reasons.”

The Senate last year sought to include the provision in the 2008 stimulus measure, but House opposition kept it out of the final package. It has also been opposed in the Senate by Republicans such as New Hampshire’s [Judd Gregg](#), who last April called the provision a reward to companies for being unprofitable.

Since then, a coalition of 71 business groups led by the National Association of Manufacturing redoubled efforts to include the provision in the new round of stimulus.

‘Proven Economic Stimulus’

Expanding the tax break “is a proven economic stimulus measure, one that can deliver vital help to our nation’s struggling employers,” the groups, which

included the Financial Services Roundtable, U.S. Chamber of Commerce, and the National Retail Federation, wrote in a Dec. 9 letter to congressional leaders.

“If there was ever a time” for the tax break, “it is now,” the groups said.

The groups say allowing the companies to get cash through a refund of past tax payments would let them take advantage of another business stimulus measure: temporary incentives such as accelerated depreciation to invest in new equipment.

Some tax experts, including New York University Professor [Daniel Shaviro](#) and Urban Institute scholar Eric Toder, a former Treasury Department official, have said they don't see how a five-year-loss carryback will boost the economy. “I'm skeptical,” Shaviro said in an interview last year.

US Democrats Reintroduce Legislation To Change Bankruptcy Law

By Jessica Holzer

Dow Jones

January 6, 2009

WASHINGTON -(Dow Jones)- U.S. Democratic lawmakers on Tuesday reintroduced legislation to change bankruptcy laws to allow homeowners to shrink their mortgage debts on primary residences, a measure fiercely opposed by the banking industry.

Sen. Dick Durbin, D-Ill., the second-ranking Senate Democrat, first introduced the legislation in 2007 as a way to combat the foreclosure crisis. The measure languished amid a heavy campaign from the banking lobby, which argued the change would increase mortgage rates for homeowners across the board.

The legislation has brighter prospects now that Democrats have recaptured the White House and increased their majorities in Congress. In a widely expected move, Durbin and House Judiciary Committee Chairman John Conyers, D-Mich., introduced companion bills Wednesday in hope of attaching the legislation to President-elect Barack Obama's economic-stimulus plan.

While on the campaign trail, Obama expressed support for changing the bankruptcy laws to help troubled homeowners. He has not yet indicated whether he would include such a measure in his economic-stimulus plan.

In a statement, Financial Services Roundtable President and CEO Steve Bartlett warned that the bills "will inject additional risk into home buying and the markets will respond by increasing interest rates, fees, down payments, or all three."

Leading Democrat Offers U.S. Mortgage Aid Bill

By Patrick Rucker

Reuters

January 6, 2009

WASHINGTON, Jan 6 (Reuters) - The second-ranking Democrat of the U.S. Senate on Tuesday introduced legislation that would let bankruptcy judges erase some mortgage debt in an effort to stem foreclosures.

The bill drafted by Sen. Richard Durbin would help millions of families avoid foreclosure by easing their monthly payments, the Illinois lawmaker said in a statement.

"After committing over \$1 trillion in taxpayer money to address the financial crisis, why don't we take a step that would indisputably reduce foreclosures and that would cost taxpayers nothing?" Durbin, the Senate Democratic whip, said in a statement.

A similar plan failed in the Senate last spring as President George W. Bush and many Republican lawmakers opposed it, but supporters of 'mortgage cram-down' believe that they will prevail as the housing crisis has deepened and President-elect Barack Obama prepares to take office.

OPPOSITION AHEAD

While the financial services industry is generally opposed to the reform, many consumer-rights advocates have come out in support of the plan that would give courts the same broad power to rewrite home loans as they can do for other debts.

"Reasonable and limited reforms of the bankruptcy laws would allow judges to readjust debt owed on primary residences, just as they can for vacation homes and family farms," 21 state attorneys general wrote on Tuesday in a letter to Congress.

While a national housing crisis has worsened in the last 12 months and foreclosures have climbed to record levels, the lending industry has warned that changes to bankruptcy law could stifle credit.

"The bills will increase the cost of borrowing for a home, at the exact moment we need home sales to restart," said Steve Bartlett, president of the Financial Services Roundtable.

The legislation could take many months to work its way through Congress. But the plan could also become law quickly if it is included in an economic stimulus package being drafted now by congressional leaders.

**MOVES-Kirkland & Ellis, RBC, Sterling Bancshares
Reuters
January 7, 2009**

NEW YORK, Jan 7 (Reuters) - The following financial services industry appointments were announced on Wednesday. To inform us of other job changes, please e-mail moves@thomsonreuters.com. KIRKLAND & ELLIS William Barr, former executive vice president at Verizon Communications and U.S. Attorney General in the administration of President George Herbert Walker Bush has joined the law firm in Washington. **FINANCIAL SERVICES ROUNDTABLE The Financial Services Roundtable, which represents 100 large financial services providers, named Peter Freeman vice president for insurance.**

Previously, as deputy chief of staff to Congresswoman Deborah Pryce, an Ohio Republican, he worked for the House Financial Services Committee.

RBC DIRECT INVESTING The discount brokerage unit of Royal Bank of Canada named Jason Storsley as chief executive and president, effective Feb. 1. He earlier led the Global Institutional Management team and was head of Global Equity Research for RBC Asset Management. STERLING BANCSHARES INC The bank holding company promoted Travis Jagers to the newly-created position of executive vice president and chief lending officer of Sterling Bank.

He was previously Sterling Bank's regional chief executive for the Southeast Houston region. **CLOSE BROTHERS** The independent business unit of British investment bank Close Brothers Group appointed John McGrath as managing director to expand its European financial services sector coverage team into the United Kingdom. McGrath, previously with NM Rothschild & Sons Ltd, will be based in London. **MACKENZIE FINANCIAL CORP** The investment management unit of IGM Financial Inc named Paul Musson as head of its Ivy investment team. Musson will take on the role in February replacing current head Jerry Javasky who is moving to an advisory role with the intention to retire from the investment business. **PURITAN FINANCIAL GROUP INC** The holding company named Trenton Sommerville as chief executive and chairman. He was earlier with Heartland Inc.

***Also appears in Forbes and CNBC

**Risk management: Common assessments criteria
Stephen Scharf, SVP & global CISO, Experian
January 01 2009**

Conducting security assessments of critical service providers is an essential part of an enterprise risk management program. Highlighting exposures external to your organization will assist in appropriate vendor selection, acceptable risk practices, and reduce the likelihood that your data will suffer a breach due to means outside your direct control.

I have seen assessments that do little more than check off a box for a thoughtful, but poorly executed security program. I have also seen assessments that are so detailed that in order to satisfy one area of the assessment I would be required to provide documentation that is clearly restricted for distribution and, hence, would result in failure of a different section of the assessment. Somehow, the folks conducting the reviews cannot seem to find the irony in this.

It is clear that the level of depth required for an assessment will be based on the criticality of the supplier and the sensitivity of the data in question. A review of an

outsourced back office data supplier who only has access to publicly available records would take considerably less time and resources than a review of a payroll processor. Since the value of varying the depth is apparent, I suggest we offer a consistent approach on breadth and leverage a common assessment template to facilitate these reviews.

The problem with the current process of seemingly random assessments formats is the resource requirement and increased time to respond. Having to field different questionnaires in different formats results in significant time wasted in rewriting answers. This in turn delays the response time and limits the number of concurrent reviews the average organization can maintain. By using a standard assessment format we can leverage a common structure, which will allow for faster turnaround and reduce wasted personnel power.

When I discuss this with other security practitioners, there is normally an agreement on the need for simplifying the process and understanding the value this will offer. When I ask the same group if they would participate in creating such a standard, they almost unanimously say “no,” but they would be happy if it eventually appears. In fact, there are some vendor-neutral associations that have made strides in creating a common assessment criteria. Perhaps the adoption levels will increase over time and the value will be further emphasized by everyone wanting to copy their neighbor. In the meantime, I will go back to filling out hundreds of dissimilar spreadsheets asking questions about firewalls and business continuity planning.

[sidebar]

For more information

Absent a shared assessments standardized information gathering questionnaire, the outsourcer must answer detailed questions from each financial institution for which it performs key functions.

– sharedassessments.org

Consortium guidance

BITS is a nonprofit, CEO-driven financial service industry group made up of 100 of the largest financial institutions in the U.S. It provides intellectual capital and fosters collaboration to address emerging issues.

Instilling trust

BITS is a division of The Financial Services Roundtable, a public policy group that promotes the interests of member companies in legislative,

regulatory and judicial forums to sustain consumer confidence and trust.

Help for finance sector

BITS will be holding a summit to be held March 3-5 at the Hyatt Regency Sarasota, Fla. to discuss the demands for enhanced operational efficiency, higher security and increased customer service.

Foreclosure Is Still On Despite Efforts of the Mortgage Service Providers

ForeclosureWarehouse.com

January 7, 2009

Despite strong efforts made by the [mortgage](#) service providers to assist the borrowers to keep back their [real estate](#), the rate of [foreclosure](#) did not stop increasing in the third quarter. The condition of the economy is really bad and more number of people defaulted on their loan payments. The new [foreclosures](#) boiled down from June end to September end by 2.6 percent to 281,298 due to reasons like extended loan terms, low rate of interest, and state moratoriums on foreclosures. Still the rate of foreclosures in the third quarter went up by 8 percent to 127,738. The number of foreclosures that were under way went up by 11 percent to 617,642.

This increasing rate of foreclosure has taken place as many borrowers have failed to pay back their money. This includes also those who have drawn advantages from loan modifications. Over half of the loans that were modified in the first quarter have gone into delinquency after a period of six months. This by the end of September was due by over 30 days. One out of every five loans modified, was due by over 60 days after a period of three months, and 37 percent of them were 60 days delinquent even after six months.

