

THE POLICY RESPONSE TO FORECLOSURES:

WHAT CAN STATE AND LOCAL ACTORS DO?

PRESENTATION TO THE  
MISSOURI HOMEOWNERSHIP PRESERVATION SUMMIT

JANUARY 14, 2010  
JEFFERSON CITY, MISSOURI

# Spillover Effects of Foreclosures

Homebuyer



Lender



Neighboring property owners, local governments, children, families

Investors, ratings agencies, etc.

# Policy Responses to Spillover Effects

- Prevent spillovers or minimize them
- Inequities in foreclosure spillovers
- Public, Nonprofit and Private Actors
- Goal: Housing markets with a balance of supply and demand and minimal involuntary displacement
- “Moral Hazard” problem

# Three Types of Foreclosure Spillovers



1. Declining Property Values
2. Social Disorder and Crime
3. Local Government Stress

# Falling Property Values

Examples of former resident belongings dumped at curb



# Property Values

- Surrounding properties within 1/8 mile (660 feet) are negatively affected.
- Chicago Study: 0.9% decline; \$159,000 per foreclosure' 1.8% in low- and moderate income neighborhoods
- 13-state study: 1.3% within 300 feet; 0.6% within 660 feet
- Rogers and Winter study of St. Louis County

# Crime

- “Broken Windows” Theory
- A 1% increase in foreclosure rate increases the number of violent crimes by 2.33% (Chicago).
- 1.7 violent crimes per 100 houses in high foreclosure neighborhoods versus 0.6 for low foreclosure neighborhoods (Charlotte/Mecklenburg)

# Effects on Children

- 2 million children directly affected; 33,900 in Missouri (2009 estimate, Center for Responsible Lending)
- Educational Effects: frequent moves reduce the chance of graduating from high school by 50%
- Behavioral effects: 20% increased chance of violent behavior in high school
- Health Effects: unstable housing has negative effects on diet and healthy body weight
- Homelessness
- Family stress: divorce, child abuse and addictions



