Metropolitan Policy Program
at BROOKINGS

RESTORING PROSPERITY INITIATIVE FROM THE METROPOLITAN POLICY PROGRAM AT BROOKINGS

Tackling the Mortgage Crisis: 10 Action Steps for State Government

Alan Mallach[1]

“Although most media attention has focused on the role of the federal government in stemming this crisis, states have the legal powers, financial resources, and political will to mitigate its impact.”

The mortgage foreclosure crisis has become an issue of growing concern over the past two years, one without easy remedies. While most attention has focused on what the federal government should do to manage the fallout, states, too, play a vital role in the process. This paper describes how the mortgage crisis came to be, and the damage it has so far inflicted. It then provides a set of concrete action steps that states can take to mitigate its impact on families and neighborhoods—and prevent a similar situation from occurring in the future.

Introduction

During 2006, the United States saw a considerable upswing in the number of new mortgage defaults and foreclosure filings. By 2007, that upswing had become a tidal wave. Today, national homeownership rates are falling, while more than a million American families have already lost their homes to foreclosure. Across the country, boarded houses are appearing on once stable blocks. Some of the hardest hit communities are in older industrial cities, particularly Midwestern cities such as Cleveland, Detroit, and Indianapolis.[2]

Although most media attention has focused on the role of the federal government in stemming this crisis, states have the legal powers, financial resources, and political will to mitigate its impact. Some state governments have taken action, negotiating compacts with mortgage lenders, enacting state laws regulating mortgage lending, and creating so-called “rescue funds.” Governors such as Schwarzenegger in California, Strickland in Ohio, and Patrick in Massachusetts have taken the lead on this issue. State action so far, however, has just begun to address a still unfolding, multidimensional crisis. If the issue is to be addressed successfully and at least some of its damage mitigated, better designed, comprehensive strategies are needed.

This paper describes how state government can tackle both the immediate problems caused by the wave of mortgage foreclosures and prevent the same thing from happening again. After a short overview of the crisis and its effect on America’s towns and cities, the paper outlines options available to state government, and offers ten specific action steps, representing the most appropriate and potentially effective strategies available for coping with the varying dimensions of the problem.

1 The Origins and Extent of the Crisis

The foreclosure crisis facing the United States today did not come out of nowhere. It is the outcome of policy choices and private decisions dating back more than a decade. Above all, it arose from the creation of the subprime lending industry that emerged from changes in the financial world during the 1990s. Although a full description of that industry and its rise and fall would fill a book, a short overview will set the context for this paper.

The Rise and Fall of Subprime Lending

The idea behind subprime lending is a simple one. Historically, homebuyers needed good credit before lenders would offer a mortgage. These mortgages were made available at a single or "prime" interest rate, with only modest variations. The subprime lending industry emerged to provide loans to borrowers with poor credit who could not qualify for prime loans. Based on the proposition that these borrowers are higher risk, subprime loans carry higher interest rates than prime loans.[3] This industry would not have grown, however, were it not for dramatic changes in the financial world, including:

- Growth of credit scoring based on financial models; this allowed firms such as Fair Isaac and Co. (FICO) to devise single credit scores for borrowers, which claimed to predict the risk of making a loan to the borrower;
- The uncoupling of home lending from the thrift and banking sectors through bank consolidation and restructuring, and the growth of independent mortgage companies and brokers;
- Securitization of mortgage debt by Wall Street firms, which created investment pools by bundling mortgages together and selling them on worldwide capital markets to investors; and
- The all but insatiable demand from investors for higher yield investments, demand that was unmet as a result of low, long-term interest rates worldwide on traditional investment vehicles.

Since the 1990s, mortgage brokers have packaged mortgages for the financial institutions that provide the funds. Those institutions in turn bundled mortgages together, selling them to Wall Street investment banks, which aggregated them into marketable securities and sold them in shares to investors.[4] The investment bankers hired trustees to hold the funds and other firms, known as servicers, to manage the mortgages in the pool on behalf of the investors. These servicers play a critical role in the foreclosure crisis.