Steve Bartlett, one of the members of Hope Now, said “Mortgage modifications work for people with incomes; it doesn’t work for people without income,” A report that has been collected from five thrifts and nine national banks shows that there are over 60 percent mortgages outstanding in US. It also shows that the quality of credit has gone down badly in all categories right from prime to Alt-A to sub-prime in the third quarter. The share of performing and current loans has dropped down to 91.47 percent by the close of the third quarter. This at the close of the second quarter stood at 93.33 percent.

According to economist Thomas Lawler a majority of the foreclosure reduction that took place during the quarter was mainly due to the state laws especially in case of [California](#). It helped in delaying the process of foreclosure. Bartlett said

that the real estate industry needs help from the federal government. In Bartlett's own words, "If the federal government puts more money into mortgage modifications, we'll have more mortgage modifications," This plan is getting some force from the Chairman of the Federal Deposit Insurance Corp., Sheila Bair. This has however faced an opposition from the White House. [Link](#)

Guarding against a data breach

Illena Armstrong

January 1, 2009

SC Magazine

A slumping economy will have a bearing on spend for safeguarding critical data in more ways than expected, reports Illena Armstrong.

For most chief executives, anxieties about the global economic plunge have far outpaced concerns regarding the risks of data breaches. As overall confidence in the market seems to continue its wane, corporate leaders are searching for ways to keep the financial crisis from further eroding business plans and profit gains.

But, a sinking economy historically has the causal effect of escalating various types of crimes – both physical and cyber.

"Numerous studies have shown that crime and the economy are linked," says Richard Starnes (*left*), special assistant in the Commonwealth Office of Technology in Kentucky. "No one is immune to market forces, not even criminals."

And this fact has a way of deepening the already challenging problem of defending against well-established risks to confidential customer and corporate information bouncing around the internet.



"There is no doubt, based on the feedback we are hearing, that 2009 will present budget challenges. On the other hand, a focus on risk would suggest that the difficult economic times we are involved in would likely also cause us to witness an increase in cyber-related crime activity – including data theft attempts," says Paul Smocer, vice president of security for BITS, a nonprofit, CEO-driven financial service industry consortium made up of 100 of the largest financial institutions in the U.S.

Predictably, this means that IT security executives responsible for safeguarding against intensifying threats to both their customers' and their company's critical data want to continue to see their programs receive a greater portion of their stakeholders' mindshare. And certainly, at least for the last couple of years now, corporate leaders, understanding the damage to brand and profits that a lone data breach can cause, have been throwing greater and greater support behind risk management plans and the IT security departments managing them.

“Protecting our products, customers, and reputation is critical to continued business success. My company certainly recognizes that. As a result, I spend a lot less time defending why we need security,” says Patty Edfors, chief privacy and security officer for Mirixa Corporation, a company sponsored by the National Community Pharmacists Association (NCPA) that specializes in targeted patient care services delivered via the nation's largest pharmacy-based patient care network.

However, some information security professionals are not as fortunate, revealing concerns that over the next six to 12 months their hard-won executive backing will wither away alongside the economy's seeming unending meltdown.

Exactly 80.6 percent of the 217 respondents to this year's second annual Guarding Against a Data Breach survey, which was conducted by *SC Magazine* and BT with research firm Millward Brown, say the threat of a data breach is greatly influencing organizations' current security initiatives. This number mirrors closely last year's result at 81.3 percent from 368 participants.

But, despite this influence, more respondents to the survey this year anticipate a decrease in budgets for IT security projects and data loss prevention efforts over the next year. About 11 percent foresee moderate or dramatic decreases – a stark contrast to about five percent last year. Additionally, approximately 53 percent expect their budgets to remain fixed compared to 41 percent last year.

Other respondents, though, have hope that the amount of funding slated for their IT security programs actually may increase despite the bleak economic times. Though the number has shrunk when weighed against 2007 results, 37 percent believe they will see dramatic or moderate increases in budget dollars as opposed to 54 percent in last year's study. Though some might deem these information security professionals too optimistic about funding, their thinking makes sense to BITS' Smocer.

“Minimally, we expect that budgets related to cybersecurity will remain relatively flat with organizations acting to sustain the programs they have put

in place to prevent data loss and data theft,” says Smocer. “We can see, however, given the risk scenarios, the possibility that selective increases will occur in cybersecurity budgets.”

Yet, times have a way of changing quickly, so, for Edfors, it's “anyone's best guess” what the future may hold in the shadow of a degrading economy.

“It may mean that we have to have less separation of duties in our workforces and have less to spend on technology security improvements,” she explains further. “So our only real defense is to work creatively and flexibly to find compensating controls.”

Moving in the right direction

Of the 217 respondents to the *SC Magazine*/BT survey, 88 percent agree that their company is taking the right steps to prevent customer/client data from being stolen, exposed or lost, which parallels closely with the 90 percent of 368 respondents in last year's survey. But, just like last year, this may be more indicative of overly optimistic views of security, rather than confirming that companies are engaging in proper planning and management of critical information.



“If 88 percent of respondents were taking the right steps to prevent data theft, then data theft wouldn't be such a big problem. My guess is that the steps they're taking are necessary, but not sufficient, to prevent data theft,” says Bruce Schneier (*left*), chief security technology officer at BT, a provider of communications solutions and services operating in 170 countries. “The respondents may believe that their company is taking the right steps, but it doesn't mean that they are addressing the right goals.”

To Schneier, the best action to protecting critical data is “setting up a comprehensive program of assessment, enhancement and testing,” with the understanding “that such a program is not a quick fix.” More importantly, in order for it to be effective, it has to have ongoing executive buy-in, both in terms of support and budget.

“If, on the other hand, they are approaching it from a check-box mentality, driven primarily by price, then they are buying nothing but a false sense of security,” he adds.

Indeed, says Kentucky's Starnes, a follow-up exercise for those who note they are undertaking the appropriate means to protect data would be to engage their external auditors, asking them the same question. "I think those numbers would more properly reflect the reality of the situation," he adds.

Still, the fact that corporate executives and their IT security officers understand the need for protecting critical data is significant. Out of the 217 respondents, approximately 65 percent agree that their IT security departments and executive leaders will make strides to continually improve overall data security, up a small bit from 63 percent last year.

"All companies understand that bad security is bad for business, but not all companies realize that good security is good for business," says Stephen Scharf, senior VP and global CISO for Experian. "As organizations continue to understand that security is a value differentiator, which can add to a competitive advantage, I would expect the percentage measurement on this question to increase."

Accounting for risks and drivers

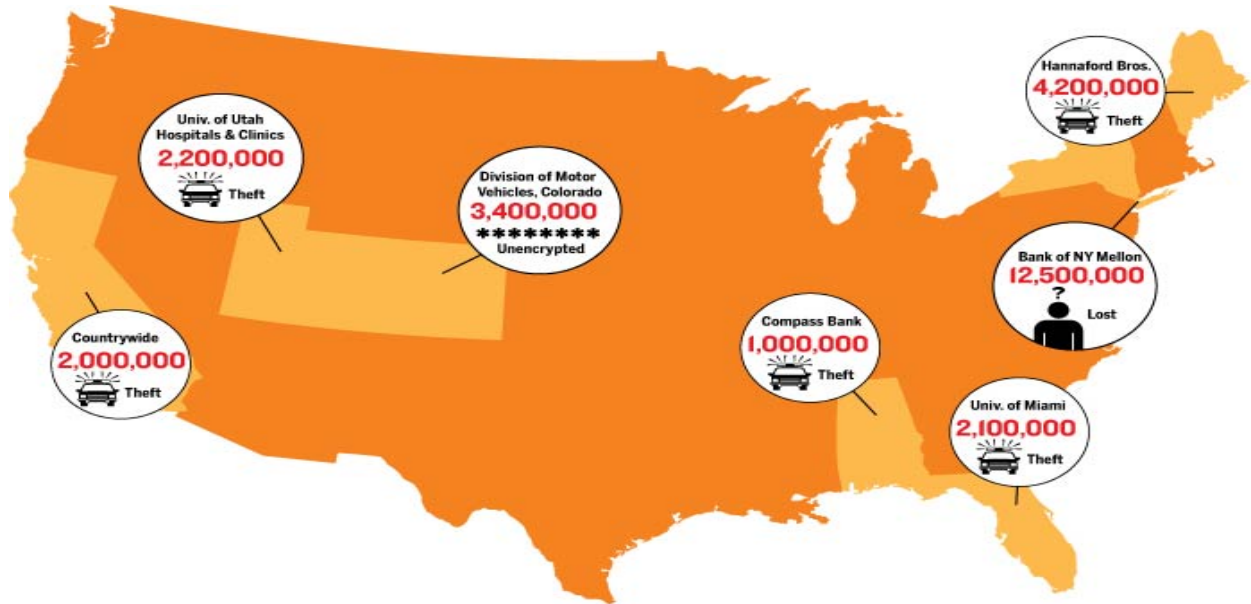
To be sure, despite expected belt-tightening, the drivers behind risk management and data protection initiatives stand strong year upon year. Possible negative impact to the company (75 percent), regulatory mandates (71 percent), possible profit loss (43 percent), customer demand (36 percent) and executive board demand (35 percent) all are factors that compel respondent to the *SC Magazine*/BT survey to better safeguard customer and other critical data from being stolen, exposed or lost.

These statistics have changed since last year's survey, which showed that regulatory mandates and possible negative impact to the company were tops at 79 percent. Executive board demand followed at 45 percent, while customer demand and possible profit loss came into the last two slots.

"It's a bit surprising that the 'regulatory mandates' category has dropped nearly 10 percent, given that there are more laws on the books and more points of enforcement each year," says Schneier. "Equally, the drop in executive board demand by 10 percent suggests that either the risk has been reduced or that pain threshold for the executive boards has. It is highly unlikely that the risk has been reduced, since the number of data breaches has only increased in the past year."

What he believes is more likely is that to some, reports of data breaches are becoming old news, too repetitive given the frequency with which they now

appear in mainstream media outlets. Additionally, because there have been no significant prosecutions for data thefts or more companies being brought before Congress to discuss why data was exposed, the risk probably is being perceived as lower.



