PREVENTING FORECLOSURE, PRESERVING HOMEOWNERSHIP

How Servicers Use High-Touch Methods to Reach Homeowners
Preventing Foreclosure, Preserving Homeownership:
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PAMELA AGAVA, PROGRAM MANAGER, AFFORDABLE HOMEOWNERSHIP
DOUG RYAN, SENIOR DIRECTOR, AFFORDABLE HOMEOWNERSHIP

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About Prosperity Now

Prosperity Now (formerly CFED) believes that everyone deserves a chance to prosper. Since 1979, we have helped make it possible for millions of people, especially people of color and those of limited incomes, to achieve financial security, stability and, ultimately, prosperity. We offer a unique combination of scalable practical solutions, in-depth research and proven policy solutions, all aimed at building wealth for those who need it most. For more information, visit prosperitynow.org.
INTRODUCTION

Since the end of the Great Recession in 2009, many researchers and housing practitioners have studied the causes of foreclosures and their effects on families, communities and the economy. This paper outlines the foreclosure process, provides more detail about the rationale of high-touch servicing as a foreclosure prevention method and describes effective practices for servicers helping homeowners resolve delinquency. Based on our research, we recommend servicers introduce the following practices:

+ **Timely and proactive initial contact:** Establish direct and personal communication with the borrower as early as possible to determine the reason for delinquency, their current financial status and potential resolutions other than foreclosure.

+ **Hands-on interaction with the borrower:** Institute customer segmentation so that delinquent borrowers are supported by staff who are technically skilled to deal with their specific manner of delinquency.

+ **Provide targeted modifications/resolutions:** Develop a clear framework of workout options that can be uniquely tailored to preserve homeowners’ ability to stay in their home or future ability to purchase, as well as the lenders’ interest in loss mitigation.

The consequences of foreclosure are well known by lenders, servicers and especially homeowners. In addition to damaging a homeowner’s access to credit, foreclosures can hinder children’s educational success, increase crime in communities and drain resources from local governments. While there is considerable research on the impact of foreclosures on homebuyers, much of the research on foreclosure prevention is framed primarily from the perspective of the lender. This very specific viewpoint creates several challenges in creating and implementing foreclosure prevention policies that also consider prospective and current homeowners. These challenges for homeowners and homebuyers include understanding the foreclosure process and finding opportunities to prevent foreclosure after missed payments.

However, throughout the term of the mortgage, there are many opportunities for servicers to support the borrower and retain mortgages by preventing foreclosure. When seen as a part of post-purchase foreclosure mitigation counseling, servicing that goes beyond standard servicing activities in the interest of the homeowner is referred to as high-touch servicing (HTS). High-touch servicing can be defined as enhanced servicing that involves closer and more frequent contact between the mortgage servicer and the borrowers. HTS, while not universally accepted as mortgage term, best captures the approach and processes of borrower-focused servicing. Servicers that employ high-touch methods more frequently contact delinquent borrowers, provide education about the loan terms and explain the options to avoid foreclosure.


2. Federal Housing Finance Agency Office of Inspector General

3. Ibid
METHODOLOGY

Leveraging public data and best practice research, we reviewed the servicing processes for 12 Community Development Financial Institutions (CDFIs), state housing finance agencies (HFAs) and other mission-oriented servicers. We selected organizations that meet two criteria: 1) they directly service a portfolio of loans, whether they own the loans or not, and 2) they implement unique solutions in their outreach to borrowers and resolutions in lieu of foreclosure. All the organizations demonstrate how servicing practices impact the total percentage of delinquencies and/or defaults in their portfolio. The practitioners and experts were asked to detail their organizations’ servicing practices and the elements of high-touch servicing that they have found most effective and why. We also covered a wide geographic area to identify solutions that could be implemented across a variety of housing markets.

OVERVIEW OF FORECLOSURE PROCESS

Foreclosure refers to formal legal proceedings initiated by a mortgage lender against a homeowner after the homeowner has missed a certain number of payments on his or her mortgage. When a foreclosure is completed, the homeowner loses their home, which is either repossessed by the lender or sold at auction to repay the outstanding debt. In general, the term “foreclosure” can refer to the foreclosure process or the completion of a foreclosure.

