Citi Monitorship

Menu Item 2A

Eleventh Report
October 2019

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I. INTRODUCTION

This is the eleventh report of the Monitor pursuant to the July 11, 2014, agreement (the "Settlement Agreement") among Citigroup, Inc. ("Citi"), the U.S. Department of Justice ("DOJ"), and the states of California, New York, Illinois, and Delaware, and the Commonwealth of Massachusetts (collectively the "Settling States").

As the Monitor has explained in prior reports, Citi agreed as part of the Settlement Agreement to pay $4.5 billion to the DOJ and the States[1]; acknowledged a statement of facts attached to the Settlement Agreement; and committed to providing consumer relief valued at $2.5 billion under the principles set forth in Annex 2 of the Settlement Agreement.[2] Under the Settlement Agreement, Thomas J. Perrelli serves as an independent monitor (the "Monitor") to determine Citi's compliance with the consumer relief and corresponding requirements of Annex 2.

This report assesses the creditable relief provided by Citi under Menu Item 2A for the full term of the Monitorship.

[1] Settlement Agreement at 2 (July 11, 2014), *available at* http://www.citigroupmonitorship.com/settlement-agreement/.
[2] Settlement Agreement, Annex 2 (July 11, 2014) ("Annex 2"), *available at* http://www.citigroupmonitorship.com/wp-content/ uploads/2015/06/annex_2.pdf.

II. CONSUMER CREDIT RELIEF EARNED FOR MENU ITEM 2A

A. Introduction

In the Monitor's Third, Fourth, Fifth, and Seventh Reports, the Monitor credited Menu Item 2A transactions submitted by Citi for relief. For the reasons described below, Citi and the Monitor agreed to revise certain procedures and parameters for crediting the transactions Citi submitted for 2A credit in 2018. Under these revised procedures and parameters, Citi's Internal Review Group ("IRG") and the Monitor's consultant, Control Risks Group, L.L.C. ("Control Risks"), tested a statistically significant sample of these transactions to confirm their eligibility for credit. This Report credits and assesses those transactions.

B. History

Under Menu Item 2A, Citi receives credit for reducing a borrower's mortgage interest rate (and performing related transactions), "regardless of loan performance status," if such relief is offered at no cost—other than any tax consequences incurred as a result of the relief received—to the borrower.[3] As the Monitor has explained in prior reports, borrowers who are underwater on their mortgages may find refinancing difficult, because a new lender may not want to pay off a preexisting mortgage that is worth more than the value of the home.[4]

[3] *Id.* at 8 nn. 12-13.
[4] Citi Monitorship Third Report at 12-13 (Sept. 2015), *available at* http://www.citigroupmonitorship.com/wp-content/uploads/2015/09/Citigroup-Monitorship-Third-Report.pdf; Citi Monitorship Eighth Report, April 2018, at 6, *available at* http://www.citigroupmonitorship.com/wp-content/uploads/2018/04/CitigroupMonitor_8thReport_FINAL-3-red.pdf.

Rate reduction addresses this problem, while also affording relief to borrowers who were not underwater but had otherwise not benefited from historically low interest rates.

A transaction is eligible for credit under Menu Item 2A if it reduces the mortgage interest rate by more than 200 basis points.[5] Credit is calculated under Menu Item 2A using an 8- or 12-year factor, depending on whether the credit is sought for a loan in Citi's CMI or CFS portfolio.[6] Thus, for example, if a CMI borrower's interest rate before modification (the "pre-action interest rate") were 5.25 percent, and the borrower's interest rate after the modification (the "post-action interest rate") were 3 percent, Citi's credit would be determined, in part, by multiplying the 225 basis point reduction by 8 years—irrespective of whether the borrower stayed in the home for precisely 8 years or 20 years, or sold the home after 1 year.

During discussions regarding credit submissions under Menu Items 1A, 2A, and other menu items that the Monitor has previously described, the Monitor and Citi have addressed how modifications or refinancings that resulted in a "step rate" should be treated. Under a step rate, a borrower's interest rate begins low, but can increase (usually up to an annual or total cap) each year depending on prevailing market conditions. The federal government's Home Affordable Modification Program ("HAMP") and Citi's proprietary equivalent to HAMP allowed modifications resulting in a step rate, which were often beneficial to the borrower given the fixed or adjustable rate that the borrower might have had.