Major 2008 data breaches showing individual records lost (Source: Privacy Rights Clearinghouse)

As for those drivers that help IT security officers to get the resources and budget they need, just like last year, regulatory mandates (62 percent) and possible negative impact to the company (59 percent) were the leaders this year. Following these were possible profit loss (at 35 percent) and executive board and customer demand (at 33 and 30 percent, respectively). But, profit loss last year was further down the list.

BITS' Smocer says the issues pushing budgets seem relatively consistent year-over-year, and while percentages may change a bit, these fundamental drivers will remain the same. Mirixia's Edfors agrees.

“Given the number of reported breaches and the activities with state security breach laws, these numbers don't surprise me,” she says. “While we all are trying

to keep up with myriad regulatory mandates, the bottom line is protecting the brand, customer and company.”

Protecting the company and its customers requires an understanding of the risks – and, make no mistake, these abound.

For many, mobile security concerns are certainly high on the list of priorities, as is application security and browser vulnerabilities, says Jerry Dixon, director of analysis, Team Cymru, and former director, NCSD, DHS.

Dixon's list ties closely to how respondents to the *SC Magazine*/BT survey are spending their money to deploy various solutions next year to safeguard customer/client data. Making the top of the list, as it did last year, is email management and content filtering (60 percent). Following up in this year's results are database security (55 percent); mobile security solutions (49 percent); email encryption solutions and secure web services for customers (45.2 percent); data loss prevention solutions/services (44 percent) and web application and secure coding (42 percent, respectively). Rounding out the list were items like two-factor authentication, laptop encryption, access controls at the perimeter, web/IM/P2P filtering appliances, and more.

“You will note a significant number of responses dealing with application-oriented security,” says Kentucky's Starnes. “This is where the threat vector has moved. Hackers are no longer primarily seeking to exploit operating system flaws. They have moved on to application-oriented vulnerabilities. This has the unfortunate effect of considerably widening the number of possible attacks.”

In addition to web application security rising in prominence over the coming year, database security and other mobile threats will continue to be a main concern, add BT's Schneier.

“There are more and more databases being pushed into the edge of the network, instead of residing solely deep inside the core of the corporate network environment,” he explains. “Also, USB port security will likely come into its own.”

Moreover, says BITS' Smocer, while the priorities noted in the *SC Magazine*/BT survey reflect what Smocer is understanding are priorities for BITS members, he sees an increase in expenditures for “the monitoring of outbound traffic levels and outbound traffic destination points.” Given some of the recent malware that has come onto the scene, this type of monitoring is proving effective in monitoring for data loss, he says.

“We do expect to see an increasing level of malware and trojan activity in the future, particularly focused at the consumer level, but also affecting corporate networks,” he adds.

Evolving with the threat landscape

“It has become clear, over the last two years in particular, that data theft has become a growing business with an increasingly growing level of crime syndication behind it,” says BITS' Smocer. “As organizations assess risk, most would have recognized this and recognized the need to keep enhancing their cyber defenses and internal controls.”

Also, generally speaking, corporate leaders must understand that as new technologies to meet business goals evolves, so too will cybercriminals, says Schneier.

“Attackers will always be looking for the path of least complexity and resistance,” he says. “Technology changes will enable new attacks.”

So, organizations have to be prepared. But, from the looks of the *SC Magazine*/BT survey, many are not.

“It is good that companies are taking the threat of data breaches seriously and taking steps to prevent them. Nevertheless, more can be done,” says Chris Painter, deputy assistant director of the FBI's Cyber Division. “I note that only 39 percent of respondents say that they have a cohesive and complete plan in place to react to data breaches. This is something that all companies should have, so that they are not scrambling to devise a plan in the midst of a crisis.”

Organizations and standards are out there that can assist security pros in building an incident response plan, says Starnes. And, while such planning does require a certain mindset, having a strategy in place before a breach occurs is critical.

Some corporate executives, though, may just think it won't happen to them. Experian's Scharf says it's probable that the 71 percent of respondents who don't have one in place haven't gone through a data incident before, which may, in their minds, “reduce the need for preparedness.”

Or, perhaps, they simply feel as if they don't have the resources to develop and test a formal incident response plan. For these companies, Scharf suggests starting “with some basic elements, such as creating calling trees and assigning system/application owners.”

“If a breach occurs, you will at least know who to call and which person is responsible for the system in question,” he explains.

Also, the plan should include arrangements to involve law enforcement entities, says the FBI's Painter, “so that we can bring those responsible to justice, help stem the distribution of stolen data, and thereby protect consumers and have a deterrent effect on those who might steal critical data in the future.”

In addition to incident response plans, it's also crucial to establish and continually strengthen overall risk management plans and security strategies. To be both effective and well-organized, IT security pros can enlist the help of standards to develop these. Approximately, 63 percent this time around, compared to 61 percent last year, are turning to standards to help evolve or better their overall security strategy. Those of note include ISO 17799 (35 percent), ISO 27001 (48 percent), the U.S. Department of Defense Trusted Computer System Evaluation Criteria (Orange Book) (26 percent), and standards such as COBIT, NIST, OWASP, PCI and HIPAA (24 percent).

The best tactic to create and maintain these: Pick and mix, says Starnes.

“None of the ... standards will exactly match the needs of a company,” he explains. “Do not be afraid to pick the components that work for your company from a wide range of standards, but never forget that compliance with a standard does not equate to security.”

The future

“Data breaches are posing an increasing and serious threat to consumers and businesses. The harm they cause is not limited to the financial cost of a stolen credit card and financial data, but includes substantial and difficult to quantify harm to the privacy of the consumers whose data is stolen,” says the FBI's Painter. “These breaches also can have a significant impact on the business reputation of those companies which are the victims of data breaches. Because of the value of financial, customer and other data, it is not surprising that cybercriminals, including online criminal groups, are targeting corporate data for theft and, later, distribution.”

And such online threats, both executed inside and outside the organization, are bound to increase, so companies must stay diligent, adds Smocer.

“The sophistication of organizations' risk processes has grown significantly over the last few years. While clearly other risks, such as credit risks, have come to the fore, we would believe that organizations' risk assessment

processes would continue to drive a focus on cyber risk,” says Smocer. “Of course, the realities of today's economy will have an influence as well.”

Growth of IT security budgets, then, might be less likely this year, he adds, but cyber risks and the potential negative impact they could cause will remain top concerns for most companies.

And since most organizations will try at least to sustain what IT security measures they have put in place, if failing to have the funding to further enhance them, the best approach for IT security executives will be to focus on risk assessment. This is because such a tactic will help focus decisions when pulling from scarcer resources, Smocer explains further.

Layoffs, cuts of non-revenue-generating services, and possibly even companies “falling into a state of non-compliance” with some regulations could be the result of reduced resources, according to Starnes, yet “consumer concerns over data protection” will continue to garner support for activities that safeguard such data in the next year.

In the end, the possible impacts to companies failing to address data security issues could be far greater than the initial capital outlay to mitigate against these, explains Experian's Scharf. Most corporate executives get this, even if bottom lines aren't what they used to be.

“Mature organizations understand that information security is not something that gets slashed indiscriminately to save a few dollars,” Scharf says. “These short-term cost savings can quickly lead to long-term losses if protections are dropped below acceptable levels. In addition, regulatory requirements demand certain thresholds that must be obtained, regardless of how the economy is performing. Where I do see increased change is in the transparency of information security spend and the need to continue to articulate the value proposition for requested initiatives. Security executives must be prepared to clearly demonstrate that their budgets are in line with industry averages and are appropriately structured.”

A good first step, he says, is to reconcile the company's existing spend and question what you pay for and what value you get for it. “Reducing costs by cutting products which have little value is a good first step in ensuring your required programs get the support they need.”

The SC Magazine/BT Data Breach Survey was conducted by SC Magazine and Millward Brown. Email notification was sent to corporate professionals and a

total of 217 IT/information security professionals completed the survey online between October 15-31, 2008. Results are statistically tested at a confidence level of 90 percent. Results aren't weighted.

[sidebars]

COMPLIANCE: Why it's important

Regulatory mandates continue to be a top reason why corporate leaders feel compelled to safeguard critical customer and company data.

Although regulatory mandates took second place at 71 percent in this year's *SC Magazine/BT Data Breach Survey*, it fell short only by a few points to possible negative impact to the company as the top factor at 75 percent. Other top drivers included possible profit loss at 43 percent, customer demand at 36 percent and executive board demand at 35 percent. In last year's survey, these two drivers tied for first place at 79 percent.

“Perhaps an explanation for the slight drop associated with ‘regulatory mandates’ is simply that they have become fairly long-lived and organizations have become used to complying with them,” says John Carlson (*right*), senior VP of BITS. “In addition, while regulatory mandates may have, at one time, served as a catalyst to action, we think most organizations have matured to the point where business issues have taken over as the key driver. Organizations realize that a perceived loss of customer trust can have a downstream effect on customer retention and on company reputation.”



Regulatory mandates were in the lead position at 62 percent for helping IT security departments get additional resources and budget, however. Possible negative impact to the company (59 percent), possible profit loss (35 percent), executive board (33 percent) and customer demand (30 percent) also helped, according to this year's survey data.

Specific mandates noted as priorities by respondents include Sarbanes-Oxley (50 percent), state data breach notification laws (43 percent), PCI (42.4 percent),

HIPAA (41.5 percent) and FISMA (34 percent). Others on the list included eDiscovery legislation, GLBA, FFIEC guidelines, EU Data Protection Act and still more. Experian's senior VP and global CISO Stephen Scharf isn't surprised by the spread.

“Most organizations have realized that properly focused SOX programs can have a positive impact on the protection of customer/client data. While attention to data breach requirements is critical, this is a reactionary process versus SOX, which is more proactive,” he says. “There is also the potential that more company have had to comply with SOX versus the number of companies that have been required to act in a breach notification process.”

To respondents of the survey this year, PCI was the most helpful mandate to 39 percent in providing details about the proper safeguards to protect customer/client data. Sarbanes-Oxley came in a close second at 36 percent, while HIPAA was third at 31 percent. Others noted included FISMA (28 percent), state breach notification laws (20 percent) and e-Discovery legislation at 18 percent.