In theory, this was a rational system. In practice, however, there was a great deal wrong with it. The notion that, instead of avoiding risk, one could simply raise the cost on the basis of the risk involved, coupled with the demand for high-yield investments, set off a race among brokers and lenders to create the most mortgages at the highest possible interest rates. This was encouraged by lender's use of Yield Spread Premiums, which gave brokers higher commissions for making higher interest, riskier loans.

To meet demand from investors for still higher yields, brokers and lenders came up with increasingly ingenious ways to qualify more buyers and make more loans. They offered adjustable rate mortgages (ARMs) with "exploding" interest rates, which started out with a low introductory or "teaser" rate that later skyrocketed, usually after two years. Another product was "no doc" loans, mortgages made without requiring borrowers to document their income or other obligations, at even higher interest rates. Other "exotic" mortgages included negative amortization mortgages and so-called Option ARMs, a form of adjustable rate mortgage in which borrowers could choose—within certain bounds—how much or how little to pay on their mortgage each month. All carried interest rates far above what prime lenders charged customers with better credit. After 2003, greater numbers of subprime loans were either

ARMs, no-doc loans, or other exotic loans. In fact, 92 percent of all securitized subprime mortgages originated in 2006 were adjustable rate mortgages.[5]

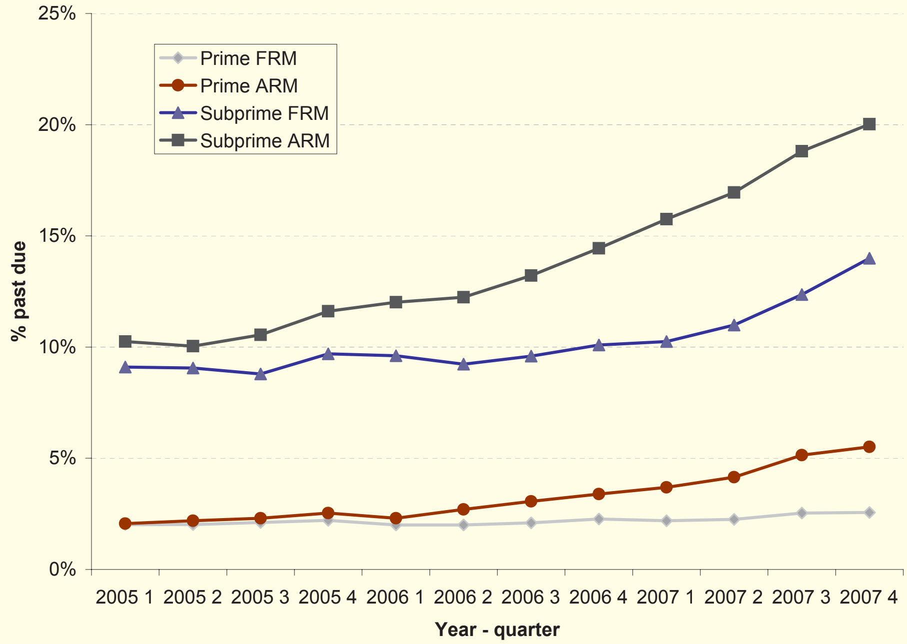
A second way of generating more business was encouraging homeowners to refinance. Aggressively marketing their products to elderly or lower-income homeowners in urban neighborhoods and taking advantage of their lack of sophistication, subprime lenders made millions on refinancing loans, sometimes refinancing the same house repeatedly. Many subprime lenders steered borrowers, often black or Latino families, into high-cost mortgages when they could have qualified for less expensive loans. Estimates suggest that between 30 percent and 50 percent of all subprime borrowers could have qualified for less expensive loans.[6]

Arguing that they were "democratizing credit," subprime lenders encouraged millions of borrowers to assume loans that they would most likely be unable to repay. Although warning voices were heard early, the federal government hoped to increase the number of low-income and minority homeowners, and Federal Reserve Chairman Alan Greenspan was philosophically opposed to regulation.[7] So long as home prices were rising in most states, which was the case through 2005, most borrowers had enough equity to enable them to sell their home or refinance their homes should they be unable to make their payments. Meanwhile, the number of subprime loans kept growing. By 2006, they represented more than one of every four new mortgage loans.

