



CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

February 23, 2009

H.R. 200 **Helping Families Save Their Homes in Bankruptcy Act of 2009**

As ordered reported by the House Committee on the Judiciary on January 27, 2009

SUMMARY

H.R. 200 would authorize bankruptcy courts to modify the terms of some mortgages on principal residences during Chapter 13 bankruptcy proceedings. CBO estimates that enacting H.R. 200 would reduce direct spending (in the form of increased offsetting receipts) by \$31 million over the 2009-2019 period and increase revenues by \$23 million over the same time period, thus reducing future budget deficits over this period by a total of \$54 million. Based on information provided by the Administrative Office of the United States Courts (AOUSC), CBO estimates that any additional discretionary costs to adjudicate more bankruptcy cases would not be significant; such costs would be subject to the availability of appropriated funds. The judiciary currently spends about \$900 million a year for all bankruptcy activities.

The effects on direct spending over the 2009-2013 and 2009-2018 periods are relevant for enforcing the House's pay-as-you-go rule under the current budget resolution. CBO estimates that enacting H.R. 200 would reduce direct spending by \$26 million over the 2009-2013 period and by \$31 million over the 2009-2018 period. Enacting H.R. 200 would increase revenues by \$18 million over the 2009-2013 period and \$23 million over the 2009-2018 period.

H.R. 200 would impose intergovernmental and private-sector mandates, as defined in the Unfunded Mandates Reform Act (UMRA), on certain creditors, including state and local pension funds and housing agencies. Because of uncertainty about the number of bankruptcy plans that would be modified as a result of this legislation and how those changes would affect holders of secured claims, CBO cannot determine whether the aggregate cost of complying with the mandates would exceed the annual thresholds for

intergovernmental or private-sector mandates (\$69 million in 2009 and \$139 million in 2009, respectively, adjusted annually for inflation).

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The costs of this legislation fall within budget function 750 (administration of justice.)

	By Fiscal Year, in Millions of Dollars											2009-	2009-
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2014	2019
CHANGES IN DIRECT SPENDING													
Estimated Budget Authority	-4	-9	-6	-4	-3	-1	-1	-1	-1	-1	*	-27	-31
Estimated Outlays	-4	-9	-6	-4	-3	-1	-1	-1	-1	-1	*	-27	-31
CHANGES IN REVENUES													
Estimated Revenues	3	6	4	3	2	1	1	1	1	1	*	19	23

Note: * = less than \$500,000.

BASIS OF ESTIMATE

For this estimate, CBO assumes that H.R. 200 will be enacted near the middle of fiscal year 2009.

H.R. 200 would allow bankruptcy courts to modify the terms of some mortgages for a primary residence during Chapter 13 bankruptcy proceedings. (This type of bankruptcy, often referred to as “reorganization,” involves a repayment plan that sets forth how debts will be settled.) Under current law, Chapter 13 halts mortgage foreclosure proceedings, thus giving homeowners an opportunity to restructure their financial arrangements. Bankruptcy courts can establish a payment plan for overdue mortgage payments on primary residences but cannot change the amount, timing, or interest rate terms of mortgage payments. In 2008, about 354,000 cases were filed for Chapter 13 bankruptcy, a 14 percent increase over the number filed in 2007.

H.R. 200 would apply to Chapter 13 cases filed before, on, or after the date of enactment, but would limit which debtors would qualify for a loan modification under the bill. First, the debtor’s mortgage would have to be initiated prior to the effective date of the bill and subject to a notice of foreclosure. Second, H.R. 200 would not apply to debtors with

loans guaranteed by the Federal Housing Administration, the Department of Veterans Affairs, or the Department of Agriculture.

Finally, the bill would require debtors to inquire about loan modifications with their mortgage servicer. Specifically, after the 15-day period beginning on the date of enactment, a mortgage modification may be proposed under Chapter 13 only if the debtor attempted to contact the mortgage servicer regarding a loan modification at least 15 days before filing for bankruptcy relief (this rule would not apply in cases where a foreclosure sale is scheduled to occur within 30 days of the date of the bankruptcy filing). For pending Chapter 13 cases, the debtor would have to certify that the debtor attempted to contact the mortgage holder about a loan modification. The bill would expand Chapter 13 eligibility by excluding home mortgage debt when determining if the debtor qualifies to file for Chapter 13, under certain circumstances.

The bill also would constrain the debtor's profit from a home sale in certain cases. H.R. 200 would require a debtor to share the net proceeds of a home sale with the lender, if the sale occurs within the first four years of the debtor completing a Chapter 13 plan. The amount the lender would receive would be 80 percent of the net profit in the first year, and then decline to 20 percent by the fourth year.

Impact on Bankruptcy Filings. Bankruptcy filings fluctuate over time and are dependent on economic trends and personal financial conditions. Between 1987 and 2008, Chapter 13 filings have ranged from a low of 140,000 in 1987 to a high of 470,000 in 2003. The primary reason that individuals file for Chapter 13 is to forestall foreclosure on their home—over 96 percent of Chapter 13 filers are homeowners and 70 percent of filers propose a plan to repay overdue mortgage payments. Because of the high number of foreclosures expected over the next several years (several million, based on information provided by the Center for Responsible Lending), CBO expects that bankruptcy filings will substantially increase in the near term—without enactment of H.R. 200. Under current law, based on information provided by the AOUSC, CBO estimates that Chapter 13 filings are likely to increase to almost 400,000 in 2009, a 13 percent increase over the number in 2008.