Patty Edfors, chief privacy and security officer for Mirixa Corporation, a company sponsored by the National Community Pharmacists Association (NCPA) that specializes in targeted patient care services, says that in her experience PCI definitely gets top billing for being the most specific.

“The certification and self assessment criteria is very prescriptive. I think SOX requirements, since they are supposed to be tailored to the business environment but are based on COBIT, are reasonably disciplined but leave room for interpretation. SOX provides a general framework that allows you to pick and choose what you believe is critical based on materiality for that environment,” she explains. “A certain level of expertise is required, however, to make the right choices.”

Generally speaking, compliance likely will continue to push companies to ensure they're doing all they can to protect critical data. Yet, problems will continue to arise for those trying to meet demands. One only has to look to Hannaford's as an example. That company, when breached last year (see map) was actually touting being in line with PCI data security standards. Many industry experts used the breach as an example to remind organizations at the time that being compliant with regulations didn't necessary mean that they were actually secure. Richard Starnes, special assistant, Commonwealth Office of Technology for Kentucky, says companies would do well to remember that “compliance instruments are philosophical.”

“This leaves them open to wide interpretation and, in some cases,

misinterpretation. Thus, compliance instruments are only as effective as your assurance staff and executive management allow them to be” he explains.

Plus, many companies, with offices all over the globe, must contend with international laws – many of which conflict, he adds.

Among the many regulations just U.S.-based companies must deal with, there are still others. For instance, identity theft ‘red flags’ just took effect.

“The regulators and the FTC released them in final form in November 2007 with a compliance deadline of November 1, 2008,” says BITS’ Carlson. “These regulations emanate from the Fair and Accurate Credit Transactions Act (FACT Act). BITS and our member companies focused a significant amount of time this year discussing how best to comply with these requirements.”

According to Bruce Schneier, chief security technology officer at BT, a provider of communications solutions and services operating in 170 countries, it’s all about how much regulations are being discussed in the media and by the creators of the mandates themselves and who’s getting prosecuted for non-compliance. With these factors in mind, compliance likely will continue convincing companies to allocate the resources necessary to safeguard critical data.

“I think the top drivers are likely to remain the same in the coming months,” says Schneier.

SECURE CODING: Why it's important

Most experts agree that secure coding practices can go a long way in helping companies protect critical corporate data since cybercriminals often take advantage of holes in applications or software.

“Such practices do help to protect critical data in the sense that insecure coding can provide the pathway into customers’ and organizations’ data,” says Paul Smocer, VP of security for BITS.

Too few organizations, however, are bettering their secure coding practices before deploying applications for use by customers and clients, according to this year’s Guarding Against a Data Breach survey. Out of the 217 respondents, only 34 percent say they have strengthened these practices. Another 23 percent say they have not, while 30 percent say they have, but not nearly enough. Some 13 percent

don't even know.

“As resources are divvied up for security programs, it is concerning that secure software development is being overlooked in over 50 percent of the respondent's organizations. A successful secure software development lifecycle is essential in protecting critical data,” says Stephen Scharf, senior VP & global CISO for Experian.

He explains that a secure design process kicks off by bringing together “software architects and security architects to discuss application features and design flows.” This first step will result in “a functional and secure design,” he says. “This is then followed up with implementation reviews to ensure that the design is being written with strong secure coding practices. Lastly, a penetration assessment against the pre- and post-production application will flush out any overlooked issues that allowed exploitable conditions to exist.”

Other techniques that organizations can enlist to get on track with secure coding include training of their programmers, encouraging programmers to obtain certifications in the area of secure coding, and enhanced white and black box testing, says Smocer.

Failing to undertake these and other steps to ensure holes in their code is plugged, companies likely are leaving themselves open to increasing attacks that use insecure code, such as buffer overflow exploits, which have been on the rise the last few years, he adds. – *Illena Armstrong*
[From the January 2009 Issue of SCMagazine](#)

Steve on Bloomberg TV
Bloomberg
January 6, 2009

<http://www.bloomberg.com/avp/avp.htm?N=tvtoday&clipSRC=http%3A%2F%2Fvideo-static.clipsyndicate.com%2Fcs-video%2Fvol2%2F2009%2F1%2F7%2F58%2F351%2Fe6758f78-c0e5-463d-beb6-8b34aa01fdc7.flv>

Citi reaches deal with lawmakers on home loans
By ALAN ZIBEL

Associated Press
January 8, 2009

Democratic lawmakers have reached a deal with Citigroup Inc. on a plan to let bankruptcy judges alter home loans in an effort to prevent foreclosures and urged other lenders to follow suit.

The lawmakers aim to attach the plan to President-elect Barack Obama's economic stimulus legislation, and said Thursday the change in bankruptcy law could ease the foreclosure crisis that has dragged the economy into the worst recession in decades.

The compromise between Citigroup and Sens. Richard Durbin of Illinois, Charles Schumer and Christopher Dodd of Connecticut, would be limited to loans made before the bill is signed. Obama has said he backs the concept.

Schumer said he received calls Thursday from several banks — which he did not name — indicating their potential interest in supporting the idea.

"This is a breakthrough day," the senior senator from New York said in a news conference on Capitol Hill. "We've been stymied because the banking industry opposed this simple provision, which is key to getting a floor to the housing market."

New York-based Citi did not immediately comment on the announcement.

The so-called "cramdown" proposal has been backed by Democrats over the past year as a potential solution to the foreclosure crisis. Consumer advocates and Democrats say it would prod the lending industry to be more aggressive about modifying loans because of the looming threat of having a bankruptcy judge involved.

But the lending industry has battled fiercely against the idea, arguing it would force lenders to hike mortgage rates because they would have to charge more for loans that could be altered later by a judge.

"This would hurt the housing market at the exact time we're trying to stimulate it," said Scott Talbott, chief lobbyist at the Financial Services Roundtable, which represents large banks and insurance companies.

To qualify, borrowers would need to demonstrate that they have asked their lender for a loan modification before filing for bankruptcy.

Currently, a 1993 Supreme Court decision bars judges from altering first mortgages on primary homes, though such changes are allowed on loans for vacation homes, motorcycles, boats and other kinds of property.

Consumer advocates say that is unfair, while mortgage lenders contend it benefits the vast majority of borrowers who don't fall into bankruptcy because it keeps mortgage credit for primary residences cheap.

Other attempts by the government to deal with the surge in foreclosures over the past two years haven't made much of a dent in the problem.

A federal program, dubbed Hope for Homeowners, was intended to let 400,000 troubled homeowners swap risky loans for conventional 30-year fixed-rate loans with lower rates. But the early results have been disappointing, with fewer than 400 applications since the program's launch on Oct. 1.

In an interview earlier this week, a lobbyist for the mortgage industry vowed to keep the bankruptcy judge plan out of the economic recovery bill.

"We think that's an unwise move that could delay the stimulus package," said Francis Creighton, the Mortgage Bankers Association's chief lobbyist.

In a speech Thursday at George Mason University outside Washington, Obama asked Congress to work with him "day and night, on weekends if necessary" to pass an economic revival plan within the next few weeks so that it can be ready for his signature shortly after he takes office on Jan. 20

Obama promised to rewrite financial regulations and pledged to launch "a sweeping effort to address the foreclosure crisis so that we can keep responsible families in their homes."

Also appears in: Sun Herald, News & Observer, CNBC Online, ABC News, The Tribune, Columbus Ledger-Enquirer, The Olympian, Miami Herald, NPR

Henry Paulson Comments on The Role of the GSEs in Supporting the Housing Recovery
StreetInsider.com
January 7, 2009

Washington – Good afternoon. Thank you, David and thanks to the Washington Economic Club for this opportunity to provide my thoughts on long-term reform of the housing Government Sponsored Enterprises, the GSEs, Fannie Mae and Freddie Mac.

Debate over the role and function of these entities has raged for years. Congress established Fannie and Freddie decades ago to meet a public policy goal – to increase the funding available for home mortgage financing. The GSEs achieve this through providing liquidity to the secondary market for a limited range of home mortgages, either through credit guarantees on mortgage-backed securities (MBS) or by directly investing in mortgages and mortgage-related securities through their retained mortgage portfolios. To further this mission, their congressional charters grant the GSEs several benefits which together created a perception that the GSEs were backed by the U.S. government, even though this was not the case. This "implicit" government guarantee provided the GSEs with a funding advantage over other mortgage market participants.

The inherent conflict in this structure is obvious – the GSEs served both a public mission and private shareholders – they received public support but operated for private shareholder gain. While policymakers of every ideological stripe have acknowledged the risks created by this conflict, entrenched debate, often with little recognition of market realities, prevented reform. Over time, the GSEs' advantages enabled them to grow at a phenomenal pace, so that today they have \$5.4 trillion in obligations outstanding, held by investors in the U.S. and around the world. As a comparison, that is almost 40 percent the size of the entire \$14 trillion U.S. economy. The systemic risk posed by such size was heightened by the fact that investors assumed that GSE securities were backed by the U.S. government and therefore virtually risk-free, despite repeated statements by consecutive U.S. administrations to the contrary. These debt-holders would be the largest, but not the only, conduits of systemic impact should either GSE fail. Derivative counterparties, for example, would also be overwhelmed by a default of either GSE.

For some time market participants had questioned whether the GSEs were adequately capitalized for the risk they were taking, and therefore able to withstand losses without triggering a systemic event. Policymakers acknowledged that the GSE regulator did not have the authorities to address these risks, yet they could not reach consensus to improve it, and instead left a clearly inadequate regulatory structure in place. When I came to Washington, I saw an opportunity to improve the regulatory structure, even if it wouldn't be perfect. I set to work in the fall of 2006 to broker progress in the House, and we did begin to solve some of the seemingly intractable differences.