The Settlement Agreement authorized credit for HAMP modifications, but did not directly address the impact of step rates and, in particular, the possibility that some of the benefit that the consumer was getting from the consumer relief under the Settlement Agreement was being offset by a higher interest rate later in the loan. In the Citi Monitorship Tenth Report, the Monitor resolved treatment of such step rates under Menu Item 1A.[7] The issue also arose, however, for Menu Item 2A loans.

Menu Item 2A and its credit calculation had not factored in step rates. A loan could, for example, be refinanced to an initial rate more than 200 basis points below the pre-action rate, but could later increase to a rate higher than, or fewer than 200 basis points lower than, the loan's pre-action interest rate.[8] The issue would become even more complex if the borrower had an adjustable rate mortgage that would be modified to a step-rate; one could elect to compare the pre-action rate and the initial

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[5] Annex 2 at 8.
[6] *Id.* at 8 nn. 14-15.
[7] *See* Citi Monitorship Tenth Report at 5-6 (May 2019).
[8] *Id.* at 5.

post-action rate to assess adherence to the 200-basis point reduction requirement, or compare the possible interest rates at multiple other points during the projected history of the loan.

In addition to issues related to eligibility, there was the question of credit. The Settlement Agreement's approach to calculating credit presumed fixed interest rates. If Citi received credit based on the initial reduction, it would receive "too much" credit if the rate later stepped up, even if the step-up was capped such that a borrower's rate would never be above the 200-basis point reduction threshold.

The Monitor determined that Citi should receive no credit for any loan that could step up to a rate at any point during the loan that would have made it ineligible under the 200-basis point reduction requirement. With respect to a borrower whose interest rate was capped below the 200-basis point threshold, but could vary as a result of a step increase, credit needed to be modified consistent with the potential for the interest rate to increase. The Monitor's team worked with Citi to review all 2A loans, including those previously credited, to apply those rules.

Upon review of the loans previously submitted for 2A credit, Citi determined that over 99.9% of the submitted population were loans where the post-action interest rate was fixed—i.e., would not "step" to a higher interest rate at any point in the future. The Monitor's Team and Control Risks tested samples of previously credited Menu Item 2A relief from both CMI and CFS and ultimately agreed that the evidence was consistent with Citi's conclusion as to the legacy Menu Item 2A relief. And while six of the previously credited loans were not fixed, the reduction of their pre-action interest rates exceeded the minimum rate reduction required for 2A relief.

The new population of loans that Citi delivered for crediting under 2A in February 2018, however, included many loans that had been modified to step-rate interest rates. And for many of those loans, the maximum interest rate that the loan could step up to ("post-action lifetime maximum interest rate") was less than 200 basis points below the pre-action interest rate.[9]

To avoid a potentially substantial loss of credit from otherwise eligible relief, the Monitor recommended that Citi freeze the post-action interest rate for borrowers who were scheduled to experience interest rate step-ups in the near future under their modifications, and that Citi could submit for credit such relief transactions if Citi could prove that it prevented the step-up from occurring.

[9] The previously submitted and credited loans, and the loans delivered for crediting in February 2018, differed in this way because the previously submitted and credited loans were issued by CitiFinancial Servicing ("CFS"), which did not participate in HAMP or offer HAMP-like propriety modifications, while the latter loans were issued by CitiMortgage, Inc. ("CMI"), which participated in HAMP and offered HAMP-like proprietary modifications.

More specifically, the Monitor agreed that Citi could receive credit under Menu Item 2A for these step-rate loans only if they were converted to fixed-rate loans by (1) changing the interest rates on these loans from step rates to fixed rates in Citi's system of record; and (2) notifying the borrowers that the loan step rate would never go into effect, and that the loan's initial post-modification interest rate would be the loan's permanent rate. In other words, many borrowers who had received modifications from Citi that, among other things, converted their interest rates into step-rate interest rates will now receive the additional benefit that their interest rates will not step up over time to a higher rate.