By the end of 2006, when the housing bubble burst, lenders had made more than 15 million subprime loans. More than one-half of those were outstanding, the balance having been refinanced or foreclosed.[8] Millions of these were ARMs, whose low introductory interest rates were beginning to reset to much higher rates. With home prices falling, borrowers could no longer extricate themselves from unaffordable loans. The resulting foreclosure wave was all but inevitable, hitting particularly hard in many urban areas, where more than one-half of new mortgage loans were subprime loans.[9]

Although the first wave of defaults was concentrated among the most questionable loans, as the crisis deepened, foreclosure rates began rising among other mortgages as well, including fixed-rate subprime mortgages and the so-called Alt-A mortgages, an intermediate category between subprime and prime loans. By 2007, delinquencies among fixed-rate subprime loans and prime adjustable-rate loans were also rising rapidly.

FIGURE 1: Share of Loans Past Due by Mortgage Type, 2005-2007



Source: National Delinquency Survey, Mortgage Bankers Association

In short, although many factors contributed to the foreclosure crisis, including fraudulent behavior by some mortgage brokers and appraisers and deceptive or irresponsible behavior by some borrowers, the roots of the problem lie not in a handful of bad apples, but in the internal dynamic of an industry that disconnected the process of mortgage making from properties, and, driven by pressure from the global investment industry, made ever-riskier mortgages at ever-higher interest rates. When thinking about alternative courses for state government action, it is important to bear that point in mind.

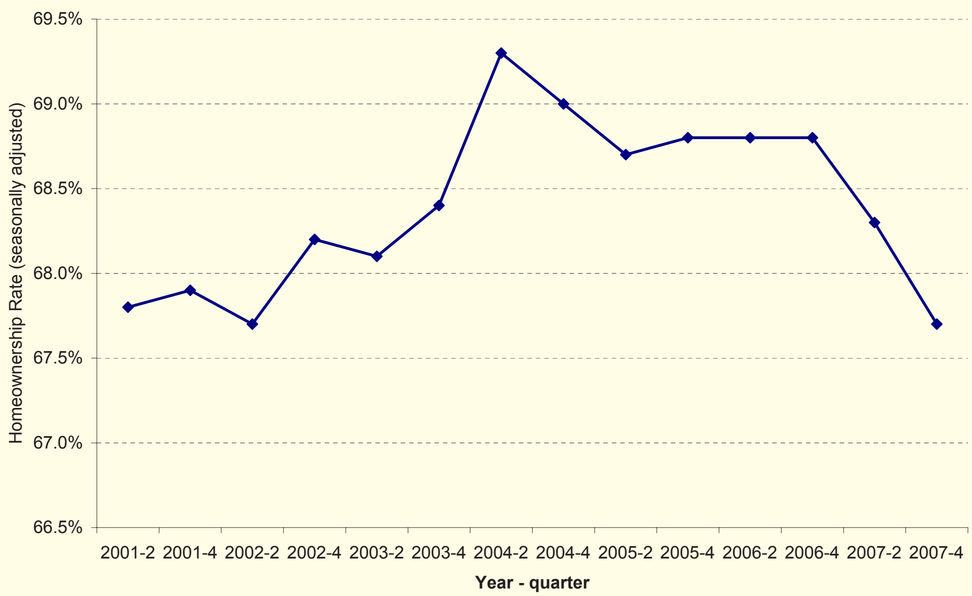
The Impact of the Foreclosure Crisis

The subprime foreclosure crisis sent ripples throughout the world economy. As foreclosures rose and housing prices fell, more than 200 mortgage lenders closed their doors.[10] The survivors are tightening credit, further depressing the housing market and affecting credit markets worldwide. The most devastating effects, however, are not on investment bankers and lenders but on the homeowners who took out subprime loans, and on the neighborhoods where they live, or once lived.