Economists and bankruptcy experts have found that the greater the financial benefit gained from filing for bankruptcy, the greater the likelihood a household will file. CBO expects that the financial benefit to filing under the bill would be greater than under current law. Based on an analysis of similar proposals to allow loan modification in Chapter 13, CBO estimates that over one million households would benefit financially from filing for Chapter 13 bankruptcy under the bill.

Studies analyzing household's decision to file for bankruptcy indicate that of those households that could realize a financial benefit from filing for bankruptcy, only a fraction actually make the decision to file. Of the over one million households that could benefit from filing for bankruptcy under the legislation in the next few years, we estimate that about 350,000 additional households would file for bankruptcy over the 2009-2019 period, with about two-thirds of those filings occurring within the first three years after enactment.

The number of additional bankruptcy filings that would occur under the bill is, however, very uncertain. Some bankruptcy experts believe that filings would not increase substantially under H.R. 200 because the current fees and legal costs associated with filing for bankruptcy are high; the Government Accountability Office (GAO) reports that the median cost for filing Chapter 13 bankruptcy is \$3,000. In the short term, new filings also might be limited by the supply of experienced bankruptcy lawyers who can handle additional filings. Further, some industry specialists maintain that the bill would encourage voluntary modification of mortgages outside of bankruptcy because many mortgage holders would prefer to work out their own arrangements rather than be subject to those imposed by a bankruptcy court. Other experts, however, contend that Chapter 13 filings would increase significantly as legal, tax, accounting, and payment concerns would deter voluntary modifications. Accordingly, debtors might view Chapter 13 modification as the best option for retaining their homes. Finally, whether significant numbers of debtors would be driven to seek bankruptcy protection by the prospect of mortgage relief might ultimately depend on how bankruptcy courts responded to the new authority that would be provided by H.R. 200.

Budgetary Impact of Additional Bankruptcy Filings. Additional filings would increase collections of bankruptcy fees. Those fees (\$235 per Chapter 13 filing) are distributed among several government entities. About half of the amount collected is used to cover the judiciary's and U.S. Trustees' added costs and thus has no net effect on federal spending. A portion of those filing fees, however, is recorded as an offsetting receipt (a credit against direct spending) in the federal budget and deposited into a special fund in the Treasury; those amounts are not available for spending unless provided in an appropriation act. CBO estimates that enacting the legislation would increase such offsetting receipts by \$31 million over the 2009-2019 period.

Revenues. Another portion of Chapter 13 filing fees is deposited into the general fund of the Treasury and recorded as increased revenues. CBO estimates that enacting H.R. 200 would increase such revenues from additional Chapter 13 filing fees by \$23 million over the 2009-2019 period.

Potential Budgetary Impact on the Government-Sponsored Enterprises for Housing. Enacting H.R. 200 could affect the value of the financial instruments (mortgages and mortgage-backed securities) held or guaranteed by the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac)). These government-sponsored enterprises (GSEs) were placed in conservatorship in 2008 and are under the direct control of the federal government. CBO considers the GSEs' operations to be part of the federal budget. Enacting H.R. 200 could change the value of those financial instruments and thus affect the federal budget. It is unclear, however, whether enactment of the legislation would increase or decrease future costs for the GSEs.

Losses resulting from mortgages held by the GSEs are shouldered by those entities. Modifying loans in bankruptcy might be more or less costly compared to foreclosure and would depend on future house prices, the length of time needed to sell foreclosed properties, the terms of potential mortgage modifications, the likelihood of re-default for modified loans, and the amount mortgage payments might be reduced in the bankruptcy process. Similar uncertainty exists for the impact of H.R. 200 on the value of mortgage-backed securities guaranteed and held by the GSEs.

INTERGOVERNMENTAL AND PRIVATE-SECTOR IMPACT

H.R. 200 would impose intergovernmental and private-sector mandates, as defined in UMRA, on certain creditors, including state and local pension funds and housing agencies. The bill would allow bankruptcy judges to modify the rights of holders of certain claims on mortgage debt by making changes to the terms of home mortgage agreements during bankruptcy proceedings. Under current law, bankruptcy judges are prohibited from changing the terms of loans for primary residences. The bill also would require such claimholders to file timely notice with the court before adding fees, costs, or charges while a bankruptcy case is pending.

The costs of those mandates would depend on the number of mortgage agreements that judges would choose to modify and how those changes would affect the value of secured claims. The amount recovered by a claimholder through a bankruptcy proceeding relative to the amount that could be recovered through foreclosure would vary depending on market conditions. In some cases, claimholders might not incur any additional costs. Because of those uncertainties, CBO cannot determine whether the aggregate cost of complying with the mandates in the bill would exceed the annual thresholds for intergovernmental or private-sector mandates (\$69 million in 2009 and \$139 million in 2009, respectively, adjusted annually for inflation).

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