THE FORECLOSURE CRISIS AND CALIFORNIA

A report by the staff of U.S. Senator Barbara Boxer

"The foreclosure crisis is having a dramatic impact across the country. California, which saw some of the greatest increases in housing prices in recent years, is at the center."

– U.S. Senator Barbara Boxer (D-CA), leading a roundtable discussion in Riverside, California on January 11, 2008

INTRODUCTION:

On January 10-11, 2008, Senator Boxer and her senior staff hosted a series of five roundtable discussions in California regarding the home foreclosure crisis, its impact on our local communities, and legislative action and other steps needed to help our families. The roundtables — which took place in Stockton, Riverside, Pittsburg, San Diego, and Fresno — were attended by local elected officials, government representatives at the federal, state, and local levels, community organizations and service providers in the housing industry, Fannie Mae, lenders, brokers, and realtors.

BACKGROUND ON THE FORECLOSURE CRISIS:

Following nearly a decade of exponential growth in the housing market, the laws of gravity have returned and we are now facing one of the biggest financial crises of the past half century. Declining home values and sharp interest rate resets have combined to drive foreclosures to record levels, and the losses to homeowners, communities, and investors are threatening to throw the economy into recession. In the third quarter of 2007, RealtyTrac, which monitors U.S. real estate activity, reported 635,159 foreclosure filings — default notices, auction sale notices and bank repossessions — on 446,726 properties nationwide, a rate of one filing for every 196 U.S. households and an increase of nearly 100 percent from the third quarter of 2006.

As a result of these foreclosures and the tightening of available credit, residential investment and construction spending are dropping, as is consumer spending, due to decreased home equity wealth. The ripple effect of this crisis is such that all levels of government are bracing for huge shortfalls due to the loss of taxable income and reduced property values.

Many believe the worst is still yet to come—the Center for Responsible Lending (CRL) has estimated that as many as 2.2 million subprime home loans made in recent years have already failed or will end in foreclosure – more than 460,000 of those in California alone – and that one out of five subprime mortgages originated during the past two years will end in foreclosure.

IMPACT ON CALIFORNIA:

California, which saw some of the greatest increases in housing prices, is being hit particularly hard by the foreclosure crisis. Of the metropolitan areas with the highest foreclosure activity in July through September of 2007, five of the top 10 are in California: Stockton, Riverside/San Bernardino, Sacramento, Bakersfield, and Oakland. Fresno and San Diego also place in the top 20.

In the third quarter of 2007, California reported 148,147 foreclosure filings -- the highest number of any state. California had the second highest foreclosure rate in the country, with one filing for every 88 households, easily exceeding the previous foreclosure peak set in 1996.

In part due to the crisis, California is facing a $14.5 billion budget shortfall and tens of billions of dollars in lost economic growth. At a local level, according to a report by the US Conference of Mayors, California cities may see a decline in collected property, sales, and transfer taxes of nearly $4 billion. Meanwhile, the Center for Responsible Lending projects that foreclosures will cost Californians a total of $67 billion in lost property values – an average individual property value loss of more than $8,000.

ROUNDTABLE DISCUSSIONS:

The first roundtable was held in Pittsburg on January 10th and attended by participants from across Contra Costa County, where one in every 80 households is in some stage of foreclosure.

On January 11th, roundtables were held in Stockton, which has the highest rate of foreclosure filings in the nation, with one foreclosure filing for every 33 households; Riverside, which ranked third in the nation with one foreclosure filing for every 43 households; Fresno, which ranked 13th with one foreclosure filing for every 79 households; and San Diego, which ranked sixteenth with one foreclosure filing for every 91 households.

While each roundtable was unique, there were several themes consistent throughout the discussions. Local governments, nonprofit service providers, and even lenders were all overwhelmed by the magnitude of the problem, and all were fearful that the situation is only getting worse.

Here is what we heard:

- ***Need for More Counseling and Legal Assistance:*** Housing and credit counselors reported high rates of success when able to work with troubled borrowers. However, as the number of homeowners facing foreclosure increases, counselors have been unable to keep up with demand, are in need of additional training, and are experiencing high turnover rates. Moreover, as counselors are diverted to help homeowners facing foreclosure, there are far fewer available to assist prospective homeowners. There is also an urgent need for more attorneys to assist with loan modifications and bankruptcy.

- ***Need for More Loan Modifications:*** Despite both a state and national plan by lenders to help at-risk borrowers, efforts to negotiate loan modifications on a case by case basis have been nearly a complete failure. Counselors complained that lenders, including those participating in the Governor's plan, are unresponsive to their requests and they are unable to reach those with decision-making authority. Meanwhile, homeowners willing to sell their homes at a loss have had to wait months for lender approval, by which time prospective buyers have come and gone. The Commissioner of the California Department of Corporations reported that servicers have hired more loss mitigation staff but that they are not keeping up with the increased number of open files.