Even as Washington debated GSE oversight, there was little debate over the extent to which government should subsidize homeownership, and whether such government support was contributing to a housing bubble. The U.S. government has many policies that subsidize homeownership – it would be oversimplifying and wrong to blame Fannie and Freddie for the bubble, but they clearly are part of the public policy bias that contributed to it.

In sum, the GSE reform debate was largely frozen in place, or moving at glacial speed. Then suddenly, the unprecedented housing correction shifted the ground under that debate and forced action.

Today I will review the actions we have taken and their effect, and address two issues before us. First, in the short-term, how do we use the GSEs to mitigate the current credit crisis and housing downturn? Second, given the temporary nature of their current status, how might we address the appropriate long-term structure?

Prelude to Recent Actions Regarding Fannie Mae and Freddie Mac

As we progressed through the current housing market downturn, investors fled mortgages that carried any credit risk. But because the GSEs take the credit risk on the mortgages they guarantee and because investors believed there was implicit government backing, the conforming loan market continued to function relatively well. As a result, the GSE share of new mortgage business rose from 46 percent in the second quarter of 2007 to 84 percent in the second quarter of 2008. Without the GSEs to finance mortgages, it was very clear that mortgage finance would essentially dry up.

However, as the extraordinary housing correction deepened, weaknesses in these entities became apparent. In July 2008, investors lost confidence as they became increasingly uncertain about Fannie and Freddie's capital position. The GSEs' already depressed stock prices plummeted further. Shareholder losses did not pose a public policy concern, but the share price drop further weakened confidence among the holders of the \$5.4 trillion of GSE debt and MBS. Investors at home and abroad were reducing purchases and even selling from their holdings of GSE debt. The consequences of either GSE failing would be catastrophic. We couldn't wait for a failure; we had to act preemptively to shore up confidence in these enterprises.

In July, I requested that Congress quickly complete work on long-sought GSE regulatory reform and also provide Treasury with expanded authority to support Fannie, Freddie and the Federal Home Loan Banks. Congress did so – giving us enormous temporary authorities to inject capital if the GSEs asked for it, and to create a back up liquidity facility for GSE debt.

Immediately after passage of the legislation, in coordination with the Federal Reserve, the newly-constituted GSE regulator, FHFA, and our advisor Morgan Stanley, we began a comprehensive financial review of the GSEs. At the same time, mortgage market conditions continued to deteriorate. Negative earnings announcements by Fannie and Freddie in August reflected those worsening conditions, and further roiled markets. Neither company appeared to have any reasonable prospect of raising private capital to allay those concerns in the foreseeable future, and our examination found capital to be inadequate – in terms of both the quality of capital and the embedded losses stemming from worsening mortgage market conditions.

Confidence in the GSE model was largely shattered. It was clear to me that simply injecting even a great deal of equity into their business model would not create the market confidence necessary to fund these enterprises going forward and to bolster confidence in the \$5.4 trillion of extant GSE obligations, which posed the greatest systemic risk. Market fragility and the GSEs' deteriorating balance sheets required that we take responsibility for the GSE structural ambiguities that U.S. policymakers had let fester for decades. If we had asked Congress for, and received, the power to explicitly guarantee the GSEs' obligations, we would have done so. But without that authority, we had to be creative and find a way to effectively guarantee the GSEs' obligations.

We had to stabilize the situation immediately. We knew that markets were exceptionally fragile and would be further threatened in September when we expected that a number of large financial institutions, including Lehman Brothers, would post disappointing earnings. Chairman Bernanke, FHFA Director Lockhart and I met almost daily, over a 10 day period, to work toward a comprehensive action plan. As I made clear at the time, we sought a temporary solution that would achieve three goals: (1) stabilize markets, (2) promote mortgage availability, and (3) protect the taxpayer.

In comprehensive action taken on September 7th, FHFA placed Fannie and Freddie into conservatorship, enabling Treasury to take creative steps to support their obligations. We moved quickly to do what was necessary. Our actions would have been impossible to implement were it not for the GSE reform legislation that gave FHFA the expanded power to make qualitative and quantitative judgments about capital and also gave Treasury the financial authorities necessary to make conservatorship a stabilizing, as opposed to a destabilizing, event. We devised Preferred Stock Purchase Agreements to effectively guarantee the GSEs' obligations by ensuring Fannie and Freddie would maintain a positive net worth. This commitment ensures that they can fulfill their financial obligations, even after the temporary authorities expire in December 2009. Additionally, Treasury

established a new secured lending credit facility intended to serve as an ultimate liquidity backstop. To further support the availability of mortgage financing, Treasury initiated a program to purchase GSE MBS and has purchased over \$50 billion thus far.

We took these actions first, to avert the financial market meltdown that would ensue from the collapse of these institutions and, second, to allow the GSEs to continue, in the midst of overall market stress, to perform their essential role of providing mortgage finance. This conservatorship, with the explicit backing of the federal government, is temporary and must be resolved for the long-term. In the meantime, the GSEs must serve the taxpayers' interest by assisting in turning the corner on the housing correction, which is critical to return normalcy to the capital markets and resume U.S. economic growth. The GSEs can facilitate progress through the housing correction by keeping mortgage rates low and by mitigating foreclosures.

Keeping Mortgage Rates Low

Lower mortgage rates enable more potential homebuyers to return to the market and help put a floor under home prices. Initially, following our September actions, mortgage rates did fall. Market turmoil subsequently increased and mortgage rates rose, but not nearly as much as the cost of other forms of credit. Still, neither the taxpayers nor the economy were getting the full benefit of the agreements put in place to effectively guarantee GSE debt. We could have gone back to Congress to ask for authority to directly guarantee GSE debt, however this would have been difficult to achieve. While a simple, direct government guarantee of GSE MBS might have reduced rates further – given the extraordinary strains in today's markets it probably would still have failed to produce all of the desired mortgage rate reductions. Therefore, we examined other means of deploying our authorities that could reduce mortgage rates.

We immediately noted that, given the effective government guarantee and the spread between Treasury rates and those of the GSEs, the taxpayers would profit if the government simply issued Treasuries to buy GSE securities. And in fact, we have funded the purchase of GSE securities with the issuance of Treasury bonds. But to make an impact on mortgage rates, such an initiative would have to be very large and those Treasury issuances would count against the debt limit.

On November 25, the Federal Reserve announced a new program to purchase up to \$100 billion in GSE debt securities and \$500 billion in GSE MBS. This Federal Reserve program had a significant impact. The 30-year fixed rate has fallen from an average of 6.04 percent the week before the policy was announced to a record low 5.10 percent last week, accomplishing a vitally important step in addressing

this housing correction – lower mortgage rates that may bring additional credit-worthy buyers into the housing market.

Foreclosure Mitigation Efforts

While the GSEs are in this temporary form, we have also worked to increase their impact on foreclosure mitigation. In November, FHFA, the GSEs, Treasury and the **HOPE NOW Alliance** announced a major streamlined loan modification program (SMP) to move struggling homeowners into affordable mortgages. The new protocol relies heavily on the "IndyMac model" developed by the FDIC and creates sustainable monthly mortgage payments by targeting a benchmark ratio of housing payments to monthly gross income. Together with the IndyMac/FDIC protocol, the SMP creates a powerful new model that should help ensure that no borrower who wants to stay in their home and can make a reasonable monthly payment will fall into foreclosure.

The SMP will directly and immediately apply to the 50 percent of homeowners with loans serviced under the GSEs' auspices. Fannie and Freddie announced that they would suspend foreclosure sales and cease evictions of owner-occupied homes until January 9th to allow time for implementation of the modification program. The timing of this initiative is especially important as prime loans now account for almost 50 percent of new delinquencies, and delinquencies are increasingly the result of overall economic factors rather than the loan features and underwriting practices associated with Alt-A and subprime products.

And the impact of the SMP will go much further. The vast majority of servicing contracts for non-GSE mortgages reference the GSEs' practices, and we therefore expect the SMP to be widely adopted and quickly move hundreds of thousands of struggling borrowers into sustainable, affordable mortgages. Further, this streamlined protocol frees up servicing industry resources that can be redirected to providing case-by-case assistance to more difficult cases that fall outside the SMP protocol.

Impact of Temporary Authorities to Stabilize the GSEs

Given the authority granted by Congress last summer, we have gone about as far as we can to avert systemic risk and to use the GSEs to speed progress through the housing correction that lies at the heart of our economic downturn. Although the effective guarantee of GSE debt and MBS has brought some degree of stabilization, it is not the most efficient way to remove the ambiguity inherent in the GSE structure, even temporarily.

To the extent that the Congress and the next Administration wish to use the GSEs

as a tool to further reduce mortgage rates, they could, under existing authorities, make large purchases of mortgages made at a target rate of, say, 4 percent – although very large volumes of Treasury issuances would be required for such a program to be effective. A targeted program such as one that purchases only new mortgages made for home purchases, as opposed to refinancing, for a one year period would require less but still substantial funding. Separately, the next Administration could pursue legislative authority to directly guarantee GSE debt for the remainder of the conservatorship period.

Long-Term Policy Recommendations

The GSEs are playing a necessary role supporting the mortgage availability which is essential to eventually turning the corner on the housing correction, reducing the stress in our capital markets and returning to growth in our economy. This must continue to be our first priority. But we will make a grave error if we don't use this period to decide what role government in general, and these entities in particular, should play in the housing market.

The public debate over the long-term structure of the GSEs is dramatically changed today – no one any longer doubts the systemic risk these entities posed. It is clear to all conservatorship is a temporary form, and that returning the GSEs to their pre-conservatorship form is not an option.

The debate about the future of Fannie and Freddie requires answering the much larger and more important question of the federal government's role in the mortgage market and in housing policy, generally. Given the bubble we have experienced, policymakers must ask what amount of homeownership subsidies are appropriate. Numerous long-standing indirect subsidies already exist, including the mortgage interest deduction, subsidized FHA mortgages, and the variety of other HUD programs that expand homeownership opportunities.