In 2006, there were 1.2 million foreclosure filings in the United States. That number grew to 2.2 million in 2007, and involved 1.3 million properties.[11] The great majority of foreclosure filings lead to foreclosures.[12] These filings are heaviest in the subprime market generally, and in subprime ARMs in particular. In the fourth quarter of 2007 alone, one in 19 subprime ARMs were in foreclosures filing. Although subprime ARMs accounted for less than 7 percent of all mortgages, they represented 42 percent of foreclosure starts during the quarter.

Many people in both the public and private sectors supported the growth of subprime lending because they believed it was opening the doors to greater homeownership by people who had been barred from achieving that dream. In reality, fewer than one in ten subprime loans were to first-time homebuyers. As the Center for Responsible Lending has shown, the cumulative effect of subprime lending has been to *reduce* the total number of homeowners in the United States.[13] Between the fourth quarter of 2006 and that of 2007, the number of American homeowners dropped by 600,000, despite an overall increase of nearly one million new households. As a result, by the fourth quarter of 2007, homeownership rates had fallen from their 2004 peak to 2001 levels. The number of renters, meanwhile, increased by more than 1.5 million.[14]

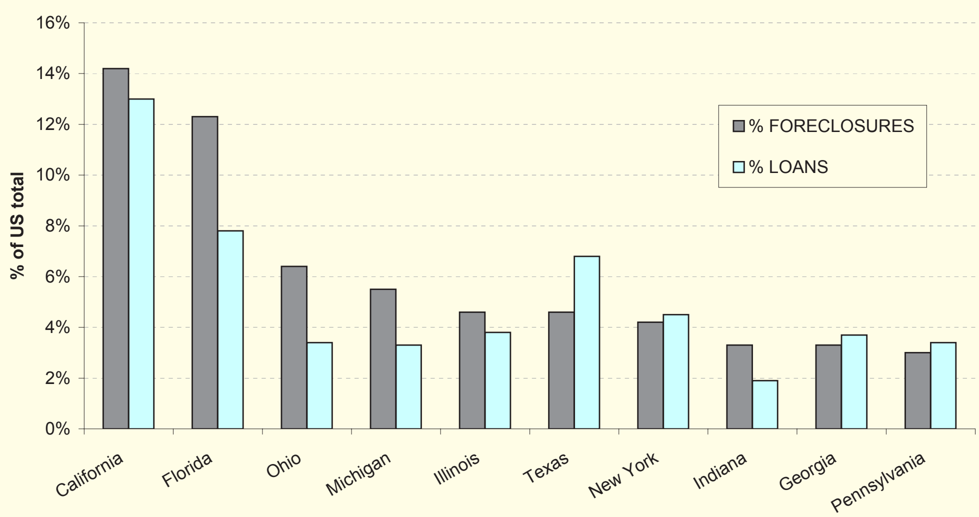
FIGURE 2: U.S. Homeownership Rate, 2001-2007



Source: U.S. Bureau of the Census

This crisis is most pronounced in the sunbelt states and in the states of the old industrial rust belt. Of the top ten foreclosure states in 2007, five are states with concentrations of older industrial cities: Ohio, Michigan, Indiana, New York, and Pennsylvania. By the end of 2007, nearly one of every eight mortgages of all types in Indiana, Michigan, and Ohio was either in foreclosure or past due on payments—and more than two of every five subprime ARMs in those states was either in foreclosure or past due. One in 28 mortgages and nearly one in five subprime ARMs in those three states was already in foreclosure.[15] As Figure 3 shows, these three states have a much higher ratio of foreclosures to loans than other states (with the notable exception of Florida), reflecting the extent to which their economic distress has affected their foreclosure rate.

FIGURE 3: Ten States with Largest Foreclosure Inventory by Share of U.S. Loans and Foreclosures, 4th Quarter 2007



Source: National Delinquency Survey, Mortgage Bankers Association

Within these states, the crisis is heavily concentrated among blacks and Latinos and in those urban neighborhoods and modest suburbs where struggling, working-class families were most likely to own or buy homes. In 2006, more than one-half of all the mortgages made to black families and 40 percent of the those made to Latinos were subprime, compared with only 22 percent among white borrowers. In many urban neighborhoods with populations that were predominantly minority, 60 to 70 percent of the mortgage loans made in recent years have been subprime loans.[16]

Foreclosure can be shattering on many levels. In the short term, families are forced to move, disrupting their lives and their children's schooling. They also lose both their money and their principal asset and see their credit tarnished. Their chance to buy another home in the future is also diminished. All told, the emotional and physical stress of foreclosure coupled with the failure to attain such a fundamental touchstone of American success can be devastating.

