I. Rep. Jeb Hensarling

A. Introduction

The topic of the March report of the Congressional Oversight Panel (COP) is an investigation of foreclosure mitigation efforts. This topic is not only timely given the recent TARP initiatives announced by the Obama Administration, but it is also one of the several areas explicitly mentioned in the Emergency Economic Stabilization Act of 2008,Pub..L. No. 110-343, which states that the regular reports of the COP shall include the "effectiveness of foreclosure mitigation efforts." To that end, I believe that this month's report is an appropriate exercise and I welcome this opportunity to review what is being done to help address the large number of foreclosures that far too many borrowers are currently facing.

There is no question that we are witnessing an explosion in the number of foreclosures in our economy. According to a January report by RealtyTrac, an online foreclosure listing firm, more than 2.3 million properties were subject to foreclosure filings in 2008, an increase of more than 80 percent from 2007 levels.[1] Separately, the Mortgage Bankers Association's (MBA) National Delinquency Survey for the third quarter of 2008 found that the percentage of loans in the process of foreclosure — 2.97 percent — set a new record, and the seasonally-adjusted total delinquency rate — 6.99 percent — was the highest recorded in the history of the MBA survey.[2] For the millions of people facing foreclosure and the untold number of others who might be on the brink of housing trouble, the economic hardship and worry associated with potentially losing one's home are real, tangible, and pressing problems worthy of attention.

Any investigation into the effectiveness of foreclosure mitigation efforts should start by identifying all the factors that contributed to its cause, the borrowers who are directly affected, the relative costs and benefits of government-subsidized foreclosure mitigation efforts, and the possible policy alternatives that could help provide relief to borrowers in a fair, responsible, and taxpayer-friendly way. The answers to these questions will, I believe, help steer policymakers in the correct direction and provide help to those deserving of it, while preventing less deserving actors from benefitting from their own mistakes and ultimately preventing more taxpayer dollars from going to waste.

B. Contributing Causes

Before we can address the foreclosure problem, we must first understand its cause. In his remarks to a joint session of Congress on February 24, President Obama stated, "it is only by

[1] RealtyTrac, *Foreclosure Activity Increases 81 Percent in 2008* (Jan. 15, 2009) (online at www.realtytrac.com/ContentManagement/pressrelease.aspx?ChannelID=9&ItemID=5681&accnt=64847).

[2] Mortgage Bankers Association, *Delinquencies Increase, Foreclosure Starts Flat in Latest MBA National Delinquency Survey* (Dec. 5, 2008).

understanding how we arrived at this moment that we'll be able to lift ourselves out of this predicament."[3] To that end, I could not agree with the President more.

One of the primary causes of the difficulties that some borrowers are facing has been the general federal objective of enabling and encouraging people to buy homes that were too expensive for them to otherwise afford. In a perfect world, the laws of supply and demand would be the fundamental driver of our mortgage markets, with qualified borrowers having reliable access to suitable mortgage products that best fit their needs. Yet, in reality, the cost of homeownership has in many places so thoroughly outpaced the ability of borrowers to afford a home that the government has chosen to intervene with various initiatives to defray parts of the cost of a mortgage. That intervention has taken many forms — affordable housing programs, federal FHA mortgage insurance, tax credits and deductions, interest rate policies, etc. — as part of a concerted effort to increase homeownership. For almost a decade, those efforts succeeded, pushing homeownership rates steadily up from 1994 through their all-time high in 2004. That increase in demand, in turn, contributed to a corresponding increase in home prices, which rose from the mid-1990s until hitting their peak in 2006. Yet those price increases created a cycle of government intervention — home price appreciation made homes less affordable, which in turn spurred further government efforts to defray more of their cost — and the involvement of the federal government in our housing markets only grew deeper.

Increased government involvement in our housing markets created significant distortions and disruptions. This increased involvement is contrary to the oft-repeated, now disproven claims of proponents of expanded government control of our economy that a "wave" of market deregulation over the last 20 years caused the current crisis. To the contrary, facts indicate that there were at least five key factors which contributed to our situation, at least four of which were a direct result of government involvement. Those four factors — highly accommodative monetary policy by the Federal Reserve, continual federal policies designed to expand home ownership, the congressionally-granted duopoly status of housing GSEs Fannie Mae and Freddie Mac, and an anti-competitive government-sanctioned credit rating oligopoly — are thoroughly discussed in the *Joint Dissenting Views* to the COP's "Special Report On Regulatory Reform" that I offered along with Senator John Sununu .along with a fifth factor (failures throughout the mortgage securitization process that resulted in the abandonment of sound underwriting practices).[4] As such, a thorough recitation of those points here would be redundant. However, a brief review of what I believe to be the two most relevant factors to the foreclosure debate — federal policies designed to expand home ownership and the market manipulations of Fannie and Freddie — may be instructive.