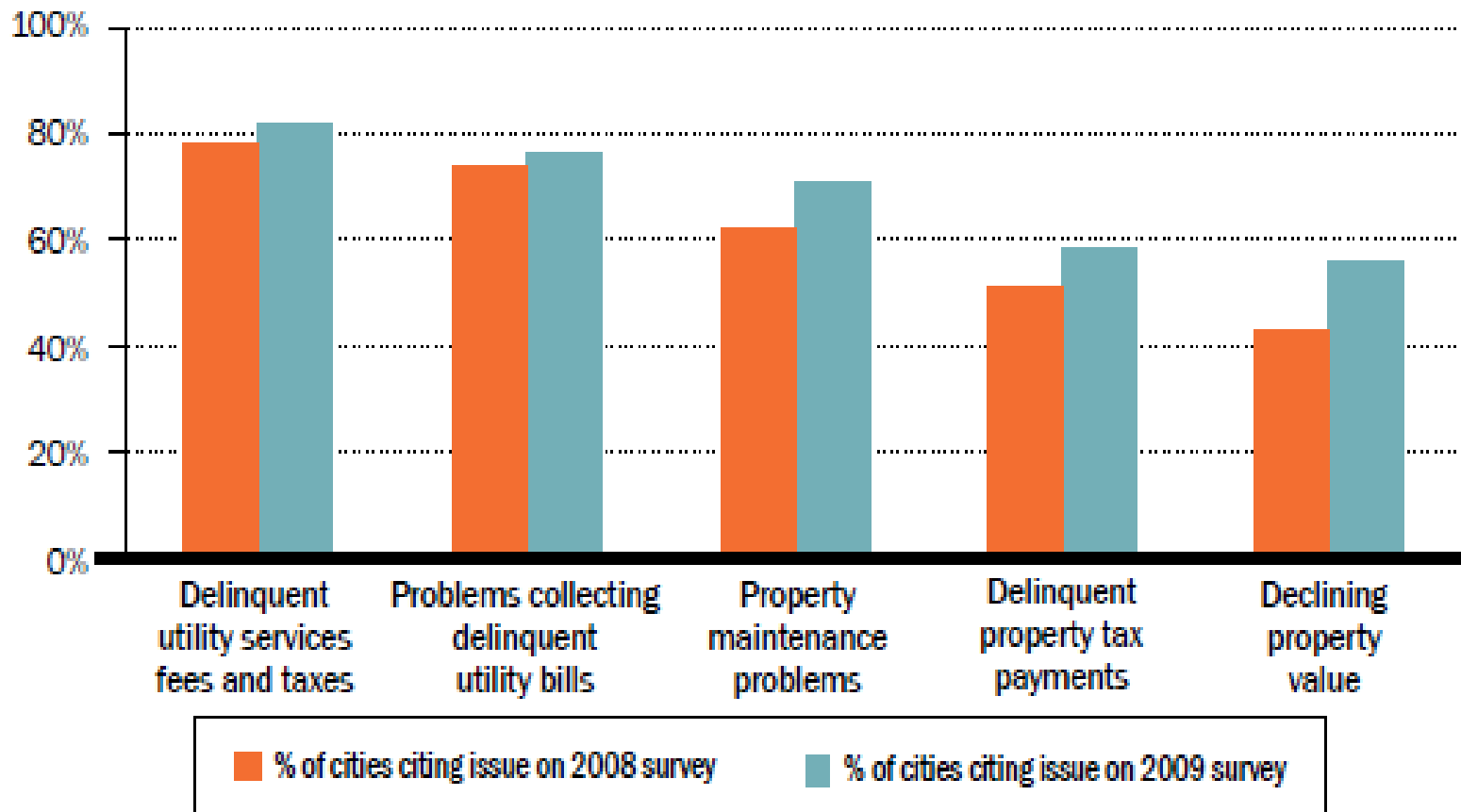
# Falling Local Government Revenues

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1. Declining property tax revenues
2. Delinquent payment of property taxes and utility service fees
3. Rising property tax rates

# Example from Minnesota

Chart RH-C: Top foreclosure-related issues in Minnesota cities



Source: League of Minnesota Cities, *State of Cities*, 2009

# Extra Costs to Municipalities

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- Five scenarios: From \$430 to \$34,199 (Chicago Study, 2005)
- Average Cost: \$19,227 (U.S. Congress, Joint Economic Committee)

