A Shared Agenda and Principles for Mortgage Market and Community Stabilization Policy

April 23, 2008

Background

The U.S. economy teeters on the edge of recession because of the wide-ranging crisis in the housing market: a vicious downward spiral in housing prices, escalating foreclosures, rising losses on mortgage-backed securities, contagion in other credit markets, and dwindling liquidity that has already toppled one major U.S. financial institution. The impact on families who lose their homes to foreclosure is substantial, and their neighbors and communities suffer as well. Foreclosures depress neighboring home values, and vacant properties become magnets for arson, crime, and vandalism. Our minority and low-and-moderate income communities are being hardest hit, but they are not alone. The housing crisis has already had macroeconomic effects, with liquidity drying up across credit markets, lost home values depressing consumer spending, and lost jobs in the housing and construction sector contributing to weak labor markets. Monetary and fiscal policies alone will not end the crisis. It is clear that after a year of exhortation, voluntary efforts developed by lenders and the Treasury Department to address this crisis have proven inadequate. The pace of modifications and refinancings is lagging far behind the ever increasing pace of foreclosures, which are expected to continue for a couple of years. The time has come for strong federal policies to restore capital markets and our communities by facilitating mortgage restructuring and community stabilization.

About This Document: The organizations below have joined together behind a policy agenda and principles, so that we can educate the public and policymakers with a unified voice, have a greater influence on the solutions that emerge, and accelerate the pace of action.

The Agenda

The goal of policy now must be to protect homeowners and communities by preventing the continued acceleration of home foreclosures and by restoring confidence in the credit markets. Policies should aim to (a) keep existing owners in their homes where possible as a way to preclude the significant costs to families, increased housing inventories, and depressed values that come from foreclosure; and (b) support the acquisition and constructive reuse of foreclosed properties for affordable housing through homeownership with viable non-discriminatory mortgages on responsible terms, and through quality rental units, as well as the creation of other community assets. Interventions that reduce foreclosures over the next couple of years and support homeownership and affordable rental housing will benefit homeowners, neighborhoods, communities, and financial markets. *These strategies are mutually reinforcing and must be pursued in tandem.*

To prevent the continued acceleration of foreclosures, government must <u>promptly</u> facilitate the bulk transfer of mortgages into the hands of new private owners with the incentive and ability to modify or refinance the loans on viable terms. Time and the limited capacities of mortgage servicers do not allow the continued loan-by-loan evaluation of options by servicers who must serve the often conflicting interests of investors in complex securitization structures. Government must create a mechanism for the transfer of mortgages from securitization trusts with limited flexibility to new holders who will be responsible for helping homeowners stay in their homes with viable loans on responsible terms. Servicers willing to refinance existing loans in bulk by offering new loans on the same responsible terms need not transfer their loans to a new party. When homeownership is not sustainable for current borrowers, as it will be in some instances, these new note holders will have the responsibility to terminate the mortgage using strategies that minimize adverse consequences for the borrowers and their communities.

Effective solutions for foreclosed properties must be centered on state and local governments and their non-profit, private sector, and philanthropic partners. To stabilize communities, the federal government must promptly provide flexible resources to allow state and local governments and non-profits to implement locally-appropriate reuse strategies for foreclosed properties. These resources must be targeted to the communities most greatly affected by high levels of foreclosures and rising foreclosure rates, and where current regulations provide guidance on the need for investment, as under Community Reinvestment Act and GSE-underserved area designations. Furthermore, we must strike an appropriate balance in assisting owners in distress as well as renters of single family homes who are being displaced by foreclosures.

Principles: In pursuing both mortgage restructuring and community stabilization, these important principles must govern:

1. Policy cannot and should not prevent market corrections, but must seek to prevent a seizing up of markets and a destabilizing and dramatic home value freefall fueled by loss of liquidity and confidence in the markets. Government has an obligation to step in to help stabilize markets to prevent widespread and devastating impacts unrelated to market fundamentals. The social costs of market overcorrections will jeopardize the life savings, college education funds, and retirement assets of millions of Americans caught in a crisis not of their own making. It will cause sharp declines in needed revenues for state and local governments, which in turn will require steep cuts in vital public services.

2. The urgency and scale of the problem require wholesale solutions, not piecemeal steps. The time has passed for reliance only upon incremental, loan-by-loan, property-by-property strategies. We must facilitate the bulk transfer of housing assets—both physical and financial—into capable hands. We must realign incentives to drive far greater activity by servicers to restructure or refinance debt and prevent foreclosure.

3. We can no longer rely solely on voluntary actions by servicers to modify or refinance loans. Servicers need powerful incentives and clarity so they are motivated to participate in new restructuring and refinancing opportunities to create sustainable loans tied to the current value of the property or to transfer loans to those who will. One such incentive would be a mechanism to modify individual loans in carefully targeted circumstances where servicers are unwilling or unable to do so.

4. Solutions on this scale require the expertise and capacity of private as well as governmental and nonprofit actors. We cannot expect to address a problem of this magnitude with only those acting for public purpose. We must attract private capital to be part of the solution. We need new investors to support the financing of modified or refinanced loans and the acquisition of foreclosed properties.