For well over twenty years, federal policy has promoted lending and borrowing to expand homeownership, through incentives such as the home mortgage interest tax exclusion, the Federal Housing Administration (FHA), discretionary HUD spending programs, and the infamous Community Reinvestment Act (CRA). CRA is a federal program created to encourage

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[3] The White House, *Remarks of President Barack Obama -- Address to Joint Session of Congress* (Feb. 24, 2009) (online at http://www.whitehouse.gov/the_press_office/Remarks-of-President-Barack-Obama-Address-to-Joint-Session-of-Congress).

[4] Congressional Oversight Panel, *Special Report on Regulatory Reform: Modernizing the American Financial Regulatory System: Recommendations for Improving Oversight, Protecting Consumers, and Ensuring Stability*, at 54-89 (Jan. 29, 2009).

banks to extend credit to "underserved" populations by requiring that banks insured by the federal government "help meet the credit needs of its entire community." As noted in the *Joint Dissenting Views*, CRA has led to an increase in bank lending to low- and moderate-income families by 80 percent. However, to make these loans, banks were encouraged to relax their traditional underwriting practices to achieve and maintain compliance. Those reduced standards led to a surge in non-traditional loan products, particularly adjustable rate subprime and Alt-A loans, which are now largely seen to be risky products. Thus, mandates like CRA ended up becoming a significant contributor to the number of foreclosures that are occurring because they required lending institutions to abandon their traditional underwriting standards in favor of more subjective models to meet their government-mandated CRA obligations.

Perhaps even more important than the impact of federal policy mandates were the unparalleled market distortions of Fannie Mae and Freddie Mac, the two now-failed, trillion-dollar housing GSEs. Fannie and Freddie exploited their congressionally-granted charters to borrow money at discounted rates. They dominated the entire secondary mortgage market, wildly inflated their balance sheets and personally enriched their executives. Because market participants long understood that this government created duopoly was implicitly (and, now, explicitly) backed by the federal government, investors and underwriters chose to believe that if Fannie or Freddie touched something, it was safe, sound, secure, and most importantly "sanctioned" by the government. The results of those misperceptions have had a devastating impact on our entire economy.

Given Fannie and Freddie's market dominance, it should come as little surprise that once they dipped into the subprime and Alt-A markets, lenders quickly followed suit. In 1995, HUD authorized Fannie and Freddie to purchase subprime securities that included loans to low-income borrowers and allowed the GSEs to receive credit for those loans toward their mandatory affordable housing goals. Fannie and Freddie readily complied, and as a result, subprime and near-prime loans jumped from 9 percent of securitized mortgages in 2001 to 40 percent in 2006. In 2004 alone, Fannie and Freddie purchased $175 billion in subprime mortgage securities, which accounted for 44 percent of the market that year. Then, from 2005 through 2007, the two GSEs purchased approximately $1 trillion in subprime and Alt-A loans, and Fannie's acquisitions of mortgages with less than 10-percent down payments almost tripled. As a result, the market share of conventional mortgages dropped from 78.8 percent in 2003 to 50.1 percent by 2007 with a corresponding increase in subprime and Alt-A loans from 10.1 percent to 32.7 percent over the same period. These non-traditional loan products, on which Fannie and Freddie so heavily gambled as their congressional supporters encouraged them to "roll the dice a little bit more," now constitute many of the same non-performing loans which have contributed to our current foreclosure troubles.

C. Necessary Considerations in Evaluating Foreclosure Mitigation Plans

In evaluating the effectiveness of a government-subsidized foreclosure mitigation plan, there are several fundamental questions that must be asked. Perhaps the most salient questions are determining who you want to help, why you want to limit help to them, and who you might hurt by doing so. Those considerations are closely linked to questions of the inherent fairness and moral hazard of any government-subsidized foreclosure mitigation plan. For example, it is a fact even admitted by the majority report that some loan modifications are simply not economical and thus some foreclosures are inevitable. Even in the best of times, the MBA's National Delinquency Survey shows that between 4-5 percent of loans become delinquent and 1 percent go into foreclosure.[5] Those unpaid loans likely stem from many reasons including the uncomfortable truth that some people, try as the might, are simply not ready for the responsibility of homeownership. It follows that efforts to keep such individuals in their homes will be a costly losing battle, diverting time, attention, and critical resources away from those who might otherwise be worthy candidates for help. On the other end of the spectrum, policymakers need to determine where to draw the line to stop offering assistance to those who do not actually need it because they have other means at their disposal or the option to resolve their own difficulties without the expenditure of taxpayer funds.