# What Can State and Local Actors Do?



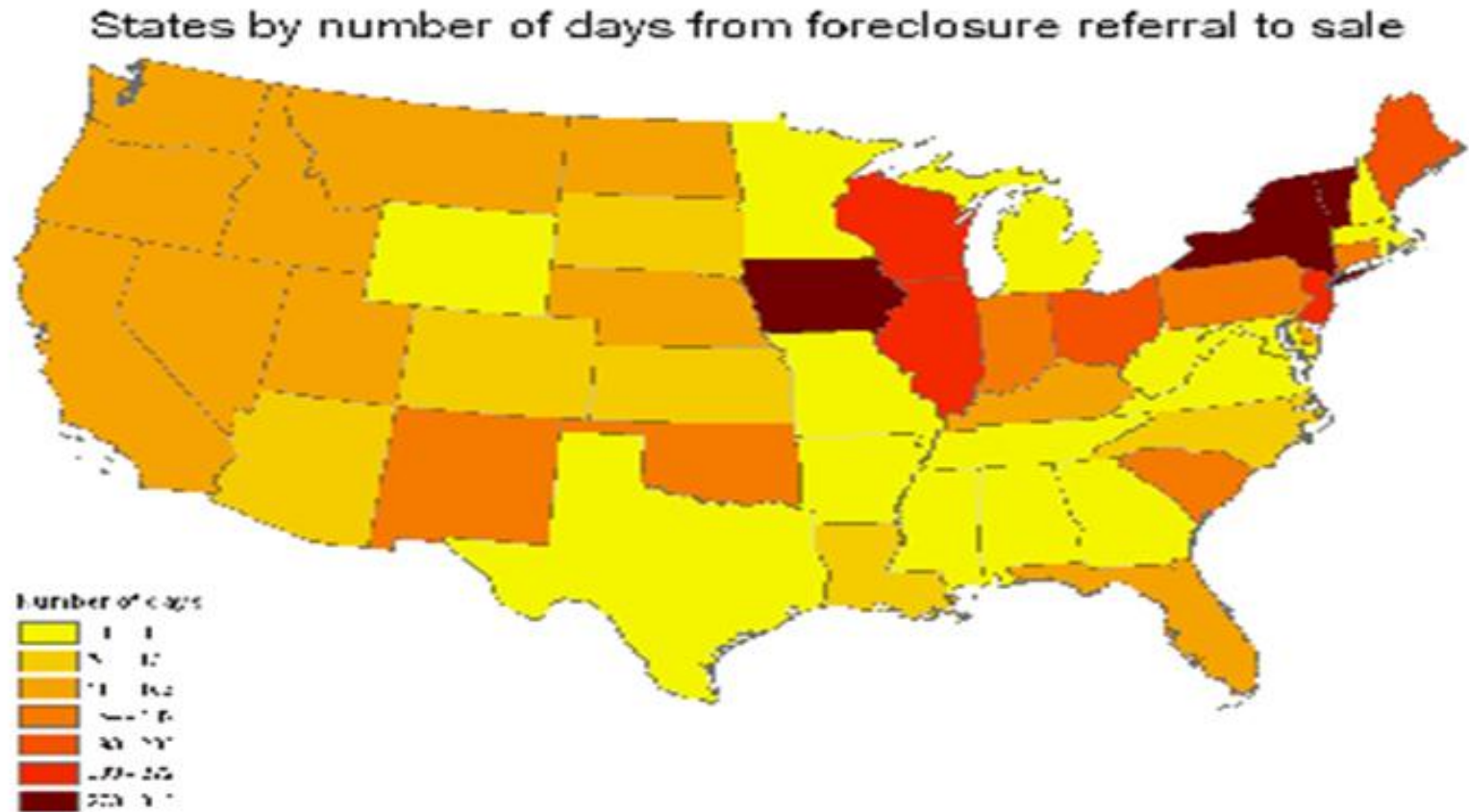
1. Prevent foreclosures and help keep families in their homes.
2. Discourage future risky lending.

# Non-judicial Foreclosure Process in Missouri



Source: Analysis by Amy Crews Cutts and William A. Merritt, "Interventions in Mortgage Default: Policies and Practices to Prevent Home Loss and Lower Costs." In *Borrowing to Live* (Brookings/JCHS, 2008). Based on Freddie Mac data.

# Foreclosure Process and Speed of Foreclosure



Source: Analysis by Amy Crews Cutts and William A. Merritt, "Interventions in Mortgage Default: Policies and Practices to Prevent Home Loss and Lower Costs." In *Borrowing to Live* (Brookings/JCHS, 2008). Based on Freddie Mac data.

# Impact on foreclosure prevention

- The fast foreclosure process in Missouri is a barrier to foreclosure prevention.
  - ▣ Missouri: as few as 38 days; 60 days on average
  - ▣ National average: 120 days

How could Missouri give homeowners more time to prevent a foreclosure?

# Foreclosure Counseling

- NeighborWorks America: \$410 million of federal support (2007 – today)
- Urban Institute Evaluation (2009) of Foreclosure Counseling
  - ▣ 373,169 homeowners have received counseling (March 31, 2009)
  - ▣ 11% of clients received a loan modification
  - ▣ Of those already in foreclosure, those who received counseling were 60% more likely to avoid foreclosure completion.
  - ▣ On average, counseling clients who received a modification reduced their monthly payments \$454 more than those who received no counseling.



# Foreclosure Counseling Can Work



Sue Livingstone

Client of Beyond Housing, St. Louis

“I tried working with my servicer,” Sue said. “They kept putting me off, kept sending notices. They would say things like, ‘Maybe you need to go to church and ask for help.’ You feel worthless. It’s a real self-esteem deflater.

The swift response that their counselor, Linda Ingram, received from her servicer amazed and frustrated Sue.

