THE WALL STREET JOURNAL.
WSJ.com

September 5, 2012, 8:00 AM ET

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ByNick Timiraos

Reuters

New research helps explain why President Obama’s signature loan-modification effort fell short of its goals.

It seemed like an easy sell to banks: dollars for mortgage modifications.

It turned out to be more complicated than that.

A new academic paper argues that President Obama’s signature loan-modification push fell short of its ambitious goals in part because large banks weren’t able to respond quickly enough.

The White House launched the Home Affordable Modification Program in 2009 with a goal of reaching at least three million borrowers, but to date it has provided permanent loan modifications to about 900,000 homeowners. It provided taxpayer money to banks that successfully provided homeowners with reduced mortgage payments, largely by cutting their interest rate and extending their loan term.

Some mortgage firms, known as “servicers,” were able to actively conduct modifications when the program launched, the report says, but the program’s overall low rates of modification “reflects servicer-specific factors that appear to be related to their pre-existing organizational capabilities.”

The report doesn’t identify particular banks or servicers, but it says that some large firms responded to the program “at half the rate of others.” For example, some servicers might not have implemented the program as quickly or robustly because it would have required wholesale changes to their loan-servicing infrastructure.

The deliberate approach of the program, with its “extensive screening” of eligible borrowers, did avoid widespread strategic defaults.

Overall, though, the research suggests the financial-incentives approach could be flawed. The researchers conclude that the "ability of government to quickly induce changes in behavior of large intermediaries through financial incentives is quite limited, underscoring significant barriers to the effectiveness of such policies."

The analysis was conducted by researchers **Sumit Agarwal** and **Gene Amromin** at the Federal Reserve Bank of Chicago; **Itzhak Ben-David** of the Ohio State University; **Souphala Chomsisengphet** at the Office of the Comptroller of the Currency; **Tomasz Piskorski** of Columbia Business School; and **Amit Seru** of the University of Chicago.

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The Obama administration has argued that HAMP made to important changes, even if it fell short of its stated goals. Loan modifications have become more sustainable and have significantly lower rates of default today, in part because HAMP forced banks to focus on reducing borrowers' monthly payments.

The administration also says that HAMP set a framework for proprietary modifications that banks extended outside of the program, which had much stricter rules that limited its reach, and that banks modified more than two million loans under similar terms outside of HAMP.

Large banks, for their part, have generally conceded that the program was needed in order to standardize the previously haphazard loan-modification process. But officials have criticized the government program for having too many rules, and for changing those rules too often, which slowed down their ability to ramp up their response.

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