HOUSING POLICY COUNCIL
THE FINANCIAL SERVICES ROUNDTABLE

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Federal Housing Finance Agency
Office of the General Counsel
Alfred Pollard
400 Seventh Street, SW
Eighth Floor
Washington D.C. 20024

Re: No. 2012-N-11 Use of Eminent Domain to Restructure Performing Loans

General Counsel Pollard:

The Financial Services Roundtable[1] and the Housing Policy Council[2] appreciate the opportunity to express our opposition to the use of eminent domain to restructure performing loans. We believe that current proposals pending before a number of local jurisdictions to use eminent domain to seize and restructure performing mortgage loans are counterproductive and would actually undermine on-going efforts to assist at-risk homeowners, hurt consumers who may seek to obtain mortgage loans in the future and ultimately damage the housing market.

Our member companies strongly support efforts to assist homeowners in difficulty and are working individually and collectively to assist borrowers through loan modifications, loan refinancings and other alternatives that prevent foreclosures. We will provide more detail below on those efforts, which we believe are far better alternatives than the use of eminent domain to seize mortgages.

Eminent domain proposals such as the one currently under consideration by the county of San Bernardino California and two of the cities therein Ontario and Hesperia would revise existing private contracts contrary to U.S. constitutional protections while providing little or no public benefit. While we recognize the significant difficulties these municipalities face, we believe that the use of eminent

[1] The Financial Services Roundtable represents 100 of the largest integrated financial services companies providing banking, insurance, and investment products and services to the American consumer. Member companies participate through the Chief Executive Officer and other senior executives nominated by the CEO. Roundtable member companies provide fuel for America's economic engine, accounting directly for $92.7 trillion in managed assets, $1.2 trillion in revenue, and 2.3 million jobs.

[2] The Housing Policy Council of The Financial Service Roundtable is a trade association that represents 30 of the leading national mortgage finance companies. HPC members originate service and insure mortgages. We estimate that HPC member companies originate approximately 75% of mortgages and service two-thirds of mortgages serviced in the U.S.

domain would reduce access to credit for borrowers, negatively impact main street investors' retirement funds and other savings and significantly and irreversibly harm mortgage finance markets. Further, these proposals would undermine the considerable on-going efforts being taken by the federal government, lenders and servicers to assist homeowners who are experiencing difficulty.

The San Bernardino Program

In the program under consideration in San Bernardino, the county and two cities have established a joint authority which would acquire performing underwater residential mortgage loans by eminent domain. Using private funds loaned to it, the Authority would purchase mortgage loans held in private label securitizations at a price deemed to be fair market value by state law, and then sell those loans one by one at a discounted price for whatever price the mortgagor can obtain funding in the market place. The newly financed loans would then be conveyed to those investors that funded the escrow. The investors would be free to securitize the loans.

Risks to borrowers in the jurisdiction – loan prices would increase

Current holders of the loans or the securities of which the affected loans are a part would receive whatever is deemed to be fair market value. We believe that the prices paid for these performing loans will be less than the investors would otherwise have willingly accepted for their investment. If it were the same or more than they would have accepted, they would of course engage in the transaction. But at that price, there would be no loss to current investors and therefore no increment to account for any profit to the new investors unless the jurisdictions used tax funds to absorb whatever amount is necessary to provide the new investors a profit.

Assuming that loss to the current investors is essential to make this program work as designed - these same investors, the fiduciaries that oversee personal, retirment, pension and other investments in mortgage loans and mortgage-backed securities that were forced to take a loss through the use of eminent domain will, of course, be reluctant to invest in mortgages in the future from jurisdictions that have such authority or have plans to exercise it.

Investors must even consider whether there is an additional risk in investing in mortgages from jurisdictions in which such authority does not currently exist, since it is possible that additional jurisdictions could implement similar programs. Investors must be compensated for that additional risk. With investors reluctant to purchase mortgages from certain jurisdictions, the price of residential mortgages in those jurisdictions would inevitably increase to attract future investors.

The reaction of investors may be more profound than that. They may simply choose to invest elsewhere and not spend the time and money to calculate the price of the additional risk of investing in an asset that can be seized at an unknown price at any point in time.