Is that enough? Or should government also reduce mortgage rates for a larger group of homebuyers? Policymakers must decide if the GSE subsidy is a public policy priority. If the GSEs are to play a role, then, the debate is clearly framed: Government support needs to be either explicit or non-existent, and structured to resolve the conflict between public and private purposes. Any middle ground is a recipe for another crisis. Although there are strong differences of opinion over the government's role in supporting housing, under any course policymakers choose, there are structures and choices that can resolve the long-term conflict of purposes issues.

And it is clear that to protect against systemic risk in the future, the GSEs should be constituted with a portfolio no larger than what is minimally necessary for

warehousing purposes. Without portfolios of significant size, the enterprises' management of interest rate risk would remain a vital function for the safety and soundness of the enterprises, but would no longer present the same potential systemic risk.

As a public policy tool to expand homeownership, the GSEs, like FHA-Ginnie Mae, reduce mortgage rates for borrowers by taking on the credit risk that mortgage investors would otherwise bear and guaranteeing that mortgage investors will be paid in full should the mortgage borrower default. As Congress considers the future role and structure of the GSEs, it must consider how much credit risk the Federal government should take.

Addressing Credit Risk

In today's stressed mortgage market, between FHA-Ginnie Mae, Fannie Mae, and Freddie Mac, almost all new mortgage market originations have federal government credit support. This is not sustainable over the long-run. It will lead to inefficiency, less innovation and higher costs. It also contradicts basic U.S. market principles. We must have some degree of private sector involvement in the evaluation of credit risk if we are going to have a mortgage market that allocates resources with efficiency.

In the mortgage market of the future, I clearly see a role for the FHA and Ginnie Mae for first-time and low income homebuyers. Beyond the explicit guarantee provided to FHA and Ginnie Mae policymakers must decide how much to further subsidize mortgage credit risk, if at all, and must decide the role of private capital in any subsidy plan. Depending on the degree of subsidy policymakers choose, there are a variety of options for structures to replace the GSEs, including:

(1) Expanded FHA/Ginnie Mae. Some advocate that beyond the current credit crisis the U.S. government's long-term policy should make the implicit, explicit. Explicitly guaranteeing Fannie and Freddie's obligations would essentially nationalize this significant portion of the U.S. housing finance market. Under this model, the GSEs could become a government entity, or their functions could be absorbed by FHA/Ginnie Mae. In either case, the GSEs would no longer have private shareholders. The size of the eligible population of homebuyers would determine how large a share of mortgage credit exposure the government would own.

I view the permanent nationalization of the GSEs, essentially expanding the role of FHA and Ginnie Mae, as a less-than optimal model. While it offers the perceived advantage of explicit government support, it eliminates the necessary private sector evaluations of credit risk and the private market stimulus to

innovation.

(2) Partial Guarantee. A hybrid of this would be to create a Ginnie Mae-like entity for non-FHA mortgages, structured as a partial guarantee mechanism. The new entity could operate on a similar basis as Ginnie Mae, but provide only partial guarantees for MBS. Investors would then have a floor under potential MBS losses, but would still evaluate the credit risk associated with individual issuers. While such a hybrid program would clearly define the extent of the government's guarantee, developing risk sharing parameters compatible with profit incentives would be as problematic, and potentially as inefficient, as in the current GSE structure.

(3) Privatization. A third alternative would be to remove all direct or indirect government support, completely privatizing these companies while breaking them up to minimize systemic risk. As appealing as this alternative sounds, it is difficult to envision a sound, practical, private sector mortgage insurance business of any significant size that does not require large amounts of capital, and consequently generates only a modest return on capital. The recent problems encountered by monoline insurers, which ventured into guaranteeing mortgage product as well as the experience of the GSEs, underscores this point. Moreover, a break up scenario does not look particularly promising, as reverse economies of scale would take hold. It is also worth noting that a regional mortgage insurer would lack diversity as a risk mitigant. Perhaps a consortium of banks would find it advantageous to own a national mortgage insurer to wrap their product, or some other good private sector business model may emerge. But I am skeptical that the "break it up and privatize it" option will prove to be a robust or even viable model of any substantial scale, without some sort of government support or protection. However, should policymakers choose to scale back public policy bias toward homeownership, we will eventually find out what business model the free market would support.

(4) Housing Utility. Finally, given traditional U.S. public policy support for marshalling private capital to expand homeownership, establishing a public utility-like mortgage credit guarantor could be the best way to resolve the inherent conflict between public purpose and private gain. Under a utility model, Congress would replace Fannie Mae and Freddie Mac with one or two private sector entities. The entities would purchase and securitize mortgages with a credit guarantee backed by the federal government, and would not have investment portfolios. These entities would be privately-owned, but governed by a rate setting commission that would establish a targeted rate of return, thereby addressing the inherent conflicts between private ownership and public purpose that are unresolved in the current GSE structure. This commission would also approve mortgage product and underwriting innovations to continually improve the

availability of mortgage finance for a population to be defined by the Congress. In this model, continued safety and soundness regulation would be essential.

Need to Support Vibrant Private Market

If we are to maintain a private-sector secondary mortgage market – which I believe serves the taxpayer and the homebuyer equally well – then we must enhance the ability of depository institutions to fund mortgages, either as competitors to a newly-established government structure or as a substitute for government funding. One way to do this is for the government to receive some compensation for its guarantee. The current GSE Preferred Stock Purchase Agreements take a small step in this direction, in that as of 2010 the GSEs must pay the government a fee for the taxpayer backstop on their guarantees. Of course, if this rate perfectly reflected the risk versus the cost of the guarantee, there would be no subsidy to mortgage availability. It is obviously inherently difficult to reach an exactly correct price, yet a long-term fee-like structure in exchange for explicit government backing would help to reduce advantages over private institutions. Over time, another approach might be to offer other financial institutions the opportunity to pay a fee for government backing on securitized, conforming loans, a structural transformation that would lower entry barriers, and increase competition and innovation in housing finance.

Covered bonds are another private sector alternative worth exploring. The FDIC has made regulatory changes to support the emergence of covered bonds, which could provide enhanced opportunities for depository institutions to fund and manage mortgage credit risk. There is strong interest in developing a U.S. covered bond market, but we will have to work through the credit crisis before a new market is likely to take hold. Some have advocated dedicated covered bond legislation, which could be helpful to establishing this market, and should be considered in the context of broader housing finance reforms.

Additionally, the President's Working Group on Financial Markets has recommended extensive reforms in the mortgage securitization process by investors, ratings agencies, underwriters and regulators, especially with respect to mortgage origination oversight. When these reforms are in place, we expect private label securitization to return with greater oversight and market discipline.

Conclusion

My thoughts today are intended to inform the necessary debate over the future structure of the housing GSEs. By allowing the GSE structural ambiguities to persist for too long, U.S. policymakers have created an untenable situation. Today, Fannie Mae and Freddie Mac are in a temporary form that, while stable, cannot

efficiently serve their Congressionally-chartered mission and protect the taxpayers' investment over the long-term. We took the right actions to meet a specific need at a specific time.

The GSEs are critical to getting us through this current period, and this is our first priority. More may need to be done to clarify and simplify their structure and to increase their effectiveness in curbing further housing price correction. But we cannot look only at this short-term need; policymakers must resolve the question of long-term structure because the pre-conservatorship model has been disproven.

The first step must be for policymakers to decide – in light of the recent housing bubble and the severe financial and economic penalty it has imposed on our nation – the role government should play in supporting home ownership. We cannot allow a repeat of the devastation this housing correction has wreaked on families and communities across the United States. Once that decision is made, the GSEs should be restructured to meet that public policy choice and satisfy three objectives: First, there must be no ambiguity as to government backing. It must be explicit or non-existent. Second, there must be a clear means of managing the conflict between public support and private profit. Third, there must be strong regulatory oversight of the resulting institutions.

As I have outlined, whatever role the U.S. government chooses to play in subsidizing mortgage finance, there is a structure that can meet the objectives. With the knowledge of recent experience, we have a responsibility to begin work now on a long-term GSE structure which avoids the dangerous mix of policy and market distortions created by the former flawed GSE model. Thank you. [Link](#)

**US ABA Text:3Q08 Auto Loans,Home Eqty Delinquencies Record Hi
The Main Wire
January 7, 2008**

The following is the text of a release Wednesday morning by the American Bankers Association, reporting that consumer auto loan and home equity delinquencies reached a record high in the third quarter of 2008, while delinquencies declined for credit cards:

In the latest sign that consumers are under financial stress, delinquencies reached their highest levels ever during the third quarter of 2008, according to the American Bankers Associations Consumer Credit Delinquency Bulletin. In addition, the composite ratio, which tracks eight closed-end installment loan categories, rose 22 basis points to 2.90 percent of all accounts (seasonally adjusted), the highest level since 1980.

ABA Chief Economist James Chessen said the figures show a continued weakening of the U.S. economy.

"The number one factor in rising consumer credit delinquencies is job losses. With one million jobs lost in the first three quarters and two and a half million expected for the year, delinquencies of all types of consumer loans will likely increase in the coming quarters," Chessen said.

Delinquencies for indirect auto loans, which account for 90 percent of auto loans, rose 18 basis points to a record 3.25 percent. HELOC delinquencies rose seven basis points, marking another record high at 1.15 percent.

The bank card category was one of only two that showed a decline in delinquencies, dropping 34 basis points to 4.20 percent of all accounts. The ABA report defines a delinquency as a late payment that is 30 days or more overdue.

"While some people are relying on credit cards to meet daily expenses like food and gas, many are being careful not to add new debt. Reducing debt and building up cash reserves are good strategies right now. If you're under financial stress, credit cards can be a bridge to meet daily expenses. And, unlike other loans with fixed payments, credit cards let you adjust monthly payment amounts. This flexibility is certainly helping people manage debt better during this difficult economic period," Chessen said.

The third quarter composite ratio is made up of the following closed-end loans. All figures are seasonally adjusted based upon the number of accounts.

