



Foreclosure Crisis: Enterprise's Response

Summary

Enterprise is developing a set of program and policy responses to address aspects of the mortgage foreclosure crisis that most directly affect the communities we serve. While our capacity to directly support homeowners at risk or influence services, lenders and investors implicated in the issue is limited, we believe we can play an important role in mitigating the impact of the crisis on low-income communities where actual and potential foreclosures are heavily concentrated. Specifically, we are working in the following areas:

- Piloting initiatives for stabilizing communities with significant concentrations of foreclosed homes in key Enterprise markets;
- Exploring creation of new financing vehicles that could facilitate neighborhood stabilization strategies; and
- Developing and advocating public policies at the federal, state and local level to help communities address foreclosures at scale.

In all of these areas, Enterprise is working to mobilize other housing organizations to address the community impact dimensions of the foreclosure crisis. For example, we are leading, in partnership with the National Housing Conference and NeighborWorks America, the creation of a National Foreclosure Prevention and Neighborhood Stabilization Task Force that will coordinate foreclosure mitigation efforts and policy development.

Background on the Community Impact of Concentrated Foreclosures

The foreclosure crisis threatens not only the millions of homeowners faced with losing their homes but also the low- and moderate-income communities that will become plagued with concentrations of foreclosed properties that lenders/investors will be unable to sell during the next few years. These lender/investor foreclosed properties are known as “real estate owned” properties, or REOs, and can trigger cycles of disinvestment and abandonment.

Without innovative disposition programs and incentives for lenders/investors, these REOs will cause a significant drain on the overall community: decreased property values and tax revenue, increased blight, rise in crime, etc.

Past experience indicates that when the number of vacant homes reaches a critical mass and property values are falling, demand from potential owner-occupants can evaporate. Investor speculators typically replace the demand left by owner-occupants and formerly owner-occupied homes become rental units. Unless these trends are reversed, many of the remaining owner-occupants will eventually sell their homes, typically to investor-landlords.



Declining markets such as these tend to attract investors whose primary goal is short-term profits. Generally, investor-landlords have little invested in the broader community, which leads to landlord absenteeism and poorly maintained properties. Indeed, if the number of foreclosures forecast by the mortgage finance industry actually materializes, the existing disposition avenues (foreclosure auctions, discounted sales) will not suffice.

Enterprise wholeheartedly supports the current focus and response to the foreclosure crisis: homeownership preservation and counseling efforts. We also believe it is critical to raise awareness about the devastating impact that concentrations of vacant properties will have on low-income communities, including neighborhoods where years of concerted revitalization by Enterprise and our partners that had begun to show success may be undermined.

Enterprise's Evolving Response

Pilot Programs for Community Stabilization

We are supporting expanded use of HUD's Asset Control Area (ACA) Program, which Enterprise worked with Congress and HUD to create in the late 1990s. Through the ACA program local governments and qualified nonprofits can purchase FHA REO in bulk within designated revitalization areas at a significant discount from HUD. Enterprise currently directly administers two ACA programs: Enterprise Homeownership Partners (EHOP) in Los Angeles and in Dallas. We also invest in or support ACA programs in Baltimore, Columbus, Cleveland, New York City and Rochester. We are supporting efforts to establish new ACA programs in San Antonio and St. Louis.

While the ACA program is exclusively for FHA foreclosures, it may offer an adaptable model for addressing non-FHA-insured mortgages. We have worked intensively with senior officials from a large mortgage servicer to develop a pilot program in Dallas that could be rolled out in other cities. Our proposal is for the servicer to sell Enterprise a select number of REOs in targeted neighborhoods at a discount. Enterprise in partnership with qualified non-profits will use a combination of public subsidy and private financing to rehabilitate the properties and sell them to qualified homebuyers or manage them as affordable rental housing.

Similar discussions are underway with other REO holders. We are working with servicing and asset management divisions of those organizations to match REO properties in a select number of Enterprise markets where a broader neighborhood stabilization strategy is already underway. Ultimately, our goal is to develop a replicable model and business plan for discussions with other national private REO holders.