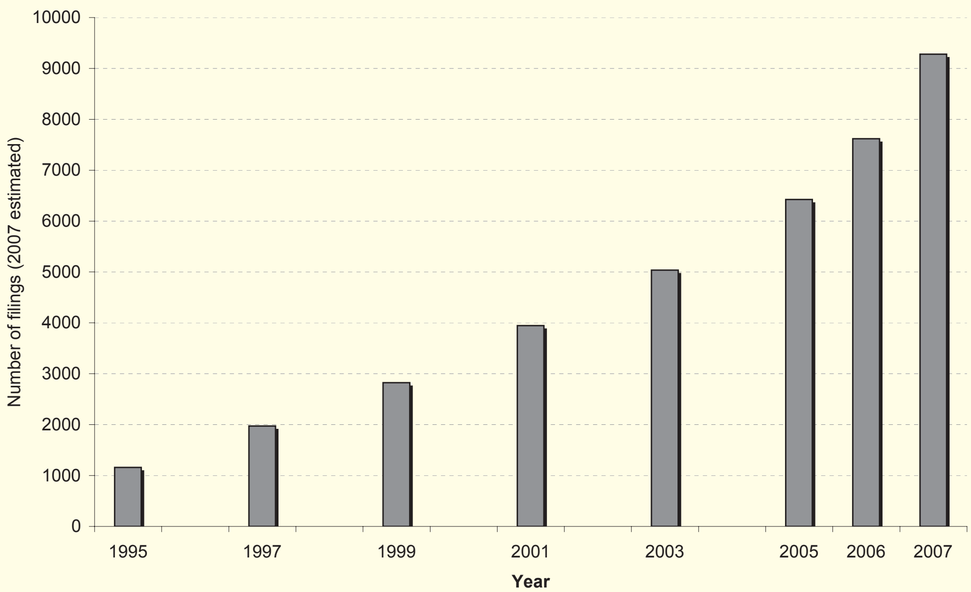
Where foreclosures lead to abandonment, neighborhoods can quickly destabilize.

The impact of many foreclosures on neighborhoods can also be substantial. When a foreclosure takes place in a wealthy or fast-growing community, the creditor generally makes sure that the property is maintained and quickly resold, usually to a new homeowner. As a result, the foreclosure has little impact on the community. However, the situation is very different in modest neighborhoods in Cleveland or Philadelphia. Housing demand in such neighborhoods is often weak, and even before the foreclosure wave it was often difficult to sell homes coming onto the market. When large numbers of homes are foreclosed, market demand is insufficient to absorb them. Properties, therefore, have little value and are more likely to be abandoned or bought by a speculator and "flipped" than sold to a new homeowner.[17]

In these situations, the creditor—usually the servicer representing the investors in the pool containing the mortgage—will have less interest in spending money to foreclose and maintain the property. According to one major industry source, the cost of each foreclosure is $50,000.[18] If the property is worth no more than that, particularly if it has been abandoned, the servicer may not even go through with the foreclosure. The property falls into a legal limbo that may take years to resolve.

Where foreclosures lead to abandonment, neighborhoods can quickly destabilize. Abandoned properties contribute to crime and fire hazard, diminishing the value of surrounding homes. A single abandoned house on a block, as a Philadelphia study found, can reduce the value of nearby properties by 15 percent.[19] Abandoned properties also place growing demands on services, which financially strapped older cities are hard-pressed to provide.

FIGURE 4: Foreclosure Filings in Cleveland , 1995-2007



Source: Frank Ford, Neighborhood Progress Inc.