In between the extremes of those who cannot be saved and those who should not be recipients of government-subsidized foreclosure mitigation assistance is a considerably diverse group of borrowers who might be technically eligible for a program but might have made decisions or behaved in ways that would call into question the desirability of expending taxpayer dollars to assist them. While a more thorough discussion of which specific undesirable decisions might merit exclusion is included below, one general characteristic worth considering involves the ability to pay. Without a doubt, in any loan mitigation program there will be some otherwise eligible borrowers who *can* pay their mortgages but who *choose* not to pay them or not to make the difficult decisions to sacrifice on other things because they want to get relief. Sorting this group of unwilling payers out from those who are unable to pay is a fundamental concern that <u>must</u> be addressed in every foreclosure mitigation plan. Unfortunately, this concern has been nearly universally omitted from previous government proposals on the subject. Until that concern is resolved, it is my great fear that we will continue to provide a tremendous incentive for borrowers on the bubble to opt not to fix (or, even worse, purposefully exacerbate) their own problems in hopes of gaining government assistance at a time when we ought to enact incentives to encourage the opposite behavior.

A closely related concern to who will receive assistance is the question of how much will that assistance cost. This fundamental concern is excluded from the majority's report. So far, over the last 16 months, the federal government has pledged more than $9 trillion to address our economy's credit crisis between new initiatives undertaken by the Federal Reserve, the Treasury Department, the FDIC, and HUD.[6] Those commitments come on top of our existing $10.9 trillion national debt[7] and an estimated 2009 budget deficit of $1.8 trillion.[8] Given the unprecedented economic challenges we are now facing, the American people have an absolute right to be suspicious of the cost of developing new government-subsidized foreclosure mitigation programs. Those that dismiss such concerns as narrow-minded display how

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[5] Mortgage Bankers Association, *Delinquencies Increase, Foreclosure Starts Flat in Latest MBA National Delinquency Survey* (Dec. 5, 2008).

[6] Mark Pittman and Bob Ivry, *U.S. Taxpayers Risk $9.7 Trillion on Bailout Programs*, Bloomberg (Feb. 9, 2009) (online at news.yahoo.com/s/bloomberg/20090209/pl_bloomberg/agq2b3xegkok).

[7] TreasuryDirect, *The Debt to the Penny and Who Holds It* (online at www.treasurydirect.gov/NP/BPDLogin?application=np) (accessed Mar. 5, 2009).

[8] Republican Caucus, House Committee on the Budget, *The President's Budget for Fiscal Year 2010: the Good, the Bad, and the Ugly* (Feb. 27, 2009) (online at http://www.house.gov/budget_republicans/press/2007/pr20090227potus.pdf).

disconnected they are from the undeniable hypocrisy of asking hardworking Americans to do more with less while their government continues to run up massive debts that it will not be able to repay without substantial tax increases.

The question of cost is also significant because it helps further define the universe of deserving people to whom assistance could be directed. It should be clear that with an unlimited supply of money, you could prevent any foreclosure for every borrower if you did not care about their worthiness. But, given a limited amount of resources, it becomes critical that you focus your attention on those who are actual priorities and limit those who are less deserving. Budget concerns also raise another question: how much assistance is appropriate to commit to any one borrower? Clearly, with finite resources, the more money you use to help those with large financial needs, the fewer total number of people you can help. For example, the original Hope for Homeowners law limited the size of eligible single-family loans to no more than 132 percent of the 2007 conforming loan limits for Freddie Mac, or roughly $550,000 for most places. According to the U.S. Census Bureau, that amount was well more than double the median national purchase price of $234,991 for a newly constructed home built in the last four years.[9] Accordingly, all things being equal, you would be able to provide the same proportional amount of assistance to more than two borrowers at the median price for every one borrower at the upper limit. Thus, if the goal of a program is to help the maximum number of people possible, then it makes sense to target assistance towards people on the lower end of the income/loan scale; if the goal of a program is to provide the most robust assistance to borrowers, then the reverse would be true.

A further necessary consideration of the effectiveness of government-subsidized foreclosure mitigation plans is how successful they will be in keeping assisted borrowers out of future foreclosure difficulty. Unfortunately, there is strong evidence to suggest that despite recent loan modification efforts at various levels, a significant number of modified borrowers end up back in default anyway, often very quickly. A December 2008 joint report by the Office of the Comptroller of the Currency (OCC) and the Office of Thrift Supervision (OTS) on the state of first lien residential mortgages serviced by national banks and federally regulated thrifts found that loan modifications were "associated with high levels of re-default." The report found that for "loans modified in the first quarter of 2008, more than 37 percent of modified loans were 30 or more days delinquent or in the process of foreclosure after three months [and a]fter six months, that re-default rate was more than 55 percent."[10] For loans modified in second quarter of 2008, the number of 30 or more days delinquent modified loans was even higher, coming in at 40.52 percent.[11] Such results seem to indicate that many of the current recipients of loan modification assistance might either fall into the category of those who have loans that are not economical to modify or those who are simply not ready for the responsibility of homeownership.