For the foreclosure process to begin, two things must happen: a homeowner fails to make a certain number of payments on their mortgage, and the mortgage holder or mortgage servicer decides to initiate foreclosure proceedings rather than pursue other options, such as offering a repayment plan or a loan modification—a restructuring of the mortgage where one or more of the terms of a borrower’s loan are changed to provide a more affordable payment. A borrower who misses one or more payments is usually referred to as being delinquent on a loan. When a borrower has missed three or more payments, they are generally considered to be in default.

The foreclosure process is governed by state law, meaning that the process and the time it takes varies by state. Typically, the servicer will send the borrower notices indicating how many payments they have missed and what workout options are available. At approximately

90 days, the servicer will send out a letter with workout options and a notice that if the borrower takes no action, the loan will be referred to foreclosure at 120 days.

The foreclosure process varies by state. Some states require judicial foreclosures, while others utilize nonjudicial, or administrative, foreclosures. Judicial foreclosures require servicers to file a lawsuit with the courts and prove they are entitled to foreclosure under state law and the loan document. Nonjudicial foreclosure does not require court approval, but rather is steered by a trustee for the servicer and governed by state law and loan documents. Due to a variety of factors, including whether a state uses judicial or nonjudicial foreclosures, the lengths of the foreclosure process vary from one month up to a year or more for both foreclosure processes. However, judicial foreclosures are typically longer and take several months to several years from the first notice of auction.

The servicer is required to notify the borrower—typically through mail—about the default before the foreclosure process begins. The Consumer Financial Protection Bureau (CFPB) requires servicers to make good faith efforts to establish contact with borrowers by the 36th day after the last payment. After notification, mediation (if required by the state) begins between the borrower and servicer. Mediation is a process by which a neutral third party assists the homeowner and servicer in reaching a fair, voluntary and negotiated agreement. At this point, the paths of judicial and nonjudicial foreclosures diverge. Judicial foreclosure requires a filing and trial with the court. A servicer representative files various documents that form a complaint, which must be served to the borrower notifying them of the litigation. Most judicial foreclosures are not contested by the borrower and result in favor of the servicer. Nonjudicial foreclosures move to notice of intent to foreclose, if required by state. It is also necessary for servicers to advertise the sale, which varies by state. However, normally the sale will be advertised in a newspaper of record a few weeks prior to the sale. Both foreclosure processes converge at the proceeding to advertisement of sale and finally, sale. If the former homeowner does not leave the home voluntarily, the foreclosure sale purchaser can have the previous owner evicted.

The servicer of the mortgage will send a notice of foreclosure sale. Some states grant a borrower a right of redemption. This process allows borrowers to repurchase their home within a certain period after the foreclosure. In New Jersey, right of redemption lasts 10 days, while the right of redemption period lasts two years in Tennessee. Though it is unlikely for a borrower to come up with the money to redeem their property, the right can be exercised during the length of time prescribed by state law.

10 Ibid
13 Ibid
Housing Finance Agency (HFA) Insights on In-House Servicing

In the last HFA Single-Family Loan Servicing Survey put out by the National Council of State Housing Agencies (NCSHA), nearly 40% of HFAs reported that they service their single-family loans in-house. Research supporting this claim is rising. A working paper published by Fannie Mae states that single-family loans originated through state HFA program perform better than similar loans to low- and moderate-income borrowers. The paper credits this to the control and flexibility of in-house servicing as part of the reason for the reduced number of default and foreclosed loans. This is because of, according to the paper, increased monitoring and additional preventative servicing practices, specifically in-house servicing and post-purchase counseling. Other services included earlier default counseling and more assistance with loan modification.
OVERVIEW OF SERVICING

Loan servicing is the process by which a company (mortgage bank, servicing firm, etc.) collects interest, principal and escrow payments from a borrower. The payments collected by the mortgage servicer are remitted to various parties; distributions typically include paying taxes and insurance from escrowed funds, remitting principal and interest payments to investors holding mortgage-backed securities (or other types of instruments backed by pools of mortgage loans) and remitting fees to mortgage guarantors, trustees and other third parties providing services. The level of service varies depending on the type of loan and the terms negotiated between the servicer and the investor seeking services, and may also include activities such as monitoring delinquencies, workouts/restructurings and executing foreclosures. Servicers can generally begin foreclosure proceedings after a homeowner defaults on his mortgage, although servicers vary in how quickly they begin foreclosure proceedings after a borrower goes into default. In exchange for performing these activities, the servicer generally receives contractually specified servicing fees and other ancillary sources of income such as float and late charges.