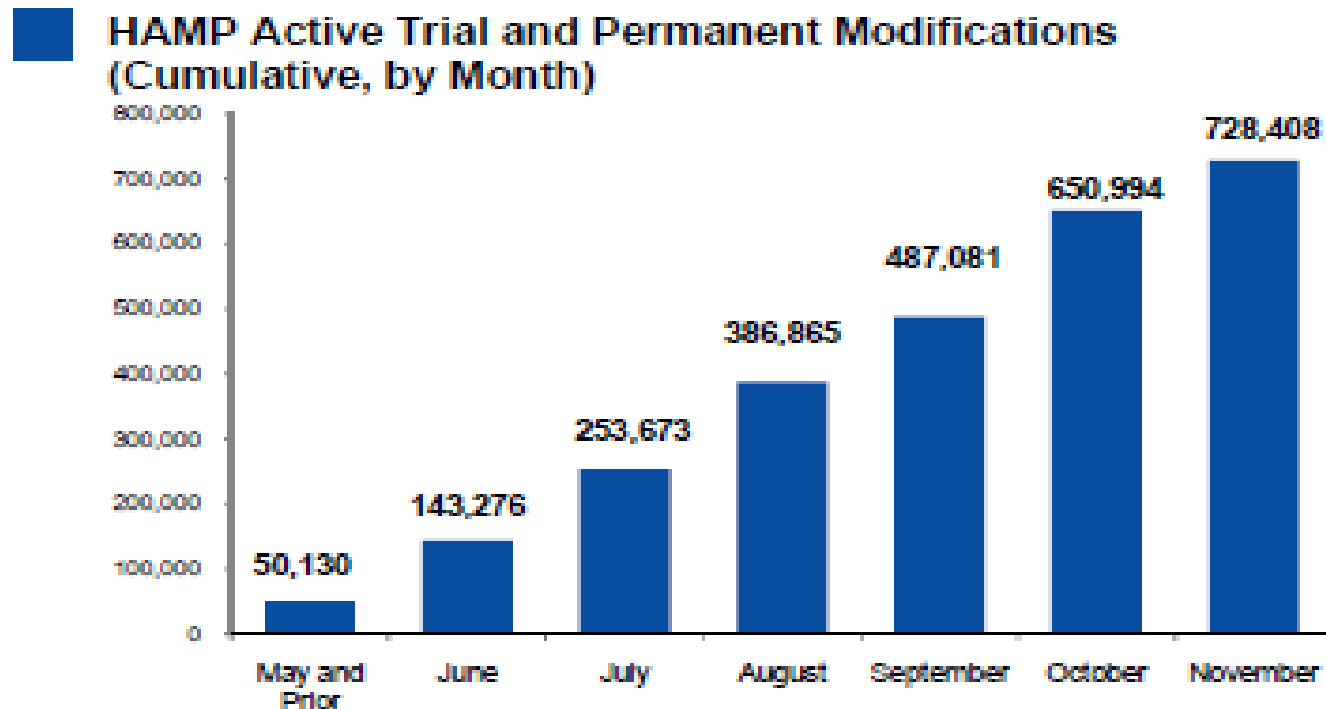
“We brought in all the paperwork, along with the 25 pages of the same documents I had faxed in. [Linda] picked up the phone and got it taken care of. Why did I have to cry for six months, and she just picks up the phone and, poof, it’s done?” she said.

# Federal Making Home Affordable Program (2009)



- Began in March 2009
- Funding:” \$75 billion
- Loan payments adjusted to 31% of income (federal subsidies)
- Incentives to servicers
- Does not require principal reductions

# HAMP Performance as of November, 2009



Source: Active trial and permanent modifications as of November 30; based on numbers reported by servicers to the HAMP system of record.