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[9] U.S. Census Bureau, *American Housing Survey National Tables: 2007* (2007) (Table 3-14: Value, Purchase Price, and Source of Down Payment--Owner-Occupied Units) (online at http://www.census.gov/hhes/www/housing/ahs/ahs07/tab3-14.pdf).

[10] Comptroller of the Currency and Office of Thrift Supervision, *OCC and OTS Mortgage Metrics Report: Disclosure of National Bank and Federal Thrift Mortgage Loan Data* (Dec. 2008) (online at files.ots.treas.gov/482028.pdf).

[11] *Id.*

D. Universe of People

As mentioned earlier, there is little doubt that the sheer number of foreclosures we are experiencing is unprecedented in modern times. Caught up in this wave of foreclosures are certainly people who, through little fault of their own actions, now find themselves in distress. These are the borrowers who have suffered what industry professionals refer to as "life events," such as the involuntary loss of a job, the onset of an illness or disability, a divorce, or had some other unexpected hardship that has materially changed their living/earning circumstance. For those individuals, the commitment required for homeownership has shifted from a manageable responsibility to a crushing burden from which they may be powerless to resolve without third-party assistance.

These "life event" affected borrowers are noteworthy because relatively few object to efforts to find achievable solutions for trying to help keep these distressed borrowers in their current residences whenever possible. Similarly, another sympathetic group of distressed borrowers involves people who were legitimate victims of blatant manipulation or outright fraud by unscrupulous lenders who pressured them into homes they could not afford. To many, those legitimate victims are certainly equally deserving of assistance. Of course, such borrowers do have the added burden proving that they were indeed victims of actual wrongdoing. However, they also have a potential remedy of pursuing legal action against fraudulent lenders, an option which is not available to others.

If the universe of individuals in mortgage distress included only borrowers from "life event" and fraud victims groups, the task of crafting an acceptable government-subsidized foreclosure mitigation plan would be much easier. However, the number of individuals in mortgage distress stretches far beyond those groups to include a much larger section of people who, for a wide variety of reasons, are no longer paying their mortgage on time. While certainly not an exhaustive list, that larger group includes:

- people who took out large loans to purchase more house than they could have reasonably expected to afford;
- borrowers who lied about their income, occupancy, or committed other instances of mortgage fraud;
- speculators who purchased multiple houses for their expected value appreciation rather than a place to live;
- individuals who decided to select an exotic mortgage loan with fewer upfront costs, lower monthly payments, or reduced documentation requirements;
- borrowers who took advantage of refinance loans to strip much or all of the equity out of their house to finance other purchases;
- those who simply made bad choices by incorrectly gambling on the market or overestimating their readiness for homeownership; and
- borrowers who have made a rational economic decision and, given their particular circumstance, it no longer makes sense to them to continue paying their mortgage.

Borrowers who fall into those categories are much less sympathetic in the eyes of many, and attempting to develop a government-subsidized foreclosure mitigation plan to assist them will inevitably raise significant moral hazard questions for policymakers.

A fundamental measure of the effectiveness of a foreclosure mitigation program is what steps the program has taken to sort those risky borrowers out from their more deserving counterparts to avoid the moral hazard of rewarding people for their bad behavior. Although that risky group might be difficult to quantify, there has been ample anecdotal evidence in the media highlighting the types of risky borrowers who should not be treated in the same way as other, responsible borrowers. For example, a 2006 USA Today story reported on a 24-year-old former website designer in California who bought eight homes in four states with no money down in seven of the eight deals, and then quickly went broke.[12] The Wall Street Journal, in 2007, published an article telling the story of a Detroit woman who refinanced her mortgage with an adjustable rate subprime loan but soon fell into delinquency after she used the proceeds of the new loan to settle old department-store bills, subsidize out-of-work relatives, and pay off some of her back property taxes.[13] A 2008 Bloomberg article featured a 28-year old self-employed Californian cabinetmaker who took out a mortgage loan with monthly payments of $6,900, and then almost instantly fell behind when his business revenue declined.[14]

There have also been several stories of the rich and famous falling behind on their mortgages, including former Major League Baseball player Jose Canseco,[15] former NBA player Latrell Sprewell,[16] pop singers Whitney Houston[17] and Michael Jackson,[18] and even an elected Member of Congress.[19] Although the financial details of each situation may be unique, the fact remains that all of those borrowers probably earned far more than the $50,000 that the Census Bureau has determined was the median annual income for households in 2007.[20] Additionally, according to a 2008 report by the MBA, at least 18 percent of loans in foreclosure in 2007 were

[12] Noelle Knox, *10 Mistakes That Made Flipping a Flop*, USA Today (Oct. 22, 2006) (online at www.usatoday.com/money/economy/housing/2006-10-22-young-flipper-usat_x.htm).