Bank servicers are any depository institutions that service mortgage loans. These are often larger banks that offer retail depository services most potential homebuyers are familiar with. In most cases, homeowners already have checking and savings accounts, so it is reasonable to get their mortgage from the same institution, and it is likely that their servicing will be in-house although the lender may transfer servicing rights. Because of the mortgage crisis, and subsequent credit constriction, as well as an overall lack of trust in traditional banking systems to finance homeownership, other alternatives have grown as the major originators and servicers of mortgage loans.

These alternatives, known as nonbank lenders, are non-deposit-taking institutions that service mortgage loans. In the private sector, these lenders tend to be online companies with revenue generating loans, including mortgages. These lenders either service loans themselves or use nonbank service companies. Some nonbank servicers are small servicer-only companies, some are full-service mortgage finance companies that also originate loans. Although bank and nonbank servicers are subject to the same regulations, the interaction with a delinquent homeowner can vary widely depending on the type of nonbank servicer.

Mission-driven and nonprofit servicers make up another category of mortgage servicer. Like nonbank servicers, some are smaller operations, servicing on loans they originate; others are servicing arms of nonprofit lenders or other types of mission-driven financial institutions. Many of these servicers are tied to larger nonprofit groups, like Habitat for Humanity or other nonprofits with lending arms like community development corporations (CDCs) or CDFIs, with community development as their primary mission. While these institutions share a common mission, they have a variety of structures with homeownership being just one of many goals that they focus on.
Jacob's Story

Jacob purchased his home in 2013 in the La Pradera Subdivision in Santa Fe. He missed his October 2015 mortgage payment, but quickly sent it in November and stayed mostly on track for the next two years. Throughout 2017 and early 2018, Jacob would fall three months behind. Homewise, his mortgage's servicer, was having trouble reaching Jacob—he would not return phone messages left at both his workplace and his cell phone. They sent him letters every month with no response.

In January of 2018, a “certified” demand letter was sent, resulting in one month's payment being made in March. A second and “final” demand letter was sent in April with the next action being foreclosure. By this time, Jacob was five months delinquent, owing over $7,000 on his first mortgage and nearly $2,000 on his second mortgage.

After receiving the final demand letter, Jacob and his fiancé, Sandra, came into Homewise offices with three months of payments and wanted to discuss a payment plan to get current and keep their home. Two Homewise loan servicing associates met with Jacob and Sandra to conduct a budget analysis. They found out Jacob’s mortgage was set up to be automatically deducted on the 5th of each month, but that he did not get paid until the 7th. Jacob did not know he could get his mortgage payment date changed to accommodate his payday, so he did nothing and continued to fall behind. After working with the loan servicing associates, Homewise moved his automatic payment date to the 15th of each month. Today, Jacob and Sandra are current on their monthly payments.
SERVICING AS POST-PURCHASE FORECLOSURE PREVENTION

Prior to the foreclosure crisis, post-purchase standards for mortgage servicing and modification for troubled homeowners were very straightforward. Servicers were responsible for collecting and processing borrower payments and for minimizing losses for investors. Although the early 2000s saw a dramatic increase in homes purchased by low- and moderate-income homeowners, the finance industry did not develop a high-touch servicing system that would support borrowers who may be more likely to default.

Instead, servicers focused almost exclusively on collection processes for the increasing number of homeowners who were delinquent in payments. In 2009, a federal program—Making Home Affordable (MHA)—was created to provide foreclosure alternatives to homeowners impacted by the financial crisis. Under MHA, the Home Affordable Modification Program (HAMP) provided a standard for mortgage modifications to reduce monthly mortgage payments of strained homeowners to an affordable amount. A 2016 report on HAMP found that “most solutions offered to a delinquent homeowner before 2009 sought to mitigate the investor’s risk by adding unpaid interest and fees to the mortgage balance.” These options often resulted in higher payments for homeowners and did not address hardship or long-term affordability.