Potential New Financing Vehicles

We are exploring opportunities to apply our acquisition fund approach to local and state efforts in gaining control of vacant foreclosed properties for demolition, land banking or rehab. Initial expedited work is taking place in Ohio. We have met with state and local officials to discuss the creation of both a state and a separate county land bank. Enterprise, working in partnership



with national partners, would structure and manage the financing vehicle and bring in private and public subsidies in order to make the program work.

We are in early discussions with other partners to jointly create special finance tools for gaining control of vacant foreclosed properties in several targeted states. The Administration recently suggested that state and local housing agencies could play an important role in addressing foreclosures by allowing states and municipalities to temporarily broaden their tax-exempt bond programs to include mortgage refinancings.

We are examining the potential use of a shared equity mortgage product to help homeowners stay in their homes.

Developing and Advocating Public Policies

There are myriad policy proposals pending in Congress, some driven by the Administration. Major proposals are summarized in an appendix to this memorandum. As we monitor these proposals and work with other housing industry groups to help shape them, we are also driving a focused agenda that addresses community impact. Our foreclosure policy agenda includes the following recommendations:

- Consider REO property disposition toward banks' CRA responsibilities when they donate real estate to a qualified nonprofit organization or state or local agency which have the capacity to restore foreclosed/vacant properties to productive use.
- Expand the Asset Control Area program to other localities and provide additional flexibilities in the most distressed communities where there are concentrations of FHA and other privately held foreclosures, where there is capacity and where it will be a useful tool.
- Authorize a special allocation of both CDFI grant/loan funds to local CDFIs and the highly successful New Markets Tax Credit program to provide capital to qualified Community Development Entities (CDEs). The selected CDEs will be able to make loans to or investments in businesses and projects located in low-income areas that are impacted by large amounts of foreclosures. Treasury should consider providing special consideration to NMTC applications in 2008 that make such loans and investments.
- Modify the Community Development Financial Institutions Bank Enterprise Awards program to target award funds to FDIC-regulated financial institutions' activities that specifically address foreclosure prevention and/or mitigation as well as REO stabilization.



- Create a temporary “Neighborhood Stabilization Tax Credit”, akin to the NMTC or the proposed homeownership tax credit. The GO-Zone tax credit legislation that Enterprise helped to enact in response to the Gulf Coast hurricanes serves as a good model. The new credit would bring equity into cities and states with high foreclosure rates in qualified census tracts. This could be constructed as a seven-year credit to purchase and rehabilitate properties, including for-sale, rental and rent-to-own properties that are easy to use and monitor. Examples of these kinds of successful projects include Baltimore City Homes and the Cleveland Housing Network’s lease-purchase models.
- Authorize an emergency allocation of CDBG resources for the rehab/resale or rental and, when circumstances merit it, demolition of vacant properties. If the number of foreclosures forecast by the mortgage finance industry materializes, the existing disposition avenues (e.g., foreclosure auctions and discounted sales) will not suffice, and concentrations of vacant properties that lenders/investors will be unable to sell over the next few years will plague communities, driving home sales prices down and inviting crime and disinvestment.
- Reinstatement of the FHA Upfront Grants program by authorizing HUD to use the General and Special Risk Insurance Fund to provide funding for such grants. This authorization was rescinded during fiscal year 2006-2011 by the Deficit Reduction Act of 2005, which eliminated the program as mandatory. Without a mechanism for HUD to sell FHA-foreclosed multifamily properties at below market prices to preservation purchasers and provide some rehabilitation funds to these purchasers, foreclosed properties in strong markets likely will be converted to market-rate units and in weaker markets may remain vacant and a community liability.