These rules could not be applied to a small subset of step-rate loans submitted for Menu Item 2A credit, which had already been sold to another servicer. For these loans, the Monitor agreed that Citi could receive Menu Item 2A credit only if the loan's pre-action interest rate was more than 200 basis points greater than the post-action lifetime maximum interest rate on the loan. Moreover, for credit calculation purposes, the Monitor required that the amount of rate reduction for these loans be calculated as the difference between the pre-action interest rate and the post-action lifetime maximum interest rate. These conditions aimed to ensure that the interest rate was truly reduced by more than 200 basis points for the life of the loan—thus giving the borrower the full benefit of the rate reduction—and that the credit calculation reflected the actual benefit to the borrower, as defined by the Settlement.

Citi and the Monitor implemented these rules in a revised testing procedure. Citi determined that the most efficient way to implement the revised testing procedures was (1) to certify that all of the previously submitted and credited Menu Item 2A loans were fixed for life, and (2) to withdraw the Menu Item 2A loans that it had submitted in February 2018 for crediting, and to resubmit these loans for testing by the IRG and Control Risks using revised testing procedures that accounted for the three conditions discussed above. This Report describes the testing process and credits Citi for Menu Item 2A loans under the revised testing procedure.

C. Testing

1. IRG Satisfaction Review

As with previous submissions, Citi performed the consumer relief activities for which it seeks credit and submitted them to its IRG. The IRG is a group of Citi employees and vendors; the group is required to be fully independent of Citi's mortgage loan servicing operations.

The IRG tested and confirmed the eligibility of Citi's consumer relief activities and the amount of credited relief under Menu Item 2A through review of a statistically valid sample of the loans submitted for credit ("Satisfaction Review"). This Satisfaction Review was guided by the "Testing Definitions" approved by the Monitor, as previously discussed in the Monitor's First Report.[10] The Testing Definitions applied by the IRG were updated for this Satisfaction Review to reflect the revised rules governing interest rates.

Specifically, the IRG tested a random, statistically valid sample of all of the Menu Item 2A transactions that Citi indicated received consumer relief during the duration of the Monitorship. The IRG used 99% confidence level testing for the possibility that the credit was overstated, and used a 2.5% estimated error rate in the population with a 2% margin of error. The IRG reviewed each sampled transaction to determine whether the transaction was eligible for credit and, if so, whether the amount of credit claimed by Citi was calculated correctly. The IRG tested the sample transactions pursuant to the Testing Definitions and related IRG Test Plan for Menu Item 2A, as revised to reflect the rules regarding interest rates. The IRG saved in its work papers screenshots from Citi's System of Records ("SOR") evidencing the relevant data.

The IRG submitted a testing certification to the Monitor on February 5, 2019.

2. The Monitor's Review

The Monitor has retained Control Risks to assist in testing and verifying Citi's submissions to the Monitor.

At the Monitor's direction, Control Risks analyzed the IRG's Satisfaction Review of Menu Item 2A using an internal form it created following the processes and procedures set out in the Testing Definitions and IRG Test Plans. Control Risks was given

[10] Citi Monitorship First Report at 12 (Jan. 2015), *available at* http://www.citigroupmonitorship.com/wp-content/uploads/2015/06/citi_monitorship_initial_report_2015-01-21.pdf.

remote access to Citi's secure FileNet platform to view loan-level SOR screenshots captured and saved by the IRG in the course of performing its Satisfaction Review. For each transaction tested, the IRG provided the data elements and evidence necessary for Control Risks to validate credits in accordance with the Settlement Agreement and the applicable Testing Definitions. The IRG cooperated in full with Control Risks.

Control Risks employees served as the testers of the transactions. Control Risks trained its testers by reviewing sample packages for loans and addressing any questions or issues that arose through that process. For each loan in the sample, Control Risks reviewed the evidence package provided by the IRG to confirm that each eligibility requirement was satisfied. Control Risks also completed an internal quality control review of its analysis.