Cleveland has been hit especially hard by foreclosures. In 2007, more than 9,000 properties, or roughly one in ten owner-occupied properties, had filed for foreclosure. Foreclosures have swamped the city's real estate market. Nearly 90 percent of properties foreclosed during the first half of 2007 had not been resold after six months. Those that had were sold for an average of only 29 percent of their market value.[20] Between 2005 and 2007, the median home value in Cleveland declined by 48 percent.[21]

This cumulative drain on property values can bring the real estate market to a halt. As Cuyahoga County Treasurer Jim Rokakis says about Cleveland's Slavic Village, "Even if [the homeowners] wanted to sell their homes, they wouldn't be able to find buyers. Who wants to live in a sea of foreclosures?"[22] A real estate agent discussing a middle-class Detroit neighborhood hit by subprime foreclosures, said, "Nobody's going to want to buy into a neighborhood with 20 percent foreclosures. You end up with no neighborhood." [23]

These neighborhoods represent ground zero in the crisis. Before the mortgage crisis, they were not typically the most distressed neighborhoods of their cities. They were often, instead, places that striving families saw as the "next step up," where they could find a house they could afford and begin to pursue the American dream.[24] For every direct victim of the crisis, many more will suffer collateral damage as a result, through loss of property values, increased crime, and increased pressure on municipal services.[25] Foreclosure and its ripple effects should thus be a priority for every state and local government.

2 Taking Action

Although state governments are constrained both by fiscal limitations and by potential federal preemption, their resources and powers give them broad scope for coping with the foreclosure crisis.[26]

First, while states may not regulate federally regulated financial institutions, most mortgage originators, particularly of subprime mortgages, are not federally chartered banks, thrifts, or their subsidiaries, but independent mortgage brokers who work with lenders—who themselves are often not subject to federal regulation.[27] Given that brokers originated 71 percent of all subprime mortgage loans in 2005, state action in this area is not only possible, it is critical.[28]

Second, states control the foreclosure process and have broad powers to regulate real property, advance health and safety, and protect consumers. States and municipal entities may also be able to bring suits against subprime lenders and other parties whose actions have triggered negative effects for state residents and drained state and local resources.[29]

Finally, each state's governor has a "bully pulpit" to focus public attention on the issue, bring lenders and servicers to the negotiating table, and attempt to secure their agreement to take the steps that the state may lack legal authority to compel.

Of course, because a state government can take a particular step does not mean that it should. Actions taken in haste without careful consideration can be wasteful, ineffective, or have unanticipated consequences. Although the crisis and state responses are still evolving, the experience so far makes it possible to identify some of those consequences, and suggest more effective directions for state action. In broad terms, these include:

- mitigating the effect of foreclosure on borrowers at risk of foreclosure;
- mitigating the impact of foreclosure on neighborhoods and communities at risk;
- preventing a recurrence of the crisis, and;
- establishing sound, long-term policies to create and preserve affordable housing.

States can take a number of specific action steps in each of these areas.

Mitigating the Effect of Foreclosure on Borrowers

The reasons are compelling for states to lower the number of families affected by the foreclosure crisis, and the economic loss and human distress that these borrowers and their families experience. At the same time, there are serious barriers to an effective public response.

Aside from cases of outright fraud, most foreclosed subprime mortgage loans were legal and represent legally valid contracts. A state cannot legally bar creditors from foreclosing, and any hurdles that it may impose on the process must be reasonable ones. While the courts will ultimately decide where to draw the line, responsible policymakers should not knowingly enact laws or regulations that are not sound law and policy.

A second obstacle is posed by the sheer magnitude of the obligations involved. According to the Center for Responsible Lending, $1.3 trillion in subprime mortages were outstanding at the end of 2007. According to financial consultant John Mauldin, $521 billion in ARMs have or will reset during the first six months of 2008.[30] Although not all are at risk, a significant and growing share are.[31] States cannot raise the capital needed to refinance even a modest share of this debt, even if it were fiscally responsible for them to do so.