- Permanent modifications nationwide = 31,382 (Nov. 2009)
- Temporary modifications in Missouri = 9,026
- Estimated permanent modifications in Missouri = 389

# Obstacles to Mortgage Modifications

## Survey of Federally Funded Counselors: What are the top challenges to successful outcomes?

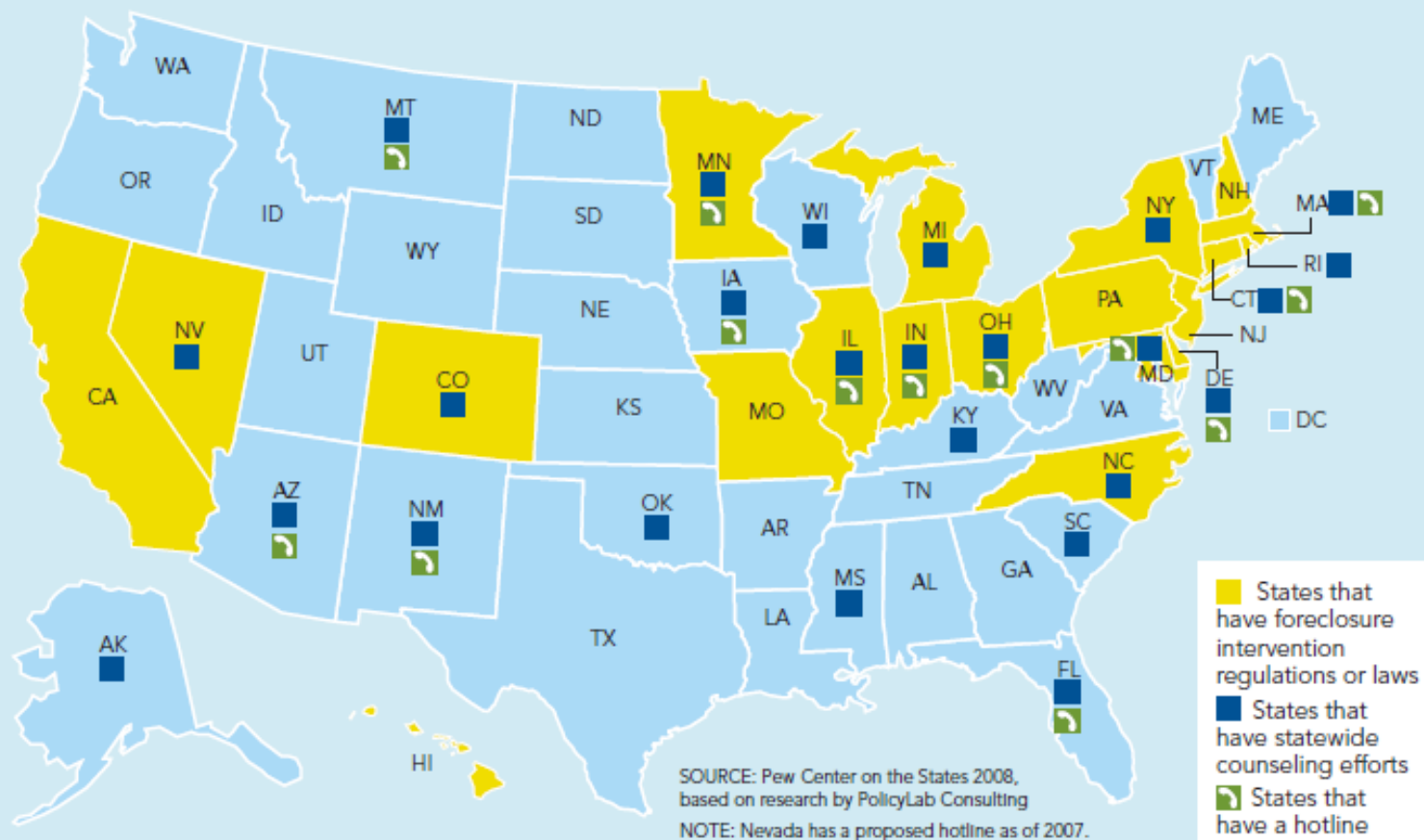
- Top challenge: loss of income due to job loss or reduced wages
- Second most serious challenge: “Slow or no response from servicers”
- Six of top seven challenges related to working with servicers.