Either way, the immediate impact would be that the price of residential housing finance in that jurisdiction would increase, and that would mean that many borrowers would not be able to obtain financing. Further, the concept of secured lending that supports our current mortgage finance system would be irreparably damaged.

Tax Consequences

If as a result of the eminent domain proceedings, adjustments in housing prices are reflected throughout the jurisdiction, then unless the jurisdiction changes their basis for assessing taxes, not a simple process, tax revenues in the jurisdiction will decline. Housing prices will, of course, fall, not only for homes that are in the program, but even for those not selected to be in the program. This will inevitably lead to additional tax revenue loss for the jurisdiction.

In addition, those homeowners who have debt forgiven will have to include that as federal income once the current Mortgage Debt Relief Act terminates as scheduled in December 2012. All other things being equal, therefore, those homeowners who may benefit from a restructured mortgage through eminent domain will also see their federal income taxes increase as a result.

Because the target population of this proposal to seize loans is performing loans, many of these borrowers who are able to service their debt and desire to stay in their home will have a recognizable tax event triggering a large cash outlay that they otherwise would not have had. For homeowners who do not move for many years, this will put them in a worse financial situation by giving them paper gains and burdening them with an immediately due and payable tax liability.

Adverse impact on beneficiaries of the owners of the loans

Many of the loans that would be seized have been securitized, and the securities have been purchased by investors such as pension funds for teachers, first responders such as fireman and policemen, unions, government employees, etc. To the extent that this process moves profits to the new investors at the cost of the current investors, it moves profits from the retirement programs of firemen, teachers and others to the investors of the investment banking firm funding the eminent domain program.

Legal Questions

The proposed program raises a number of serious legal questions, some of them constitutional questions. Notwithstanding the research undertaken by proponents of the program, these are questions of first impression, as the concept has not yet been addressed by current statues or judicial decisions.

For example, it is not clear that any particular performing mortgage loan is harmful to the community, notwithstanding that the outstanding balance of the loan exceeds the current market price of the property. Such loans are performing, are not abandoned property and on the surface are just like any other mortgage loan in the community. While perhaps there is potential harm to an individual mortgagor when his loan is underwater, it is difficult to see how this harms the community as a whole if the homeowner is able to continue to pay his mortgage and maintain the property. Yet harm to the community or correspondingly, benefit to the community, is the essence of eminent domain proceedings. The eminent domain program will proceed one loan at a time, is not part of a redevelopment plan, and it is unclear which loans will be targeted by the program and which will not. It is clear that loans owned by the GSEs will not. A strong argument could be made that this system provides potential benefits only to the individual homeowners selected, but perhaps not to the community, and therefore is truly a government mandated transfer of property from one private individual (the holder of the mortgage loan) to another private individual (Mortgage Resolution Partners) that lacks the constitutional protection of being in the public interest.

In addition, there is a question concerning the property involved in a mortgage loan. Some intangible assets have been found to be susceptible to a taking through eminent domain, but no clear case has been cited in which a performing mortgage loan has been deemed eligible for taking by eminent domain.

Yet another hurdle is in the mechanics by which the program can move to scale. To do so, the authority would have to successfully negotiate with the Trustee of a private label security. That raises questions about the fiduciary responsibilities of the trustee, REMIC rules, and negotiations between the trustees and the interested parties in the trust. Raising the program to scale, therefore, seems unlikely without substantial litigation.

Further, it is unclear how the fair market value of the loans be determined. Pricing loans such as that in this market has been a daunting task for everyone, made less daunting only when the parties are in agreement that a sale should occur. Eminent domain takings, however, are not peaceful takings, and parties will contest the values ascribed unless they are seen as “full value” by the party whose property is being taken.

We believe that the use of eminent domain raises serious legal and constitutional questions that subjects San Bernardino County and its residents to substantial liability and would, at a minimum, result in costly and lengthy litigation.

<u>There would be no compensating public benefit.</u>

In exchange for the increased price of mortgage loans, and suppression of housing prices in the jurisdiction, no discernible public benefits have been identified by proponents of the program. Of course, borrowers that get to stay in their homes with a smaller mortgage loan will receive an immediate benefit, but the impact on property values throughout the jurisdiction will diminish that relief. Moreover, those borrowers that are not selected for the program will receive no benefit, but will be disadvantaged by the attendant diminution in housing market values. In those circumstances, it is difficult to see how the community as a whole will benefit.