[13] Mark Whitehouse, *'Subprime' Aftermath: Losing the Family Home*, Wall Street Journal (May 30, 2007) (online at online.wsj.com/article/SB118047548069017647.html).

[14] Kambiz Foroohar, *Vulture Fund Deals With Delinquent Homeowners Lost by Subprime*, Bloomberg (Feb. 28, 2009) (online at www.bloomberg.com/apps/news?pid=20601109&sid=aaKT9Z_X9okg&refer=home).

[15] *Jose Canseco: Former Slugger's Home Foreclosed*, Associated Press (May 5, 2008) (online at archives.chicagotribune.com/2008/may/05/sports/chi-jose-canseco-080505-ht).

[16] *Federal Marshal Seizes Sprewell's Yacht*, Associated Press (Aug. 22, 2007) (online at http://www.usatoday.com/sports/basketball/2007-08-22-sprewell-yacht_N.htm).

[17] *Houston, We Have A Problem: Whitney's Foreclosure*, Associated Press (Nov. 15, 2006) (online at cbs2.com/local/Whitney.Houston.Mortgage.2.524392.html).

[18] Alex Veiga, *Records: Michael Jackson Late on Payments for Family Home*, Associated Press (Feb. 28, 2008) (online at www.usatoday.com/life/people/2008-02-28-jackson-home_N.htm?csp=34).

[19] *Report: Congresswoman's Homes Defaulted 6 Times*, Associated Press (May 31, 2008) (online at cbs2.com/politics/Laura.Richardson.Default.2.737694.html).

[20] U.S. Census Bureau, *Household Income Rises, Poverty Rate Unchanged, Number of Uninsured Down* (Aug. 26, 2008) (online at www.census.gov/Press-Release/www/releases/archives/income_wealth/012528.html).

for non-owner occupied homes.[21] Separately, the National Association of Realtors in 2008 found that known second home sales accounted for 33 percent of all existing- and new-home sales in the previous year, a figure which was close to historic norms.[22] While the individual needs of the rich and famous and those who own multiple homes might be great, surely this collection of borrowers is not the universe of people on whom we ought to spend limited taxpayer dollars to extend government-subsidized foreclosure mitigation efforts.

Beyond those who made unwise borrowing decisions, attention must be paid to excluding individual borrowers who committed outright fraud in obtaining their mortgages. Many of these loans likely fall into the no-doc/low-doc category of Alt-A loans where borrowers were not required to provide real verification of their income to lenders. According to a February 2009 by the Department of the Treasury's Financial Crimes Enforcement Network (FinCEN), reports of mortgage fraud have increased more than 1,600 percent from 2000 to 2008, and almost doubled since June 2006.[23] Despite heightened concerns and a depressed real estate market, the report found that the total number of suspected mortgage fraud reports filed in 2008 was 62,084, a 44 percent increase over 2007. FinCEN also reports that mortgage loan fraud remained the third most prevalent type of suspicious activity reported in 2008. Given the tremendous potential for fraud, it should be readily apparent to all that preventing taxpayer money from being used to aid these criminal borrowers must be a priority for any government-subsidized foreclosure mitigation plan.

Distinct from a moral hazard question, in any consideration of the effectiveness of a taxpayer-funded foreclosure mitigation program, there is an inherent question of fairness as those who are not facing mortgage trouble are asked to subsidize those who are facing trouble. After all, why should a person be forced to pay for their neighbor's mortgages when he or she is struggling to pay his or her own mortgages and other bills? To many people, this question is the most important aspect of the public policy debate. On this point, despite the persistent externality admonitions of some economists, it is difficult to dismiss the concerns of those members of the ultimate "no fault of their own" demographic.

The evidence supporting the potential unfairness of current government-subsidized efforts is compelling. According to recent Census Bureau statistics, in 2007 there were roughly 110,692,000 occupied housing units in the United States.[24] Of those units, approximately 35,045,000 were occupied by people who were renters.[25] The remaining 75,647,000 housing units were occupied by people who were to some degree homeowners, both those with active

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[21] Jay Brinkmann, Mortgage Bankers Association, *An Examination Of Mortgage Foreclosures, Modifications, Repayment Plans and Other Loss Mitigation Activities in the Third Quarter of 2007* (Jan. 2008) (online at www.mortgagebankers.org/files/News/InternalResource/59454_LoanModificationsSurvey.pdf)

[22] National Association of Realtors, *Second-Home Sales Accounted for One-Third of Transactions in 2007* (Mar. 28, 2008) (online at www.realtor.org/press_room/news_releases/2008/03/second_home_sales_one_third_of_2007_transactions).