Source: *National Foreclosure Mitigation Counseling Program Evaluation, Interim Report #2* (Washington, DC: Urban Institute, May 12, 2009)

# State Support for Foreclosure Prevention

Exhibit  
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## STATES RESPOND: HELPING HOMEOWNERS PREVENT FORECLOSURE



# State Foreclosure Prevention Programs

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- Requirements that borrowers be notified earlier about counseling opportunities (e.g., with foreclosure notice)
- Direct support for foreclosure counseling agencies
- Refinance Loan Programs (MHDC Program: up to \$13,000)

# Local Foreclosure Prevention Programs

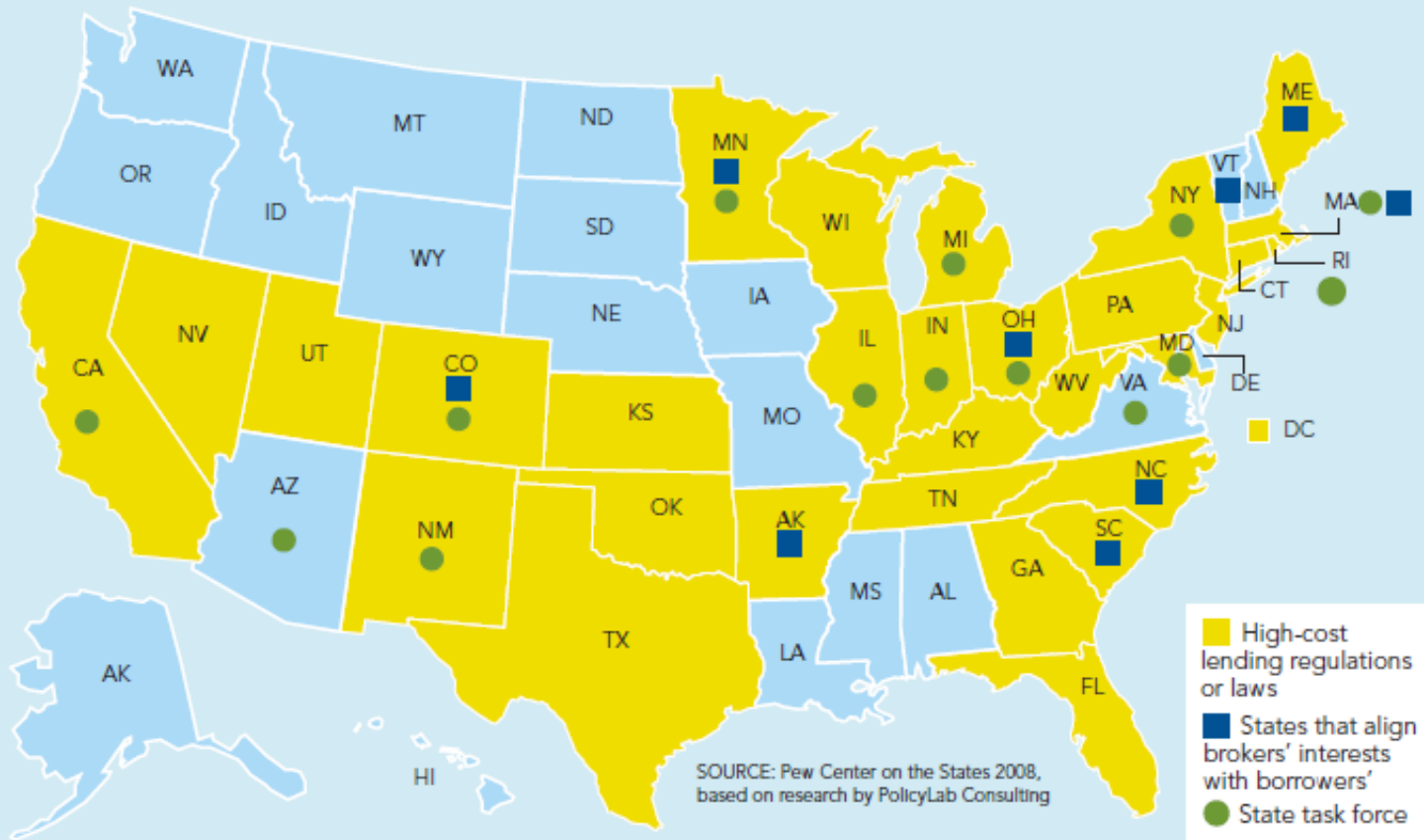
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- Direct support for foreclosure counseling (Cuyahoga County)
- Local Rescue Funds (St. Louis City and County)
- Negotiated Agreements with Servicers (ESOP)
- Foreclosure Mediation Programs (Philadelphia)
- KETC: Facing the Mortgage Crisis