Although states can neither bar creditors the right to foreclose or refinance on more than a minute share of the mortgages that are at serious risk, they still have several options they can pursue. These include:

> *Action Step 1:* Help borrowers gain greater access to counseling and short-term financial resources;
> *Action Step 2:* Ensure a fair foreclosure process, which includes opportunities for borrowers to negotiate with creditors;
> *Action Step 3:* Encourage creditors to pursue alternatives to foreclosure;

Action Step 4: Prevent predatory and fraudulent foreclosure "rescue" practices.

Action Step 1: Help borrowers gain greater access to counseling and short-term financial resources

When unsophisticated homeowners receive a notice of default, which is often soon followed by a foreclosure proceeding, they typically believe there is no recourse. Even when the default has been triggered by a temporary or remediable problem, or when they may be able to refinance or otherwise save their homes, these homeowners are often intimidated by the letters from the creditor and unaware of their options.

State governments can help borrowers better understand their options by increasing access to high-quality counseling programs and supporting local information campaigns, including door-to-door efforts in high-risk areas. Such measures require only modest financial resources.[32] Although each case is different, counseling organizations report average costs of between $1,000 and $2,000 for each borrower who receives meaningful foreclosure prevention assistance, a cost that is far less than any other form of assistance. Well-trained counselors, working in tandem with qualified lawyers, can assist borrowers to restructure or modify their loans and ultimately enable them to keep their homes. At a minimum, these programs may help borrowers find a less painful alternative to foreclosure.[33]

All told, such efforts could require state funding of $1 million to $10 million per year, depending on the size of the state and the severity of its foreclosure problems. These funds can come from the state general fund, from reserves accumulated by a state housing finance agency, or from a fee on foreclosure filings or on subprime originations. A fee of $500 to $1,000 per foreclosure, for example, is modest in light of the mortgage amount or the overall cost of foreclosure, and yet in the aggregate would permit states to significantly expand services for borrowers at risk.

In addition to expanding counseling and information programs, many states are also providing either short-term emergency assistance or permanent refinancing of problem loans to at-risk borrowers. Short-term emergency assistance can enable borrowers to address a temporary financial problem that has led to delinquency, such as loss of a job or a medical emergency. In such situations, the borrower can usually regain the ability to make mortgage payments, and ultimately pay back the assistance. The Pennsylvania Homeowner's Emergency Mortgage Assistance Program (HEMAP) is a model program. Since its inception in 1983, it has assisted more than 35,000 homeowners with a total of $365 million in disbursements. Funds are provided as a loan, and the program has a 73 percent repayment rate.[34]

Emergency assistance programs only work for some borrowers, however. They are of little use to borrowers whose mortgage is unsustainable—a growing share of those at risk. Such borrowers gain nothing from short-term assistance other than buying time. Instead, this group needs a long-term resolution of their situation, whatever form it may take.

Although emergency assistance programs can be a good policy tool, state programs to refinance problem loans, even though widely proposed, are more problematic. Given that nearly 750,000 subprime ARMs were 90 days or more past due at the end of 2007, the amount that states can afford to allocate to this purpose is absurdly small relative to the need.[35] New York State recently created the "Keep the Dream Mortgage Refinancing Program," using $100 million borrowed from Fannie Mae. At most, this program will help fewer than 1 percent of those in need.[36] Other state programs are equally modest.[37]

What is more, these programs are a lottery, where a few people win, and the rest get nothing. That in itself makes them poor public policy, made worse by the difficulty in choosing who should benefit. Given that the funds are a debt to the state, the program may cherrypick lower-risk households to minimize its own risk. Finally, by compensating the lender who made a bad loan, these programs insulate the responsible party from risk and undermine efforts to hold the industry accountable for resolving the situation it has created.

Action Step 2: Ensure a fair foreclosure process

States are empowered, within the bounds of the Constitution, to regulate how foreclosures take place.[38] States have broad powers to address borrower and public concerns while still providing legitimate creditors with the means of obtaining redress for mortgage defaults. The state has the power to impose fees, time frames, notice, and information requirements on those who engage in foreclosure proceedings. Those requirements may be demanding, but not so onerous that they create de facto bars to using the process.