[23] Financial Crimes Enforcement Network, *supra* note 45; Financial Crimes Enforcement Network, *Mortgage Loan Fraud: An Update of Trends Based Upon an Analysis of Suspicious Activity Reports* (Apr. 2008) (online at www.fincen.gov/news_room/rp/files/MortgageLoanFraudSARAssessment.pdf).

[24] U.S. Census Bureau, *American Housing Survey National Tables: 2007* (2007) (Table 2-1: Introductory Characteristics--Occupied Units) (online at www.census.gov/hhes/www/housing/ahs/ahs07/tab2-1.pdf).

[25] *Id.*

mortgages and those who owned their homes outright with no mortgage. The latter group, those with no mortgage, totaled approximately 24,885,000.[26] Thus, the aggregate total of those who either rent their housing or own their homes outright is roughly 59,930,000 people, or more than 54 percent of the entire occupied housing unit market. That majority group, by definition, cannot be late on a mortgage payment, yet as taxpayers they are being asked to subsidize, at least in part, the mortgages of some of the minority 46 percent of the population that has an active mortgage.

The numbers become even more pronounced when you factor in which people from the active mortgage group are actually currently in delinquency. According to the MBA's National Delinquency Survey for the third quarter of 2008, which includes data on more than 85 percent of the active mortgages on the market, the non-seasonally adjusted total of loans beyond 30-days past due was percent 7.29, and the percent of loans in foreclosure was 2.97, for a combined total of 10.26 percent of loans not being paid on time.[27] Assuming that rate was consistent for all of the 50,762,000 active mortgages projected by the Census Bureau's statistics, that would mean that there were some 5,208,000 loans which were currently not being paid on-time versus 45,554,000 loans which are being paid on-time. Adding together the number of mortgages being paid on-time with the total of those who rent or own their homes outright, you get a total of 105,484,000 housing units that are not delinquent on a mortgage, or 95.3 percent of the 110,692,000 occupied housing units in the United States.

In light of these statistics, an essential public policy question that must be asked regarding the effectiveness of any taxpayer-subsidized foreclosure mitigation program is "*Is it fair to expect 19 out of every 20 people to pay more in taxes to help the 20th person maintain their current residence?*" Although that question is subject to individual interpretation, there is an ever-increasing body of popular sentiment that such a trade-off is indeed not fair. Given the massive direct taxpayer costs that have already been incurred through TARP and the potential costs that could be incurred through the assorted credit facilities and monetary policy actions of the Federal Reserve, I believe that it is difficult to justify asking those 19 out of 20 Americans to shoulder an even greater financial burden on yet another government foreclosure mitigation program that might not work.

Moreover, while the effect of the underlying credit crisis has been nationwide, statistics show that the bulk of the foreclosure wave has been concentrated in a few places where, admittedly, the problem is robust. According to the aforementioned January RealtyTrac report, nearly half (47.4 percent) of the 2.3 million properties with foreclosure filings in 2008 were concentrated in exactly four states: Nevada, Florida, Arizona, and California.[28] In fact, 15 of the top 16 and 18 of the top 22 metropolitan areas with the highest foreclosure rates were located in those four states. If you add to those four states the states with the five next highest foreclosure rates — Colorado, Michigan, Ohio, Georgia, and Illinois — the top nine foreclosure rate states contain more than two-thirds (66.9 percent) of all the properties with foreclosure filings in the

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[26] U.S. Census Bureau, *American Housing Survey National Tables: 2007* (2007) (Table 3-15: Mortgage Characteristics--Owner-Occupied Units) (online at www.census.gov/hhes/www/housing/ahs/ahs07/tab3-15.pdf).

[27] Mortgage Bankers Association, *Delinquencies Increase, Foreclosure Starts Flat in Latest MBA National Delinquency Survey* (Dec. 5, 2008).

[28] RealtyTrac, *Foreclosure Activity Increases 81 Percent in 2008* (Jan. 15, 2009) (online at www.realtytrac.com/ContentManagement/pressrelease.aspx?ChannelID=9&ItemID=5681&accnt=64847).

country. Additionally, in its third quarter 2008 National Delinquency Survey, the MBA found that there were only nine total states which had rates of foreclosure *starts* above the national average (Nevada, Florida, Arizona, California, Michigan, Rhode Island, Illinois, Indiana and Ohio), while the remaining 41 states were all below the national average.[29] Clearly, these data show that the foreclosure problem is very real, but it is also very concentrated in select areas, so much so that a few states are skewing the statistical average for the preponderance of the other states. This fact must be taken into consideration when considering the effectiveness of any government-subsidized foreclosure mitigation effort.