- Home equity loan delinquencies increased from 2.56 percent to 2.63 percent.
- Property improvement loan delinquencies increased from 1.49 percent to 1.63 percent.
- Indirect auto loan delinquencies increased from 3.07 percent to 3.25 percent.
- Direct auto loan delinquencies fell from 1.77 percent to 1.71 percent.
- Marine loan delinquencies increased from 1.54 percent to 1.82 percent.
- RV loan delinquencies increased from 1.07 percent to 1.27 percent.
- Mobile home loan delinquencies increased from 3.03 percent to 3.08 percent.
- Personal loan delinquencies increased from 2.67 percent to 2.69 percent.

Chessen advised consumers to watch for warning signs of financial problems and act quickly. Warning signs of overextended credit include:

- Paying only the minimum payment month after month;
- Being out of cash constantly;
- Being late on important payments such as rent or mortgage;
- Taking longer and longer to pay off balances; and

- Borrowing from one lender to pay another.

For homeowners having trouble paying their mortgage, ABA strongly recommends they consult www.hopenow.com or call 1-888-995-HOPE. **HOPE NOW** is a cooperative effort between counselors, investors, and lenders to help homeowners in distress.

For others who are having trouble paying down debts, ABA advises taking action -- sooner rather than later -- to solve debt problems with the following tips:

- Talk with creditors - the sooner you talk to them, the more options you have;
- Don't charge more purchases until your problems are solved;
- Avoid bankruptcy - it's a short-term solution with long-term consequences; and

Contact Consumer Credit Counseling Services at 1-800-388-2227.

For more information on budgeting, saving and managing credit, visit the ABA Education Foundations Consumer Connection web page at www.aba.com.

The American Bankers Association brings together banks of all sizes and charters into one association. ABA works to enhance the competitiveness of the nation's banking industry and strengthen Americas economy and communities. Its members the majority of which are banks with less than \$125 million in assets represent over 95 percent of the industrys \$13.6 trillion in assets and employ over 2 million men and women.

Indirect auto loan:

Loan arranged through a third party such as an auto dealer.

Direct auto loan:

Loan arranged directly through a bank.

Delinquency:

Late payment that is 30 days or more overdue.

Bank card:

A credit card provided by a bank.

Closed-end loan:

A loan for a fixed amount of money with a fixed repayment period and regularly scheduled payments.

Citi Reaches Deal With Lawmakers on Home Loans

By **CARL HULSE**

New York Times

January 9, 2009

WASHINGTON — In a move that would help troubled homeowners, [Citigroup](#) agreed to support legislation that would let bankruptcy judges adjust mortgages for at-risk borrowers, leading Congressional Democrats said on Thursday.

Financial industry lobbyists, however, said the plan was flawed and vowed to fight legislation aimed at easing up on homeowners facing foreclosure.

Members of the House and Senate said Citigroup had agreed to drop its opposition, providing no future mortgages are covered by the law.

Citigroup, which is receiving more than \$300 billion in bailout assistance, says that it is open to measures that would help homeowners.

“Citi shares this legislation’s goal to help distressed borrowers stay in their homes, and believes it will serve as an additional tool to the extensive home retention programs currently in place to help at-risk borrowers,” [Vikram S. Pandit](#), the chief executive of Citigroup, wrote in a letter released Thursday night.

The revised bill that Citigroup endorsed would allow bankruptcy judges to adjust the principal payments or interest rates on existing loans.

Judges could also extend the terms on mortgage loans, according to the language of the bill, which would force lenders to take losses without a say in bankruptcy court proceedings.

Senator [Richard J. Durbin](#) of Illinois, the No. 2 Senate Democrat, said he and fellow backers of the plan see it as a way to create more voluntary negotiations between struggling homeowners and financial institutions. So far, voluntary programs have proved ineffective, Democrats said.

Citigroup had been part of the Bankruptcy Coalition of the Financial Services Roundtable, an industry group, since it aggressively lobbied for changes to the bankruptcy code in 2005.

The coalition — a group of major trade associations and lenders like [Bank of America](#), [JPMorgan Chase](#) and [Wells Fargo](#); also fought to block the so-called cramdown legislation last year.

No other bank has broken ranks with the industry on the proposed bill. Mr. Durbin said he hoped the move by Citigroup, should other banks and financial trade associations take the same stance, would lead to backing by enough Democrats and moderate Republicans to push the bill through.

Senator [Charles E. Schumer](#), Democrat of New York, said he had been contacting officials of top financial institutions for months, trying to persuade them that it would be to their advantage to back the plan since it could help stabilize a housing market that has severely hurt the economy.

Three changes were made to the legislation sponsored by Mr. Durbin and Representative [John Conyers Jr.](#), Democrat of Michigan and chairman of the House Judiciary Committee: only existing mortgages will be eligible; homeowners will have to certify they tried to contact their mortgage holder lenders regarding loan modifications before filing for bankruptcy; and only major violations of the Truth in Lending Act will cause lenders to forfeit their claims in a bankruptcy.

Backed by bankers and other financial groups, many Congressional Republicans and some Democrats have balked at the plan to let bankruptcy judges alter mortgage terms on primary residences, saying that would drive up mortgage costs.

But officials said financial institutions were coming to the conclusion that it might be better to get a reduced loan payment through a bankruptcy or voluntary negotiations than to get no money at all.

Aides to Senator [Richard C. Shelby](#) of Alabama, the senior Republican on the Senate banking committee, said he would have no immediate response to the plan.

Scott E. Talbott, senior vice president for government affairs at the Financial Services Roundtable, said the group opposed cramdown legislation because it “creates huge risks” for the mortgage market.

He suggested the bill would force banks to further restrict lending and absorb huge losses as the economy worsens. He also suggested the bill would create perverse incentives that might encourage more homeowners to seek bankruptcy protection.

Citigroup recently began negotiating with lawmakers, in a move that some observers suggest reflects its desire to win favor on Capitol Hill after receiving billions in funds from the bailout program.

The government has invested \$45 billion in Citigroup and agreed to guarantee about \$269 billion in highly illiquid mortgage investments.

“If you’re looking at a way to get to the bottom of the economic problems in our country, this is the cause of our economic problems,” said Senator [Christopher J. Dodd](#), Democrat of Connecticut and chairman of the banking committee. “It is the housing foreclosure problem. We’ve got to address that.”

The plan has been backed by members of Congress who see it as a way to help distressed homeowners and balance federal relief efforts that have been aimed at Wall Street and the automobile industry.

Mr. Schumer said he had been in contact with other large banks and he expected they would soon announce their support or at least drop their opposition to the plan.

“Citigroup’s action has broken the dam,” he said.

Does Citigroup Stand Alone? Industry Balks at Bankruptcy Bill

By Theo Francis

BusinessWeek

January 8, 2009

If you want a sign the financial world is changing fast, look no farther than [Thursday’s announcement](#) that Citigroup would back legislation allowing judges to modify mortgage terms in bankruptcy.

The bill, championed for more than a year by [Sen. Richard Durbin](#) (D-Ill.) — and backed by many Democrats, including President-elect Barack Obama and Sen. Chuck Schumer (D-NY) — has been anathema to the financial-services industry

for just as long. The industry successfully fought it off several times over the last 18 months, most recently in this fall's negotiation over the [Emergency Economic Stabilization Act](#). And as recently as December, industry officials were promising an ugly fight, and saying they might still be able to head off the measure entirely.

No longer. Citigroup's announcement comes even as the same officials acknowledge that a compromise is likely — though perhaps not this compromise. “I think the politics, the substance, the economics, the tax angle all work against the industry on this one,” a financial-services industry official said in an interview Wednesday night, before the Citigroup agreement was public.

That doesn't mean the deal is done. Much of the industry still opposes the measure — and some even argue that Citigroup's support can be explained by its own self-interest: the bill could hurt its competitors more than Citigroup.

As it stands, [Durbin's bill](#) (SB 61) would essentially give judges the authority to rewrite the terms of a home mortgage -- a so-called "cramdown," something possible already for every other kind of debt, mortgages on vacation homes and any real-estate other than a primary residence. It would also extend [Truth in Lending Act](#) protections to bankruptcy court, meaning predatory loans -- made in violation of TILA -- would be wiped out.

To get Citigroup's support, Durbin agreed to three minor modifications. First, it would apply only to mortgages in existence when the bill passes, not future loans; lenders have argued that applying it prospectively would drive up the cost of borrowing for all homebuyers. Second, to qualify for a modification, homeowners would have to contact their lender at least 10 days before filing for bankruptcy, to give it a chance to offer a voluntary workout. And minor violations of TILA wouldn't wipe out a debt, but would instead incur a fine, bringing it into line with how the statute already operates outside bankruptcy court.

That's not enough for much of the industry. **The [Financial Services Roundtable](#), a trade group that represents a hundred banks, insurers and other big institutions, put out a statement opposing the compromise, calling the revised bill "a first step," but "still far too broad" and "a serious risk to the mortgage markets."**

The industry's main objections: the bankruptcy-modification provisions would apply to all existing mortgages, even million-dollar homes or those where the homeowner hasn't fallen behind on payments, and there's no time-limit, meaning lenders could still be dealing with bankruptcy modifications for current mortgages 30 years from now. Moreover, that truth-in-lending provision means a mortgage

can be wiped out. **"You get that house for free," FSR's Scott Talbott said in an interview.**

Supporters dismiss the industry's complaints. Unless they're at risk of foreclosure, most homeowners wouldn't qualify for bankruptcy, notes one Democratic Senate aide, and the truth-in-lending provision just mirrors the penalty outside bankruptcy court for abusive lending practices. As for putting a time-limit on seeking a modification in bankruptcy, "there's no good policy justification for that at all," the aide says.

So given the bulk of the industry's opposition, why does Citigroup support the bill? In a letter to lawmakers, Citi CEO Vikram Pandit says it "will serve as an additional tool" to help homeowners at risk of foreclosure. "Given today's exception economic environment, we support its swift passage," he wrote.

But some see a more sinister motive: Changing the bankruptcy law could force lenders and mortgage-backed security holders to take write-downs, under accounting rules that require companies to recognize hits to asset values once they become likely. (Since some homeowners will surely file for bankruptcy, and then receive mortgage modifications under the new law, some losses are likely.)