In 2013, the CFPB developed mortgage servicing rules that developed a framework for the industry. Through Regulation X of the Real Estate Procedures Act (RESPA), the agency implemented provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act regarding mortgage loan servicing. Dodd-Frank refers to both the statute and the comprehensive implementing regulations born of the Great Recession. Intended to protect consumers from the risky lending practices that caused the crisis in the first place, the act implements a set of requirements on lenders and servicers. Some industry practitioners as well as some analysts view these regulations as an overreaction to the recession that burden financial institutions with cumbersome and expensive paperwork and red tape.

The regulations required servicers to correct errors in servicing brought to the servicer’s attention by borrowers; addressed servicers’ obligations to establish reasonable policies and procedures to achieve certain delineated objectives; to provide information about mortgage loss mitigation options to delinquent borrowers; to establish policies and procedures for providing delinquent borrowers with continuity of contact with servicer personnel capable of performing certain functions; and to evaluate borrowers’ applications for available loss mitigation options. It also required servicers to provide disclosures to borrowers about transfers of mortgage servicing.

17 Ibid
While inefficient or poor mortgage servicing increases costs and causes irreparable damage to homeowners, communities and investors, the costs of servicing mortgage loans have increased since the 2008 foreclosure crisis. By 2008 and 2016, the per loan cost of servicing a “nonperforming” loan, one that is either delinquent or in default, has more than quadrupled. In the same period, the cost of servicing a “performing” loan, one for which the borrower is not behind on payments, has nearly tripled. Many in the industry would say this reflects the regulatory costs post-Dodd-Frank and RESPA. Many criticisms, however, fail to account for the benefits that are derived from the prevention of foreclosures.

The rules of RESPA and Dodd-Frank established the bare minimum standard of servicing. This opened the door to viewing servicing from the context of the borrower—rather than the investor—with the primary goal shifting to preserving homeownership instead of loss mitigation. As a result, there are now opportunities to use servicing as a method to prevent homeowners from foreclosing on their home. Servicing can take shape in a variety of ways before and after a mortgage is acquired.

High-touch servicing can involve education, early detection of delinquency, providing financial training, supporting clients’ negotiation with lenders, and providing financial assistance to make mortgage payments or meet financial emergencies. High-touch servicing is not a one-size-fits-all solution; rather, the servicing requires a variety of approaches with individual specific measures. Organizations that implement high-touch servicing provide intensive contact with delinquent borrowers, multiple forms of education, and thoroughly-explained options to avoid foreclosure.

High-touch servicing results in more positive outcomes for borrowers and servicers. For servicers, a portfolio of 384,000 higher-risk loans serviced by utilizing high-touch servicing could realize credit loss savings ranging from “approximately $1.7 billion to $2.7 billion over the subsequent five years.” Sixty-five percent of homeowners have seen improved monthly budgets, 72% have improved credit scores and average credit scores improved by 25 points after 12 months of coaching.


23 Ibid

24 Ibid, 16

Manner of Crisis

Manner of crisis refers to the many reasons why a homeowner might be delinquent on a payment. Servicers will determine available options in lieu of foreclosure based on how early they are informed of what caused the delinquency. The timing of intervention can also minimize the severity of impact to the homeowner’s credit score. We already know that 39% of households are not prepared to deal with an emergency of $1000 or less and still be able to pay all their bills for the month.* Servicers also consider different households’ cases according to their unique circumstances. For example, a servicer will deal with a household experiencing delinquency based on a short-term, unexpected emergency differently from a couple that is divorcing and neither person can continue to afford the mortgage on their own. It is important for the servicer to determine whether the circumstance that is causing non-payment is a chronic or prolonged issue with no clear end in sight, i.e. unemployment or underemployment, divorce, reduced income because of death of primary or secondary breadwinner, or some other scenario that can be addressed through a loan modification or workout plan. Unique scenarios present opportunities for innovative and creative solutions to avoid foreclosure.

RECOMMENDATIONS

High-touch servicing requires ensuring the appropriate level of operations and capacity needed in a non-crisis environment; how operations and/or processes can be simplified or elaborated; how servicing practices can most effectively address the needs of homeowners and investors; and how servicing solutions can affect homeowners’ access to credit and homeownership in the future.26 High-touch servicing practices that help servicers, homeowners and investors range from low-level interventions to more complex and involved practices. When all these issues are addressed in practical ways, high-touch servicing can prevent foreclosures, in turn promoting healthier communities while encouraging asset development for moderate- and low-income families. The following recommendations have proven effective at helping homeowners resolve their delinquency and avoid foreclosure.