# States Regulate High-Cost Loans

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STATES RESPOND: PROTECTING CONSUMERS FROM HIGH-COST LOANS





# State Policies to Prevent Future Risky Loans

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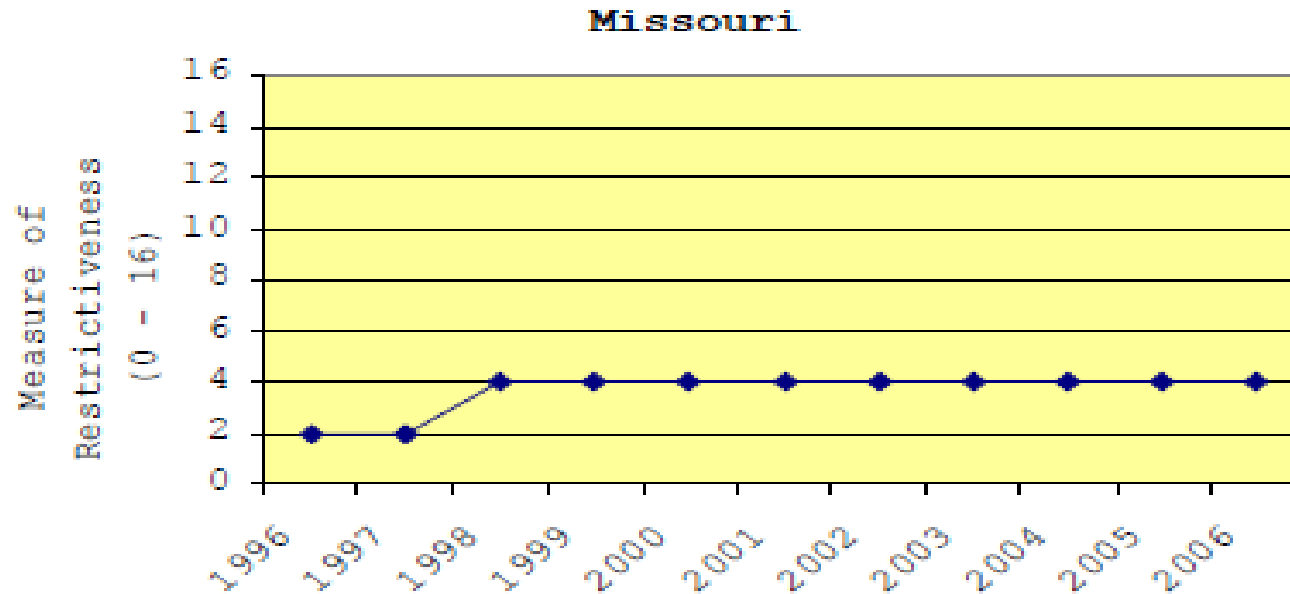
- Require lenders to verify income.
- Limit or ban predatory prepayment penalties.
- Encourage consumer education and counseling before a loan is made.

# Mortgage Broker Licensing

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- Why important?
- Two-thirds of all high-cost and predatory loans were made by state-regulated mortgage brokers.

# Missouri Mortgage Brokers in Are Lightly Regulated



- ❑ 18 states rated “high” (9+)
- ❑ 17 states rated “medium (5 – 8)
- ❑ 15 states rated “low” (4 or less)

# State Foreclosure Prevention Task Forces

- Formed in 14 states
- Public, private and nonprofit representatives appointed by the governor
- Recommendations to governor and legislature
- Puts the foreclosure issue on state agenda