D. Overview of Relief Provided under Menu Item 2A

Under Menu Item 2A, if a borrower receives a mortgage interest rate reduction of more than 200 basis points, Citi receives credit based on a formula that seeks to estimate the amount of future interest payments forgone.[11] If the rate is reduced by 400 basis points or more, Citi receives an additional 25% in credit.[12]

As the Monitor has previously explained, Citi also can provide relief creditable under Menu Item 2A by facilitating refinancing through a third party that reduces the borrower's current interest rate with Citi.[13] For such relief, Citi can receive dollar-for-dollar credit by paying the refinancing and related costs for the borrower, and by facilitating the refinancing through forgiveness of part of the borrower's loan balance, in addition to credit for reducing the borrower's interest rate.[14]

Lastly, where it facilitates a refinancing by forgiving the borrower's loan balance, Citi receives an incentive bonus of 15% added credit for reducing borrowers' loan-to-value ("LTV") ratio below 100%,[15] which means that the new, lower amount owed on the loan is less than the value of the home. Citi also receives an incentive bonus of 15% added credit for Menu Item 2A relief provided before October 1, 2015.[16] Citi received that incentive bonus for relief provided before October 1, 2015, even when loans were not submitted to the Monitor for credit until after that date, because the actual relief was provided to borrowers before the October 1, 2015 bonus cut-off.

[11] Annex 2 at 8.
[12] *Id.*
[13] Citi Monitorship Third Report at 6-7, 13.
[14] Annex 2 at 8.
[15] Citi receives 115% credit for incremental LTV reductions below 100%. *Id.*
[16] Citi receives 115% credit for all consumer relief activity offered or completed by October 1, 2015. *Id.* at 2 n.2.

On February 5, 2019, Citi submitted a claim to the Monitor for crediting consumer relief under Menu Item 2A for the time period of February 1, 2018, through February 1, 2019. As discussed in greater detail below, the Monitor has determined that Citi earned consumer relief credit for this period in the amount of $106,867,113.11. This credit is for the following consumer relief:

- Citi earned $106,332,704 in credit through both proprietary and third-party rate reductions.

- Citi earned $534,409 in credit for facilitating refinancing through a third party, 1st Alliance Lending, by either reducing costs and/or forgiving principal.

- This relief comprised modifications of 3,191 loans,[17] including 3,163 modifications for Citi-proprietary reductions.

- For both Citi-proprietary and third-party rate reductions, interest rates were reduced by an average of 5.77 percentage points after loan modification. The average post-modification interest rate for loans that received Menu Item 2A Citi-proprietary reductions is 2.13%, and the median post-modification interest rate for such loans is 2%. The corresponding post-modification interest rates for third-party rate reduction relief are 5.22% and 5%, respectively.

- 858 of the submitted loan modifications reduced the borrower's mortgage interest rate by more than 200 basis points, but less than 400 basis points. These claims were eligible for credit for rate reductions between 200 and 400 basis points.

- 2,333 of the submitted loan modifications reduced the borrower's mortgage interest rate by at least 400 basis points. These claims were eligible for an additional 25% in credit for rate reductions.[18]

- Citi earned $8,387,367.58 in incentive credit for 1,903 loan modifications under Menu Item 2A. Of that total, $8,384,870.98 was early incentive credit (which applied to 1,903 loan modifications) and $2,496.60 was credit for incremental LTV reductions below 100% (which applied to all 10 loan modifications Citi submitted for balance forgiveness credit under Menu Item 2A).

The Monitor has confirmed the eligibility of Citi's modifications and a total of $106,867,113.11 in credit under Menu Item 2A.

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[17] For one of these loans, Citi is seeking credit only for paying the costs to facilitate a refinance through 1st Alliance Lending and is not seeking credit for the rate reduction related to that refinance.
[18] The 2,333 loan modifications figure includes the modification of the one loan referenced in the preceding footnote, for which Citi did not seek rate reduction credit.

