



Curing Underwater Mortgages, Preventing Foreclosures and Avoiding Moral Hazard through Principal Reduction, Shared Appreciation Modifications

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The Negative Equity Problem

According to a recent report by CoreLogic, as of the fourth quarter, 2010, over 11 million homeowners were “underwater” with their mortgages, that is, they owe more than the market value of the home. This negative equity problem afflicts nearly 23% of all mortgages in the United States. Upwards of two million underwater homeowners are expected to go into foreclosure. Many will be the result of “strategic defaults” – borrowers driven to give up homeownership in favor of renting rather than to continue to make monthly payments with no real prospect of regaining positive equity in their home. Based on our experience from our servicing portfolio, homeowners in a negative equity position are 150% to 200% more likely to default on their mortgage than those with positive equity. If, as a growing consensus predicts, home prices decline another 5% to 10% in 2011, homeowners currently underwater will sink deeper and millions more just barely above water will go under.

Principal Reduction Modifications

As a mortgage loan servicer, we find that principal reduction modifications are key weapons in our arsenal to cure defaults and prevent foreclosures due to negative equity. Of course, all modifications -- with or without principal reductions -- must be designed to return to the loan investor greater cash flow, on a net present value basis, than foreclosure proceeds. Taking into account homeowner income, home valuation, degree of delinquency, borrower acceptance, prepayment and redefault probabilities, resolution timelines and other relevant data, our optimization models and behavioral science research increasingly demonstrate that principal reduction modifications of underwater mortgages are indeed NPV-positive for investors.

Concerns have been raised, however, over whether principal reduction modifications create a “moral hazard” by rewarding imprudent over-borrowing by consumers and providing an incentive for even more strategic defaults. In

response to these concerns, and consistent with our ongoing commitment as servicer to continue to find creative win/win solutions for both loan investors and homeowners in this challenging environment, we have added a shared appreciation component to our principal reduction modifications, as described more fully below.

The Shared Appreciation Solution

We are pleased to announce the national roll out of our Shared Appreciation Modification, or SAM, program. In a SAM, we are writing down principal to a newly modified loan-to-value ratio of 95%. The write down is designed to optimize borrower acceptance of and commitment to the program, which in turn lowers redefaults. The written down portion of the principal is held in a separate, non-interest bearing account which is completely forgiven in one third increments in each of the three years following the modification, so long as the homeowner stays current on the modified terms.

If, upon a subsequent sale of the home or refinance of the loan, the home value has appreciated, then the SAM allows the borrower to retain 75% of the gain and pay the remaining 25% to loan investor (not loan servicer). In calculating the amount of home value appreciation, the homeowner gets full credit for any capital improvements made to the property during the term of the SAM.

We believe our SAM program provides an effective and balanced approach to preventing foreclosures of underwater mortgages while ameliorating potential moral hazard, to the benefit of mortgage loan investors, homeowners and, ultimately, the housing market and our national economy.

About Ocwen

Ocwen Financial Corporation is a leading provider of residential and commercial loan servicing, special servicing and asset management services. Ocwen is headquartered in Atlanta, Georgia, with offices in West Palm Beach and Orlando, Florida, and Washington, DC, and support operations in India and Uruguay. Utilizing proprietary technology and world-class training and processes, we provide solutions that make our clients' loans worth more. Additional information is available at www.ocwen.com.