- ***Declining Revenues and Increased Blight:*** Local governments are faced with sharp drops in property taxes and development fees collected, while unemployment in the construction and financial sectors is spiking. At the same time there is great concern about the number of vacant properties that are becoming magnets for vandalism and crime. To address this latter problem, several communities have passed ordinances requiring lenders to maintain foreclosed properties or face stiff penalties.

- ***Renters at Risk:*** The number of tenants in investor-owned properties affected by the crisis is also on the rise. Many renters are unaware that the homes they are living in or moving into are already in foreclosure, and that the owner may be collecting rent but not paying the loan. This problem has been seen even among Section 8 properties, where tenants who already are facing economic hardships and instability are being kicked out of their rental homes.

- ***Need for Greater Fraud Prevention:*** Fraud and deception were at the root of many of the problem loans that are now going bad, and fraud, in the form of phony counselors and others offering assistance – for a fee – is at play as homeowners become desperate for solutions.

  Minority communities were targeted for most subprime loans and many signed documents in English that they did not understand and that frequently listed different terms than what they had been told in their primary language. In addition to addressing language concerns, participants called for tougher and more consistent licensing requirements for loan originators and for greater enforcement.

- ***Need for Increased Loan Limits:*** Lenders, brokers, and realtors, along with government officials were unanimous in their calls for an increase in the loan limits for Fannie Mae, Freddie Mac, and the Federal Housing Administration. The use of FHA loans has all but disappeared in California and an increase is essential so that Californians and the residents of other high cost areas can benefit from these programs.

LEGISLATION PASSED AND SIGNED INTO LAW:

Congress has already taken the following action to address the foreclosure crisis:

- **HUD Counseling and Loss Mitigation Activities:** The FY2008 Omnibus Appropriations Act signed into law on December 26, 2007 provided $230 million to HUD for a NeighborWorks program to provide grants to public and non-profit housing groups to assist those in default or at risk of foreclosure.

- **Mortgage Forgiveness Debt Relief Act of 2007:** Signed into law on December 20, 2007, the Act provides three years of tax relief for families whose banks have forgiven debt on their home loans. This will ensure that those families already unable to meet their mortgages avoid incurring large tax bills as well.

SENATOR BOXER'S 15-POINT FORECLOSURE CRISIS ACTION AGENDA

As Congress reconvenes this month, there will be opportunities for legislative action to address the foreclosure crisis, including crafting comprehensive legislation targeted to address California's needs. As Congress and the Administration work together to develop an Economic Stimulus package, key congressional committees are also scheduled to hold hearings and consider additional legislation to address the foreclosure crisis. There are also immediate steps that can be taken that do not require congressional or White House approval.

ONGOING WORK IN CALIFORNIA:

- Turn foreclosure roundtables into ongoing community working groups to address the crisis in the months and years ahead.

- Ensure that new Department of Housing and Urban Development (HUD) funding for counselling reaches California communities quickly and effectively and that HUD and the Federal Housing Administration (FHA) are working to ensure that California borrowers are able to access their full range of products and services.

- Work closely with the HOPE NOW coalition and major California lenders and servicers to ensure they live up to the commitments they have already made to freeze interest rates and speed up the review and modification process. HOPE NOW is an alliance of counselors, investors, lenders, and servicers that is working to maximize outreach efforts to homeowners in distress.

LOAN MODIFICATIONS:

- Congress should immediately explore initiatives that would freeze interest rates for borrowers in danger of foreclosure.
- Allow bankruptcy judges to modify unaffordable mortgages on a homeowner's primary residence, the same power judges already have for vacation homes or investment property.
- Insist that the U.S. Federal Reserve and the Office of Thrift Supervision require Bank of America and Countrywide Financial to demonstrate significant progress in modifying loans as a condition of approving their merger.

CONGRESSIONAL ACTION:

- Advocate new CDBG funds for the purchase and rehabilitation of foreclosed properties. Funds should go to local governments in the most affected areas and could be used to maintain or purchase foreclosed homes in order to preserve and protect our communities.
- Advocate additional funding for nonprofits to help existing and future borrowers by providing foreclosure prevention activities, including counseling and legal services, training and capacity building, and pre-purchase counseling for all subprime loans.
- Advocate for the higher loan limits for FHA, Fannie Mae and Freddie Mac qualifying loans. The Senate-passed FHA modernization bill would raise FHA loan limits from the current $362,790 up to a maximum of $417,000, while the House-passed bill would allow for FHA loans up to nearly $830,000.
- Expand the FTC's enforcement authority to cover unfair and deceptive acts and practices committed by federally chartered depository institutions, which are currently governed by the federal financial regulators. FTC already has enforcement authority over non-depository institutions.
- Support local government requirements that lenders maintain foreclosed properties.
- Establish licensing and registration requirements for all loan originators and provide funding for anti-fraud enforcement activities.
- Request a GAO study on different options to establish a land trust to purchase the land beneath foreclosed properties and allow existing structure to be resold to homeowners at reduced price.
- Require that homeowners be notified whenever their loan is sold so that the holder of the loan can be easily identified and contacted.
- Provide funding for and encourage high school financial literacy programs.