E. General Characteristics of Relief Provided

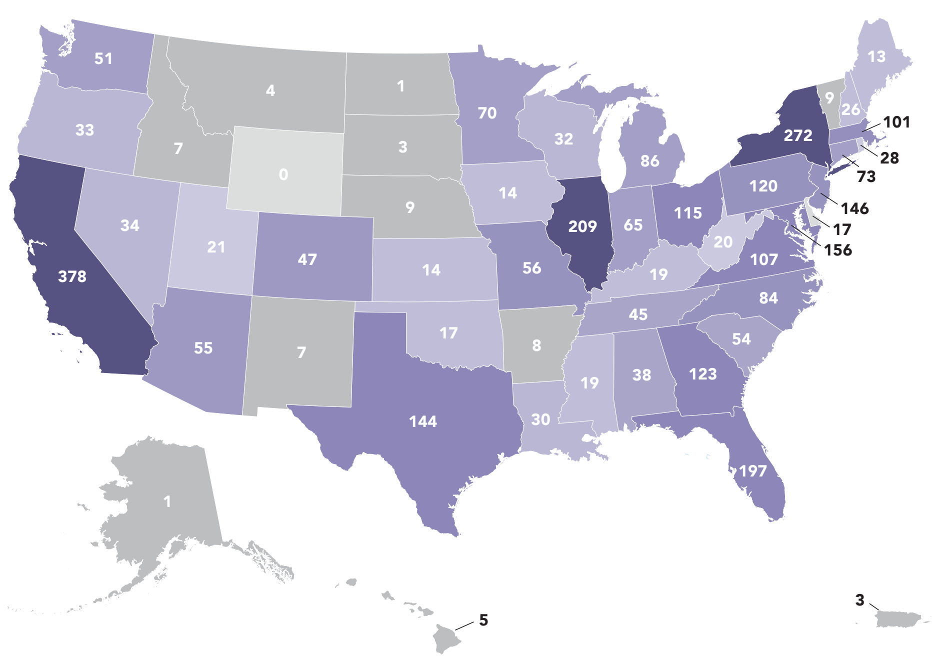
The Monitor makes the following observations about the relief provided under Menu Item 2A:

- **Geographic Distribution:** Citi provided Menu Item 2A relief in 49 states, Puerto Rico and the District of Columbia, including the Settling States of California, Delaware, Illinois, Massachusetts, and New York. California had the most borrowers receiving Menu Item 2A relief (with 378 modifications), followed by New York (272), Illinois (209), Florida (197), and Maryland (156).

  Table 1 sets forth the amount of Menu Item 2A credit that Citi earned in Settling States:

Settling States	Number of Claims	Total Credit
California	378	$15,253,894.30
Delaware	17	$590,580.04
Illinois	209	$5,702,668.90
Massachusetts	101	$3,409,446.17
New York	272	$12,434,415.55
Total	**977**	**$37,391,004.96**

  Map 1, below, shows the number of modifications in each state:



- **Interest Rate Reductions:** On average, borrowers who received a creditable rate reduction from Citi had their monthly mortgage payments decreased by $326.84. Monthly mortgage payments were reduced, on average, by 49.58%.

  The average pre-modification interest rate for borrowers receiving rate reductions was 7.93%, with the pre-modification interest rates ranging from 2.75% to 15.12%. The average post-modification interest rate was 2.16%, with the post-modification interest rates ranging from 0% to 12.53%.

  The number of modifications that had a post-modification lifetime maximum interest rate that was greater than the post-modification interest rate was 1,360. For those 1,360 loans, the post-modification lifetime maximum interest rate ranged from 0.11 to 8 percentage points greater than the post-modification interest rate.

  Citi submitted 3,224 claims for credit under Menu Item 2A. These claims included the following:

Type of Credit	Number of Claims	Total Credit	Average Pre-Action Interest Rate	Median Pre-Action Interest Rate	Average Post-Action Interest Rate	Median Post-Action Interest Rate
Citi loan rate reduction	3,163	$104,623,317	7.91%	7.90%	2.13%	2.00%
Citi-facilitated creditable rate reduction with 1st Alliance Lending (i.e., 200 or more bps)	27	$1,709,388	9.95%	10.11%	5.22%	5.00%

Type of Credit	Number of Claims	Total Credit	Average Amount Paid or Forgiven by Citi per Borrower	Median Amount Paid or Forgiven by Citi per Borrower
Other Costs Paid	24	$250,804	$9,087	$7,920
Balance Forgiveness	10	$283,605	$24,412	$24,207

F. Citi's Earned Credit To Date

Menu Item	Total Credit Earned
Menu Item 1A	$27,531,179
Menu Item 1G	$31,172,235
Menu Item 1H Secured	$36,586,150
Menu Item 1H Unsecured	$274,000,933
Menu Item 2A	$478,171,314
Menu Item 4A	$275,955,575
Menu Item 4D	$57,500,000
Menu Item 4E	$34,500,000
Menu Item 4F	$23,000,000
Menu Item 5	$759,704,640
Total	**$1,998,122,026**