E. Voluntary Mitigation Alternatives

In reviewing the effectiveness of government-subsidized foreclosure mitigation efforts, it is important to keep in mind that there is no single reason why borrowers decide to buy a home and there is no single reason why some borrowers go into foreclosure. Home buying and home owning, like any other activity, are the culminations of a wide variety of individual factors including cost, location, availability, and station in life. Different people can approach the decision in distinct ways, weigh competing factors differently and perhaps even make unwise, foolhardy, or bad choices despite every reason to the contrary. Nevertheless, because the factors that go into the decision to buy and keep a home can vary greatly, it stands to reason you cannot devise a single foreclosure mitigation program that will appeal to or benefit everyone who might be at risk. Thus, a more sensible approach would be encourage a series of different mitigation programs and approaches instead of attempting to force all distressed borrowers into one massive government-subsidized foreclosure mitigation effort.

To that end, since the onset of the mortgage crisis the federal government has worked with banks and other private parties to develop a number of voluntary initiatives to assist borrowers in danger of foreclosure. While by no means perfect, these efforts have been helping borrowers to varying degrees without having to resort to government mandates or increased taxpayer risk. Some of these initiatives have included:

- **HOPE NOW**: In response to the downturn in the U.S. mortgage market in 2007, the Bush Administration helped broker an alliance of mortgage lenders, servicers, counselors, and investors called the HOPE NOW Alliance. The goals of HOPE NOW are to "maximize outreach efforts to homeowners in distress to help them stay in their homes" and to "create a unified, coordinated plan to reach and help as many homeowners as possible." HOPE NOW estimates that it has helped nearly 3.2 million homeowners avoid foreclosure since July 2007.[30]

- **JP Morgan Chase**: On October 31, 2008, JP Morgan Chase announced it would expand its mortgage modification program by undertaking multiple initiatives designed to keep

[29] Mortgage Bankers Association, *Delinquencies Increase, Foreclosure Starts Flat in Latest MBA National Delinquency Survey* (Dec. 5, 2008).

[30] HOPE Now, *Mortgage Lending Industry Prevented Almost 240,000 Foreclosures in December* (Jan. 29, 2009) (online at www.hopenow.com/upload/press_release/files/HOPE%20NOW%20December%202008%20Data%20Release%20p.df).

more families in their homes, including extending its modification programs to customers of Washington Mutual, which Chase acquired in September, and EMC Mortgage, the lending arm of Bear Stearns, which Chase acquired in March 2008.[31] Chase will open regional counseling centers, hire additional loan counselors, introduce new financing alternatives, proactively reach out to borrowers to offer pre-qualified modifications, and commence a new process to independently review each loan before moving it into the foreclosure process. Chase has selected sites for 24 Chase Homeownership Centers in areas with high mortgage delinquencies where counselors can work face-to-face with struggling borrowers. Chase anticipated 13 of these centers — in California and Florida — open and serving borrowers by the end of February 2009. The other 11 around the country will be open by the end of March 2009. Chase expects these changes will help an additional 400,000 borrowers. While implementing these enhancements, Chase will not put any additional loans into the foreclosure process.

- **Wells Fargo Home Mortgage Servicing**: Over the past year and a half, through the Leading the Way Home program, Wells has provided more than 700,000 foreclosure prevention solutions.[32] Wells' program is designed to work with all its customers — including those not yet in default — to determine if they qualify for a modification. For example, since Wells acquired Wachovia and its unique Wachovia Pick-a-Payment option ARM loans, Wells will use more aggressive solutions through a combination of means including permanent principal reductions in geographies with substantial property declines. In total, Wells predicts 478, 000 customers will have access to this program if they need it.[33] Wells has also extended a foreclosure moratorium on loans it owns through March 13, 2009.

- **Bank of America**: In early October, Bank of America announced the creation of a proactive home retention program that will systematically modify troubled mortgages with up to $8.4 billion in interest rate and principal reductions for nearly 400,000 Countrywide Financial Corporation customers nationwide.[34] (Bank of America acquired Countrywide July 1, 2008). The program was developed together with state attorneys general and is designed to achieve affordable and sustainable mortgage payments for

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[31] JPMorgan Chase, *Chase Further Strengthens Robust Programs to Keep Families in Homes* (Oct. 31, 2008) (online at files.shareholder.com/downloads/ONE/514430481x0x245621/b879b4eb-40c0-43f8-8614-6f2113759d0c/344473.pdf).

[32] *Wells Fargo and National Urban League Publish New Foreclosure Prevention Workbook: Advice from Foreclosure Experts Given to Homeowners Across the Country*, Business Wire (Feb. 28, 2009) (online at www.businesswire.com/portal/site/home/permalink/?ndmViewId=news_view&newsId=20090228005030&newsLang=en).

[33] Wells Fargo, *Wells Fargo Merger Gives 478,000 Wachovia Customers Access to New Wells Fargo Solutions if Their Mortgage Payments Become At-Risk* (Jan. 26, 2009) (online at www.wellsfargo.com/press/2009/20090126_Wachovia_HMS).