5. Foreclosure rules should build community assets, not strip them for short-term private gain. Opportunistic investors who acquire foreclosed assets at bottom basement prices, leaving homes abandoned and waiting for markets to rebound, can exacerbate, not ameliorate, the consequences of house price depreciation. Government must set ground rules to better protect homeowners, neighbors, and communities in the process of asset recovery and disposition.

6. Many share responsibility for the crisis and so must share responsibility for its solutions. Borrowers, lenders, investors, and the government must contribute and bear some of the cost of recovery. Specifically:

- **No bailout for investors.** Policies that help to stabilize the housing and credit markets are not aimed at softening the losses that flow from bad decisions by investors in risky mortgages, but on stabilizing families, communities, and the economy. Losses must be taken transparently to move forward. By the same token, action now to stabilize the situation and provide an effective and orderly path to resolution will minimize the risk of catastrophic losses throughout the economy fueled by market panic and overreaction.
- **No windfall for homeowners.** Homeowners who benefit from reduced balance loans or lower-than-market-price terms should share subsequent home price appreciation with taxpayers and credit providers. Soft second liens, shared equity, and other tools can be used to ensure some horizontal equity among homeowners.
- **No participation by speculators.** Resources should be focused on owner-occupants and not reward speculation by investors.

7. Solutions must offer affordable loans and comply with fair lending laws. Financing available under new programs should be non-discriminatory and viable, made on responsible terms that the homeowner can reasonably be expected to sustain. Anti-discrimination laws must be vigorously enforced to prevent redlining and racial steering.

- Adequate funding must be available to allow organizations on the front lines to address redlining, racial steering and other practices that violate fair lending and fair housing laws.
- Regulatory agencies must conduct vigorous examinations of their member institutions that include the institution's entire enterprise and that are comprehensive—assessing not only the quality, terms and conditions of loans being made in underserved communities, but the distribution systems through which those loans are made.
- Government entities with enforcement responsibilities must step up their endeavors to ensure that fair housing laws are effectively enforced.
- All relevant players, including lenders, mortgage originators, investors, regulators, and government agencies must address issues of discriminatory impact and effect to ward against unintended discriminatory consequences in the marketplace.

8. Counseling resources will prevent foreclosures and result in more sustainable loans. Sufficient funds must be available from government, private—including lender and investor—and philanthropic sources to build and support the capacity of organizations trained to effectively and efficiently advise and guide borrowers through the system.

9. All available delivery channels should contribute solutions. The scale of the problem requires multiple strategies.

- **FHA can play a critical credit enhancement role in facilitating the orderly restructuring of assets, and its capacity must be enhanced in order to do so.** FHA's authority and capacity (staff, contracting, expertise, and flexibility) needs to be significantly strengthened if FHA is to be part of the solution and not create new problems for taxpayers and communities in resolving our current crisis.
- **The GSEs also must be part of the solution.** The government-sponsored enterprises, Fannie Mae, Freddie Mac, and the Federal Home Loan Banks, were created by government charter with a public purpose and benefit from that status. We have not seen as urgent a need in decades. Whatever their current challenges, they must be encouraged and, if necessary, required to use their sizable advantages to help address this great national challenge. The GSEs must be strongly encouraged to invest quality

capital in historically underserved communities to avoid further decline and boost redevelopment opportunities.

- **Private originators, portfolio holders, and securitizers of mortgage loans must contribute to the solution.** Write-downs of principal and restructuring of loans to make them sustainable for current borrowers; discounted sales of assets and properties to assist in neighborhood and community stabilization; and assistance to community-based organizations in their fair housing promotion, counseling, and other work are essential. Regulated depositories should receive CRA credit for substantive and additive actions that they take to ameliorate this crisis. Other entities also should be encouraged to participate in similar efforts.

10. Public funds should be carefully targeted. Significant public funds will be needed to acquire, rehabilitate, and in some cases demolish and redevelop foreclosed homes. These funds should be targeted to the communities where the concentration of foreclosures is causing housing markets to seize up, with serious consequences for public safety, the tax base, and economic sustainability. Public funds should be repaid or recycled to maximize their effective use where possible, but this possibility may be limited in severely damaged areas.Adhering to these principles will provide broad benefits to families and communities, and to our economy as a whole. By contrast, in the absence of direct government involvement in solving these housing market failures, the outcomes will be disastrous for both markets and communities.

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Signatories:

ACORN
AFL-CIO
Center for American Progress Action Fund
Center for Responsible Lending
Consumer Federation of America
Consumers Union
Enterprise Community Partners
Laborers' International Union of North America
Leadership Conference on Civil Rights
Local Initiatives Support Corporation
National Community Land Trust Network
National Community Reinvestment Coalition
National Council of La Raza
National Fair Housing Alliance
National NeighborWorks Association
New America Foundation
Service Employees International Union (SEIU)
The Lawyers' Committee for Civil Rights Under Law
U.S. Public Interest Research Group