But the federal government has twice come to Citi's aid, plowing \$45 billion into the company to keep it stable. The second time, the government guaranteed the company against big losses on \$306 billion of real-estate loans and securities. (See the Treasury's [press release](#) and the [term sheet](#).)

Does that government guarantee protect Citigroup against losses from bankruptcy modifications, or from write-downs the company would otherwise have to take if the bill passed? Some in the industry worry that it does, giving Citi an edge over its competitors. If so, what harm to Citi to support the measure, ingratiate itself with lawmakers and look like the white knight?

A Citigroup spokesman declined to comment late Thursday. The Senate aide dismisses the argument, saying it makes sense only if the legislation were likely to drive a lot of viable mortgages into bankruptcy court, where they would be modified to the lender's detriment. In fact, the aide says, if homeowners can pay their mortgage, they're not likely to qualify for bankruptcy reorganization; most of the people helped by the bill would likely face foreclosure otherwise -- and in foreclosure, lenders stand to get a lot less than they would from a court modification.

"This actually helps all those firms that hold garbage on their balance-sheets," the aide says. "They would be hurt less badly than if these loans went through foreclosure."

[Kurt Eggert](#), a Chapman University law professor, notes that Citi and other financial firms have other reasons to support the bill as well: Most have taken billions of dollars in federal aid, any may be hoping for more. "It's harder for them to just say no to something that will obviously help homeowners," Eggert says.

Eggert says he worries that the 10-day notice requirement will hurt homeowners who don't know about the provision and file for bankruptcy to head off foreclosure. He also thinks applying it to future mortgages could make sense. "Having bankruptcy cramdowns is a way of instilling discipline to subprime lenders," he says. Investors could be more vigilant because they "aren't going to want to buy bad loans where there's going to be a cramdown."

Citigroup, Senators Agree on Bankruptcy Role to Trim Loan Rates
By Margaret Chadbourn
Bloomberg
January 9, 2009

Jan. 9 (Bloomberg) -- Citigroup Inc.'s agreement to back legislation that lets bankruptcy judges cut mortgage rates for at-risk borrowers drew criticism from bank industry lobbyists who said the compromise with Senate Democrats was flawed.

Citigroup endorsed the bill after Senate Banking Committee Chairman [Christopher Dodd](#), and Senators [Charles Schumer](#) of New York and [Richard Durbin](#) of Illinois, said they will limit the legislation to existing mortgages, rather than future loans. Durbin, the Senate's second-ranking Democrat, brokered the deal with Citigroup and sought similar agreements with other lenders.

"We can create a force that brings a bipartisan vote to the Senate floor," Durbin said in a Washington news conference yesterday. "I think we can enact this and I hope we can make it part of the economic recovery and reinvestment act."

The Citigroup deal with the Democrats failed to win support from the banking industry, which joined Republicans last year to help kill the legislation as the Senate sought to slow a record pace of foreclosures. Durbin yesterday said 8.1 million, or 16 percent, of homeowners may face foreclosure.

The Financial Services Roundtable, representing 100 banking, insurance and investment companies, said the compromise was a “first step” to improve a measure the group said remained “far too broad.” The Mortgage Bankers Association objected to the Citigroup agreement and said modifications are needed before the measure helps stem housing declines.

“We remain opposed to bankruptcy cram-down legislation because of the destabilizing effect it will have on an already turbulent mortgage market,” said [John Courson](#), president of the Mortgage Bankers Association, in an e-mailed statement.

Power to Judges

The revised bill Citigroup endorsed would give judges the ability to adjust principle payments or interest rates on existing loans, and could extend the term on the loan, according to the language of the bill, which would force lenders to take losses without a say in bankruptcy court proceedings.

“This legislation would represent an important step forward,” Citigroup Chief Executive Officer [Vikram Pandit](#) said in a letter to the three senators released by Durbin. “It will serve as an additional tool to the extensive home retention programs currently in place to help at-risk borrowers.”

Citigroup in November got \$306 billion of U.S. government guarantees for troubled mortgages and toxic assets to stabilize the bank. The deal, brokered by the Federal Reserve, Treasury Department and Federal Deposit Insurance Corp. required the bank to modify terms for guaranteed troubled loans based on a model created by the FDIC.

Congress Actions

Congress has passed several measures in the past year to stem home foreclosures, including a \$300 billion bill passed in July aimed at helping 400,000 borrowers keep their homes. Senate Democrats were unable in April to adopt the bankruptcy proposal. Republicans, and the banking industry, said the plan would raise costs because lenders would try to recoup losses in court with higher rates on other loans.

Durbin, set back by the defeat of the legislation in April, reintroduced his legislation Jan. 6, the same day House Judiciary Committee Chairman [John Conyers](#) introduced a similar bill. The Senate and House bills may be included in the economic stimulus proposals this year, said Max Gleischman, a Durbin spokesman.

Lawmakers modified the bill to require that borrowers show they had contacted their lender 10 days prior to filing with a bankruptcy judge to determine if an agreement can be reached, Durbin said. Schumer said limiting the provision to current mortgages helped ease Citigroup's opposition.

'Poker Game'

"This is something that Citi is championing but it's not clear that anyone is with them," said [Bert Ely](#), chief executive officer of Ely & Co. Inc., a financial institutions and monetary policy consultant in Alexandria, Virginia, in a phone interview. "It's an interesting political problem. There may be a poker game going on."

Consumer groups said the Citigroup agreement is a step that may help stem the record pace of foreclosures.

"We have long endorsed this and feel it is an important part of the puzzle that has hurt consumers and communities," said [Barry Zigas](#), director of housing and credit policy, Consumer Federation of America, in a telephone interview.

Citigroup accounted for 7 percent of the U.S. market for servicing home loans as of Sept. 30, according to the Inside Mortgage Finance newsletter in October.

Citigroup rose 1 cent to \$7.16 in New York Stock Exchange trading yesterday, and the shares have tumbled 74 percent in the past 12 months.

Citi backs measure to help avoid foreclosures

By Kevin Drawbaugh and Patrick Rucker

Reuters

January 9, 2009

WASHINGTON (Reuters) - Financial giant Citigroup Inc will support a proposal in Congress to rewrite U.S. bankruptcy law to help troubled mortgage borrowers avoid foreclosure, Chief Executive Vikram Pandit said on Thursday.

Citi had previously opposed changing the law to let bankruptcy court judges, in some circumstances, cut mortgage debts to help bankrupt homeowners. Its backing comes amid a recession and a mounting housing market crisis.

"If enacted, this legislation would represent an important step forward," Pandit wrote in a letter to lawmakers who midwived the plan including Senators Charles Schumer and Richard Durbin.

The letter called the proposal "an additional tool" to help prevent foreclosure.

Schumer of New York, Durbin of Illinois and Sen. Christopher Dodd of Connecticut, all Democrats, said the legal reform would help "millions of families save their homes."

The senators said they hope to attach the bill to a broad economic stimulus package.

A coalition of five consumer groups, including the Center for Responsible Lending, said: "We welcome the support of Citigroup, one of the nation's largest mortgage lenders, for responsible and urgently needed legislation."

A financial industry group said it still opposes the bill, calling it too broad and a "risk to the mortgage markets."

"The industry will still oppose the Durbin bill," said Scott Talbott, a lobbyist for the Financial Services Roundtable, in a statement.

SECOND ROUND FOR PLAN

Last year, Durbin failed to win Senate passage of a similar measure. Opponents, including Republicans, some Democrats and banking and housing industry lobbyists said the proposal would raise costs for future homeowners.

Republicans were wary of staking out a position on the measure. "It's far too early to make that kind of decision," Utah Republican Sen. Robert Bennett told Reuters on Thursday.

Michigan Rep. John Conyers, a Democrat, has introduced the measure in the House of Representatives so the plan can come before Congress even if it is not tacked onto the stimulus.

MORTGAGES PROTECTED

Today, most forms of personal debt such as vacation homes and family farms can be restructured in bankruptcy. But a mortgage on a primary residence cannot.

Under the proposed reform, the senators and Citi agreed that only mortgages entered into prior to its enactment would be eligible for the treatment. Homeowners would have to certify that they have tried to contact their lender before filing for bankruptcy.

Creditor claims on bankruptcy would be invalidated only by major violations of the "Truth in Lending Act" -- meant to protect homebuyers from fraud.

"Citigroup's support means that the dam has broken across the banking industry. We now have a real chance to pass this legislation quickly," Schumer said.

The National Association of Home Builders has dropped its opposition and the National Association of Realtors is mulling whether to support it.

The government has injected billions of dollars in taxpayer funds into Citigroup since October, making the nation's third-largest bank a top recipient of federal bailout money.

Senators, Citigroup reach cramdown deal
Seattle Post Intelligencer
January 9, 2009

Citigroup has reached a deal with Democratic senators on a plan to let judges alter mortgages for people in bankruptcy. See the [post](#) below for background.

Legislation allowing mortgage "cramdowns" would be part of an upcoming stimulus package and would be limited to existing mortgages, according to a Bloomberg [story](#).

"This legislation would represent an important step forward," Citigroup Chief Executive Officer Vikram Pandit said in a letter to the Senate released by Durbin and reported by Bloomberg. "It will serve as an additional tool to the extensive home retention programs currently in place to help at-risk borrowers."

The [Financial Services Roundtable](#), which represents 100 banking, insurance and investment companies, had issued a [news release](#) Tuesday opposing cramdown legislation. On Thursday, it called the compromise a "first step" to improve a measure that remained "far too broad," according to the Bloomberg story.

The Mortgage Bankers Association issued a [statement](#) in which President and Chief Executive John Courson and Chairman David Kittle restated opposition to the move.

"We remain opposed to bankruptcy cram down legislation because of the destabilizing effect it will have on an already turbulent mortgage market," they wrote. They said any such legislation should be limited to subprime loans, have a sunset date and move through the normal legislative process.