[34] Bank of America, *Bank of America Announces Nationwide Homeownership Retention Program for Countrywide Customers: Nearly 400,000 Countrywide Borrowers Could Benefit After Program Launches December 1* (Oct. 6, 2008) (online at newsroom.bankofamerica.com/index.php?s=press_releases&item=8272).

borrowers who financed their homes with subprime loans or pay option adjustable rate mortgages serviced by Countrywide and originated prior to December 31, 2007. Bank of America has also implemented a foreclosure sale moratorium on mortgages it holds as well as mortgages owned by investors that have agreed to the moratorium for mortgages it services until final guidelines are issued by the Obama Administration on its foreclosure plan.

- **Citigroup**: In November 2008, Citigroup announced the Citi Homeowner Assistance Program for families particularly in areas of economic distress and sharply declining home values whose mortgages Citigroup holds.[35] In February, Citigroup also initiated a foreclosure moratorium effective through March 12 while awaiting implementation of the Obama Administration's foreclosure plan.

These initiatives, coupled with other efforts like the federal Hope for Homeowners law and the FDIC's IndyMac loan modification program, are providing options to distressed borrowers. However, some have complained that these programs are not doing enough to help more borrowers and are advocating for a larger government program to fill that void. Such calls seem to ignore the reality that loan modifications can be complicated, time consuming exercises and are of course dependent upon the borrower being willing and qualified to participate. As noted in the majority's report, foreclosures can cost lenders up to $70,000 in costs and fees, providing ample economic motivation for lenders to avoid such an outcome wherever possible.

Ultimately, instead of creating new government-subsidized programs, the best foreclosure mitigation program is having a strong economy, a job, and the freedom to keep more of what you earn. That's why I have supported legislation to encourage an economic turnaround, help preserve jobs, and spur widespread economic growth by lowering the tax burden that job-creators face, such as the Economic Growth Act of 2008. That legislation, introduced last year by Rep. Scott Garrett, would have provided for full, immediate business expensing, a significant reduction in the top corporate tax rate, an end the capital gains tax on inflation, and simplification of the capital gains rate structure. Any one of those components would have increased our economic growth, and helped hardworking Americans keep their jobs and earn more money. For example, while reviewing the impact of just one component of the bill, Dr. Mihir Desai of the Harvard Business School has estimated cutting the corporate capital gains rate from 35 percent to 15 percent could unlock $1 trillion worth of wealth for the economy.[36] Even though such proposals might not contain a specific foreclosure mitigation program, the vast economic growth and prosperity that bills like the Economic Growth Act could unleash would help countless numbers of Americans pay their mortgages and other bills without government-subsidized foreclosure mitigation plans.

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[35] Citigroup, *Citi Announces New Preemptive Initiatives to Help Homeowners Remain in Their Homes* (Nov. 11, 2008) (online at www.citigroup.com/citi/press/2008/081111a.htm).

[36] Americans for Tax Reform, *America's Growth Agenda Part Four: Cut the Corporate Capital Gains Rate to 15%, Unlocking Wealth for Job Creation* (Jan. 21, 2008) (online at 74.6.239.67/search/cache?ei=UTF-8&p=%22Mihir+Desai%22+capital+gains&fr=my-myy&u=atr.org/content/html/2008/jan/012108pr-growthcorpcapgains.html&w=%22mihir+desai%22+capital+gains&d=AwxrU52uSUbL&icp=1&.intl=us).

Additionally, providing tax relief to Americans instead of creating new government programs would help address some of the fairness concerns behind such programs because tax relief is unbiased towards home owners, borrowers, and renters. Additionally, tax relief proposals have the added benefit of being able to provide more relief to more people at a lower cost. For example, the tax reduction alternative offered by Reps. Dave Camp and Eric Cantor to the recently enacted $1.1 trillion stimulus bill contained several provisions that would help America's small businesses and employers.[37] Those provisions combined — creating a 20 percent deduction for small business income (which would affect 99.9 percent of the 27.2 million businesses in America), extending the favorable bonus depreciation rules for small businesses, extending the Net Operating Losses carryback rules for previously profitable companies to seek immediate cash refunds of past taxes paid, and repealing of 3 percent withholding requirement for government contractors — would have cost less than $83.1 billion over 11 years. That amount is slightly more than the one year cost of the $75 billion Homeowner Affordability and Stability Plan proposed by President Obama last month, which would affect fewer people.[38]

[37] House Committee on Ways and Means Republicans, *Summary of Camp-Cantor Substitute to H.R. 1* (Jan. 28, 2009) (online at republicans.waysandmeans.house.gov/showarticle.asp?ID=462).

[38] Federal Deposit Insurance Corporation, Homeowner Affordability and Stability Plan (online at www.fdic.gov/consumers/loans/hasp/index.html) (accessed Mar. 5, 2009).