The financial gain would go to the investors in the program, since in exchange for their loans, they would receive mortgage loans of performing borrowers with loans less than the value of their houses. Those would be profitable loans, and could easily be securitized and sold for an immediate profit by those investors. In other words, the losses to the current investors would become the profits of the new investors.

The loans that would be seized and restructured are loans that are currently performing, so unlike loan modification programs already underway, this proposed program would not increase the number of performing loans in the county. These are not abandoned properties with tall grass in the front yards, but homes with performing mortgages and property value that will potentially increase as the market recovers. Perhaps some of the potential participating homeowners could experience financial difficulty sometime in the future, but servicers have programs in place to work with these borrowers at that time making this preemptive and harmful program unnecessary.

While GSE loans are currently excluded from the program, it is likely that there would be pressure to add such loans if the program received favorable media coverage. Especially given that GSE loans are such a high percentage of the total loans in any jurisdiction. Certainly, absent GSE loans, only spotty coverage of the jurisdiction could be obtained. When one segment of the citizenry is benefitted and others of comparable standing are not, it is questionable whether that is a public benefit. This concern is magnified given that the reduced access to credit and other long term ramifications would be borne by all residents.

<u>Current assistance to borrowers is overlooked.</u>

The proposed eminent domain program does not help troubled borrowers; it assists those who are making payments regularly. Both the government and private sector have implemented a variety of programs to help those borrowers most in need.

As of June 2012, almost 42,000 homeowners in the Riverside-Ontario-San Bernardino MSA have received permanent modifications through the federal Home Affordable Modification Program (HAMP), almost 253,000 Californians have received a HAMP permanent modification and more than 188,000 Californians refinanced through the Home Affordable Refinance Program. In addition, the federal government through the Hardest Hit Fund Program has allocated almost $2 billion to California for the Keep Your Home California program. Since 2007, the mortgage servicing industry has provided permanent, non-foreclosure solutions to more than 6.43 million households nationwide. These plans are offered free of charge and with none of the negative implications noted above. Municipalities should explore ways to help struggling homeowners take advantage of these existing programs that are working, rather than implement plans that benefit few at the cost of many.

In addition, homeowners in California and elsewhere are being assisted by proprietary refinancing and loan modifications through their servicers. Housing Policy Council members and other mortgage servicers continue to actively participate in the HOPE NOW Alliance to reach and assist at-risk homeowners. Since mid-2007 HOPE NOW Alliance servicers have completed 506,722 permanent proprietary modifications and initiated 619,016repayment plans in the state of California.[3] Distressed homeowners have also use the Homeownership Preservation Foundation's Homeowners' HOPE hotline (888-995-HOPE), which has fielded 954,027 calls from California residents since 2008 and the hotline's non-profit counselors have completed almost 68,000 counseling sessions with homeowners in the last year and a half. HOPE NOW provides nationwide outreach to local markets and has hosted over eight homeowner preservation events in the greater Los Angeles Area since 2008. HOPE NOW has an outreach event for homeowners scheduled on for December 4 in Ontario, CA to offer homeowners the opportunity to meet in-person with a non-profit housing counselor and their mortgage servicer.

These statistics underscore the fact that recent eminent domain proposals are really unnecessary solutions in search of a problem. <u>Borrowers most in need are finding help</u>.

<u>Conclusion</u>

Our members have a shared goal of providing affordable and accessible mortgage funding to consumers. Our member companies strongly oppose any use of eminent domain to seize and restructure mortgage loans. While we recognize the significant difficulties affected counties and cities face, we believe that the use of eminent domain would reduce access to credit for borrowers, negatively impact main street investors' retirement and other savings and significantly harm mortgage finance markets. It would also likely reverse recent improvements in a number of housing indicators. In sum, the costs would far exceed any benefits.

With best wishes,

John H. Dalton

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The Housing Policy Council

Richard M. Whiting

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[3] Based on July 2012 Hope Now Alliance Survey data. Hope Now Alliance Survey is representative of 70% of the market.