1. PROACTIVE, EARLY AND CONSISTENT COMMUNICATION BY SERVICERS WITH DELINQUENT HOMEOWNERS

Servicers should have a more personal and timely interaction with homeowners. All letters and calls to delinquent homeowners must meet federal regulations, but also convey a sense of willingness to support homeowners regardless of their financial


circumstances and as quickly as possible. This includes making sure that borrowers can speak with a live person, in their language about their modification and loss mitigation options. Furthermore, this method of effective communication should be implemented as early as possible to establish a valuable relationship between the borrower and lender.

Research has shown borrowers ignore letters from their lender/servicer once they are in default. However, many HFAs and non-bank servicers use creative methods to reach out to borrowers via snail mail. For example, Neighborhood Housing Services of Chicago (NHS)—a nonprofit neighborhood revitalization organization that provides housing services and lending to homeowners and new homebuyers—facilitates a co-branded letter as a part of its written correspondence procedures. A co-branded letter is when the investor and/or servicer partners with a third-party organization, usually one with community standing, to send out a letter to delinquent homeowners. The letter includes the organization’s logo, address and contact information, and will contain details about borrowers’ accounts and possible workout plans available if they reach out to their lender. Borrowers may be more likely to open and respond to letters from a more trusted or favorably recognized organization than from their lender or servicer.

The Pennsylvania Housing Finance Agency (PHFA) reaches out to homeowners if they are more than 12 days delinquent and then reaches out to homeowners who did not respond to the first mailing through a second mailing with colored envelopes and hand-written, informal prose to avoid a formal business look. PHFA found that these high-touch servicing methods raised the odds of borrowers reaching out and considering their mortgage options. PHFA found that 59% of high-touch servicing recipients remained current with payments, 38% were delinquent and three percent were in the foreclosure process.

Research also indicates that troubled homeowners who receive early outreach and intervention are more likely to receive loan modifications and/or keep their homes. Habitat for Humanity Michigan Fund (HFHMF), a nonprofit that originates and services mortgage loans for Habitat for Humanity affiliates throughout the country, reaches out to the borrower on the first day after the grace period, which could be as early as 10 days after missed payment. They send out standard delinquency letters in addition reaching out via phone. By initiating contact earlier, a servicer can facilitate more interactions, which means the homeowner has more to respond before initiating foreclosure. This also means that the servicer can present more options as resolution in lieu of foreclosure.

2. **HANDS-ON INTERACTION WITH DELINQUENT BORROWERS**

Another powerful tool in high-touch servicing is customer segmentation, which is sometimes absent in mortgage servicing. HFHMF has three full-time staff dedicated solely to contacting delinquent borrowers. One staff person is responsible for all delinquencies up to 45 days, another for delinquencies between 46-90 days and

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27 Merrill, W. “‘Interventions in mortgage defaults: Problems and practices to prevent home loss and lower costs.” In N. P. Retsinas & E. S. Belsky (Eds.) (2008);


the last for all delinquencies over 90 days. HFHMF has specific staff dedicated to borrowers in this way to ensure staff have the knowledge and skillset to address the potential problems that will be faced by borrowers at each stage of delinquency. Effectively meeting the needs of these customers will generate better resolutions for the investor and the homeowner.

The hands-on approach to communicating with borrowers goes beyond speaking on the telephone or face-to-face interviews. The hands-on approach in high-touch servicing involves servicers taking direct actions to understand clients’ financial situations and end goals and working to communicate their goals and expectations. Loan servicers should be experienced in both lending practices related to loss mitigation and effective personal counseling skills. They need to be able to negotiate with lenders on behalf of clients and, when necessary, bring pressure on lenders to respond.

While this structure may be staff-intensive, it almost always brings quicker results for the borrower. First, the borrower is working with someone who is skilled enough to accurately assess the borrower’s situation and needs. Second, the servicer knows that any plan that is developed has a reasonable chance of success. All the servicers we spoke to indicated they would be willing to negotiate a solution, especially if they can be assured that the borrower is able and willing to follow any plan that is designed for them.