In addition, Columbus, Ohio Mayor Michael Coleman invited Enterprise to participate in the U.S. Conference of Mayors (USCM) Mortgage Foreclosure Summit in Detroit on November 27. In his role as an executive board member of USCM and a member of a select group of mayors working to address the foreclosure issue, Mayor Coleman has asked Enterprise to work with his staff to develop a policy position paper to USCM on mortgage foreclosure and neighborhood stabilization solutions. Mayor Coleman also has invited Enterprise to co-host a future mortgage foreclosure summit in Columbus.



Appendix: Major Federal Proposals

Administration

On December 5, the Administration announced an agreement with the industry and bank regulators to freeze interest rates for certain subprime mortgages for five years. In December 3 remarks at the Office of Thrift Supervision-sponsored (OTS) Housing Forum, Treasury Secretary Paulson called on Congress to:

- **Appropriate funds for mortgage counseling in the fiscal year 2008 Transportation-HUD Appropriations bill.** The 2008 T-HUD omnibus appropriations bill includes \$230 million in funds available for housing counseling and foreclosure mitigation. The President is likely to sign the bill.
- **Pass FHA modernization legislation.** According to Paulson, the President's FHA reform proposal will lower down payment requirement, increasing the loan limit and allowing risk-based pricing, which will make affordable FHA loans more widely available. The Administration's proposed bill would help refinance another estimated 200,000 families into FHA-insured loans.
- **Enact legislation to improve the regulatory structure of the government-sponsored enterprises (GSEs).** The Administration's proposals call for a stronger independent regulator for Fannie Mae and Freddie Mac while recognizing the value that the GSEs bring to increasing the availability and affordability of mortgages.
- **Approve legislation to temporarily relieve tax liability for mortgage debt forgiveness.** The House and Senate have already passed bills to this effect, and the President has indicated he will sign the legislation.
- **Pass legislation to allow state and local governments to use tax-exempt bonds for home mortgage refinancings.** Current law allows states and localities to issue tax-exempt bonds only to assist first time homebuyers or homebuyers in designated distressed areas. Some states' housing agencies have initiated pilot programs, backed by taxable bonds, to help refinance struggling subprime borrowers into more affordable mortgages. If enacted, Paulson believes this will reduce the cost of innovative mortgage programs and allow these programs to reach more struggling homeowners.

On December 18, the Federal Reserve is expected to adopt proposed rules under regulatory authority established by the Home Ownership Equity Protection Act of 1994 (HOEPA), which would establish new subprime loan practices and help prevent predatory lending. More specifically, the proposed rules would:

- Restrict lenders from penalizing certain subprime borrowers — those with tarnished credit or low incomes — who pay off their loans early. The restriction would apply to



loans that meet certain conditions, including that the penalty expire at least 60 days before any possible payment increase.

- Force lenders to make sure that subprime borrowers set aside money to pay for taxes and insurance.
- Bar lenders from making loans when they don't have proof, or verification, of a borrower's income.
- Prohibit lenders from engaging in a pattern or practice of lending without considering a borrower's ability to repay a home loan from sources other than the home's value.

The Fed is also considering a variety of other related proposals, such as:

- Requiring financial disclosures to borrowers early enough to use while shopping for a mortgage. Lenders could not charge fees — except for a fee to obtain a credit report — until after the consumer receives the disclosures.
- Prohibiting certain types of misleading or deceptive advertising for certain loans.
- Require that all applicable rates or payments be disclosed in ads with equal prominence as advertised introductory, or “teaser” rates.
- Barring lenders from paying mortgage brokers a fee that exceeds the amount the would-be borrower had agreed to in advance that the broker would receive.
- Ban certain mortgage practices, such as failing to credit a mortgage payment to a borrower's account when the company servicing the mortgage receives it, or prohibiting a broker from coercing or encouraging an appraiser to misrepresent the value of a home.

The proposed rules are expected to be finalized later this year.



Congress

Congress – mainly the House of Representatives – has recently increased their efforts to approve legislation intended to mitigate the current mortgage foreclosure crisis. The following sums up several relevant bills that are at various stages in the legislative process.

Predatory Lending

On November 15, the House passed the Mortgage Reform and Anti-Predatory Lending Act of 2007, H.R. 3915. The bill establishes a minimum standard for all mortgages directing that borrowers must have a reasonable ability to repay; attaches limited assignee liability to secondary market entities that securitize loans beyond this standard; requires licensing and registration of mortgage originators, including brokers and bank loan officers; expands and enhances consumer protections for “high-cost loans” under the Home Ownership and Equity Protection Act; and requires successor owners of foreclosed properties to honor preexisting leases.

On December 12, Senate Banking Committee Chairman Christopher Dodd (D-CT) introduced the Senate companion bill, the Homeownership Preservation and Protection Act, S. 2452, which would establish new protections for all borrowers, provide new protections for subprime borrowers and borrowers who get nontraditional mortgages, establish strong remedies to make sure these standards are met, and provide for limited liability for holders of a mortgage made in violation of law, whether it is the original lender or a subsequent investment trust. It is unclear whether or when the Banking Committee will act on the bill.

Bankruptcy Legislation

Also on December 12, the House Judiciary Committee reported the Emergency Home Ownership and Mortgage Equity Protection Act of 2007, H.R. 3609, introduced by Rep. Brad Miller (D-NC). The bill repeals a provision that prohibits a bankruptcy court from modifying a home mortgage, but allows a bankruptcy court to modify any other secured debt, including mortgages on other properties.

On December 5, the Senate Judiciary Committee held a hearing on the Senate companion legislation, the Helping Families Save Their Homes in Bankruptcy Act, S. 2136, introduced by Sen. Richard Durbin (D-IL). It is unclear whether or when the Judiciary Committee will act on the bill.

FHA Modernization

Congress is moving on FHA legislation that will make more families eligible for FHA mortgages, which has an additional positive feature as they require HUD to devote its attention to counseling and affordability for FHA mortgagees. On September 18, the House passed its FHA modernization bill, H.R. 1852, which would increase FHA loan limits; authorize zero and lower down payment and 40-year loan products; and allow HUD to base mortgage insurance premiums on borrower credit risk.



On December 14, the Senate passed its own less expansive version of FHA modernization, S. 2338. The differences between the two bills, including whether revenue generated by removing the cap on FHA reverse mortgages will be set-aside for a National Affordable Housing Trust Fund, will need to be resolved during conference negotiations conducted early next year.

Mortgage Debt Forgiveness

On October 4, the House passed the Mortgage Forgiveness Debt Relief Act of 2007, H.R. 3648. The bill permanently eliminates the tax on mortgage debt forgiven by lenders as part of a mortgage restructuring or foreclosure on a borrower's primary residence. The legislation applies to debt forgiven since January 1, 2007 and going forward and is limited to mortgages that do not exceed \$2 million. The bill would also extend the deductibility of mortgage insurance premiums, and would restrict capital gains tax benefits available to people who buy second homes and later convert them to principal residences.

After holding a December 13 hearing on the subprime crisis, during which mortgage debt cancellation legislation and the administration's proposal to allow state and local HFAs to use tax-exempt bond proceeds to refinance mortgages was discussed, the Senate largely adopted most of H.R. 3648, making slight revisions and adding a few other provisions on December 14. The House is expected to pass the Senate version of H.R. 3648 on December 18, and the President will likely sign it soon thereafter.

Housing Counseling

On December 17, the House passed the FY 08 Appropriations omnibus bill, H.R. 2764, which provides FY 08 funding for all discretionary accounts except defense. It includes \$50 million in housing counseling funding (which is a set-aside in the HOME account) – an increase from \$42 million in FY 07 – and \$180 million to the Neighborhood Reinvestment Corporation (a.k.a. NeighborWorks America) in new foreclosure mitigation funding targeted to help borrowers in danger of foreclosure. The Senate is likely to pass the bill soon (with housing funding levels unchanged), and the President has indicated that he will sign the omnibus.