3. PROVIDE TARGETED MODIFICATIONS AND RESOLUTIONS.

Servicers need to be aware of what is available for clients based on the investors’ interests but also in preservation of the borrower’s future ability to purchase a home and meet other credit needs. This includes non-traditional solutions that are typically not available to depository institutions—particularly in the case of mission-driven organizations and CDFIs—such as requiring financial coaching or counseling, working with homeowners to supplement mortgage payments through loan modifications, forbearances and other workout options. The specifics of these options need to be determined by the servicer because they will have to be fully implemented with the same characteristics of high-touch servicing: as early as possible, with a strong focus on communication and a very hands-on process.

In foreclosure prevention, the “why” of a missed payment is as essential as how many payments are missed. There are many reasons why homeowners default on their home loans: changes in employment that lead to lower or no income, a chronic illness of a family member of the household or even more personal reasons, such as divorce or the death of a wage earner. While these events are hard to predict and guard against, families are particularly vulnerable in costly housing markets.

The lack of adequate loss mitigation options is a major reason why foreclosures are the only option for some homeowners. When the loss mitigation option does not address the “why” of homeowners’ inability to pay their mortgages, it should be considered ineffective, even when loss to the investor is mitigated. Most homeowners are looking for forbearance or payment assistance, generally in the form of loan modifications. It is the servicer’s job to determine the loan modification that will adjust the terms of the loan to an amount that the homeowner can afford. If loan modifications cannot address the delinquency, the servicer should work with
the homeowner to come to a solution that is realistic based on the homeowner’s financial situation, preserves the homeowners credit and mitigate loss to the lender. This will often require innovative solutions not commonly employed in the servicing industry. Homewise, a CDFI in Santa Fe, New Mexico, offers a variety of services and programs for new homebuyers and homeowners. Depending on the borrower’s situation, the organization may buy back property from a delinquent homeowner to keep the home in its portfolio until it can be sold again. This cuts costs on collections and relieves the homeowner of a financial burden that no loan modification could satisfy, preserving their credit and saving them money as well. Because Homewise also does lending, it can offer specialized loan products as resolutions.

CONCLUSION

In our observation of best practices in high-touch servicing, we found a variety of organizational models. There are organizations that make live phone calls, personalized mailers and direct visits to the home; and more narrowly-focused organizations that rely on a network of community partners to provide a wider array of support services, like financial coaching or assisting delinquent borrowers with accessing state or federal funds. Across these organizational models, we identified essential components for effective service provision in foreclosure prevention. Organizations may implement different mechanisms depending on servicer or loan type and manner of crisis of the borrower.

High-touch servicing can prevent foreclosures, promote healthier communities while encouraging asset development for moderate- and low-income families. Although the number of delinquencies and foreclosures subsided in recent years, the resources needed to service delinquent homeowners should still be implemented. Going forward, CDFIs, HFAs and other service organizations designing future loss mitigation programs with high-touch servicing should implement:

+ **Timely and proactive initial contact**: Establish direct and personal communication with borrowers as early as possible to determine the reason for delinquency, their current financial status and potential resolutions other than foreclosure.

+ **Hands-on interaction with the borrower**: Institute customer segmentation so that delinquent borrowers are supported by staff who are technically skilled to deal with their specific manner of delinquency.

+ **Provide targeted modifications and resolutions**: Develop a clear framework of workout options that can be uniquely tailored to preserve homeowners’ ability to stay in their home or future ability to purchase, as well as the lenders’ interest in loss mitigation.
Overall, high-touch servicing seeks to resolve a homeowners’ financial burden in a way that works not just for the investor, but the homeowner as well. We know that investors take heavy losses on foreclosures: on average, 50% or more of the remaining loan value. 30 This suggests that a significant portion of distressed mortgages could and should be resolved short of foreclosure. Servicers and investors should be willing to conduct a loan workout whenever the net present value of loss mitigation exceeds the net present value of foreclosure. 31 A home is often a family’s most valuable possession. Preventing foreclosures will not only prevent unnecessary loss for the lender but also helps keep families in their homes and preserves communities.

31 Ibid