Because state foreclosure procedures vary widely, policymakers must determine how to apply basic principles to state-specific legal provisions. Some of these principles are straightforward matters of sound practice:

- Notice of foreclosure should allow ample time for the borrower to seek counseling or other assistance before it is too late;
- The standard of notice should not permit alternatives to direct service except after due and diligent inquiry;
- Notice of foreclosure should include clear, highly visible notice to borrowers in straightforward nontechnical language of their rights, information about counseling and other resources, and warnings about fraudulent counseling and rescue scams;
- Borrowers should have ready access to individuals who are empowered to act on behalf of the creditor throughout the process to facilitate negotiated alternatives to foreclosure;
- All required notices should also be served on state and local government, including the government entity responsible for code enforcement or property maintenance;
- Courts (or appropriate parties in nonjudicial foreclosure states) should adopt standards to screen foreclosure filings for potential evidence of fraud or misrepresentation in the initial transaction;
- Courts (or appropriate parties in nonjudicial foreclosure states) should adopt clear standards for the information required in foreclosure filings, and refuse to accept any filings that fail to provide all required information. This can include not only information about the mortgage, but also about the property, including whether it is occupied or vacant or in code compliance.

Although on their face these provisions seem unexceptionable, and clearly impose little or no burden on creditors, many states do not in fact offer these procedures, which can protect both borrowers and the integrity of the foreclosure process.

In addition, a small portion of individual transactions may have involved fraud or misrepresentation. For example, mortgages in which the amount of the loan significantly exceeded the fair market value of the property may have involved misrepresentation by the broker to the lender, while in other cases brokers may have failed to provide mandated disclosures to prospective borrowers.[39] Evidence of such practices can be a legal basis for denying the creditor the right to enforce the loan. At a minimum, it is a basis for shifting the burden and requiring the creditor to prove that the loan was *not* fraudulent.

Other, more substantive changes to the foreclosure process should also be considered. For example, states should enact legislation to permit former homeowners to remain on the premises as tenants after foreclosure until the property is sold to someone who intends to use and occupy the property.[40] When former homeowners are evicted after a sheriff's sale, the vacant property often deteriorates before a new owner takes possession. Worse, many homeowners facing foreclosure abandon the property well before title changes hands. By remaining as tenants—paying a fair market rent and subject to a tenant's statutory obligations—the former homeowners stay housed and the property remains occupied, preserving value for the creditor and minimizing harm to surrounding properties.

States should also require forbearance or waiting periods between filing and foreclosure.[41] Negotiating and putting into effect an alternative to foreclosure can be time-consuming. Borrowers should have the opportunity to seek alternatives, and creditors should make good-faith efforts to work with borrowers during reasonable time frames. This is particularly important when the default is triggered by an ARM interest rate reset, where prepayment penalties apply, or where there is some question about the mortgage itself, particularly if the borrower has filed a consumer complaint. Provisions for forbearance should specify that if the owner abandons the property, the forbearance period ends immediately, and the foreclosure should proceed expeditiously to sheriff's sale.

States should impose penalties on creditors who fail to pursue foreclosure in a timely and responsible fashion.

State landlord-tenant laws should permit tenants of absentee-owners or owner-occupied two-, three-, or four-family properties to remain on the premises until the property is sold to someone who intends to use and occupy the property. If it makes sense to permit former owners to remain on the premises, it makes even more sense to permit tenants, who had no hand in the default, to remain until or unless a new user plans to occupy the property. Foreclosure, except where the new owner needs to physically occupy the premises, should not be grounds for eviction under state law.

Finally, states should impose penalties on creditors who fail to pursue foreclosure in a timely and responsible fashion. Historically, government has recognized the right of creditors to recourse while limiting that right where dictated by compelling public policies.[42] If a creditor initiates a foreclosure, or has obtained the legal right to do so by serving notice of delinquency on a borrower, it has an obligation to do so in a timely and responsible fashion. Where the creditor fails to do so, the property is at risk of becoming vacant and in legal limbo.

A legal remedy would allow state or local government to "step in the shoes" of nonperforming creditors. If a creditor, having initiated foreclosure, fails to move forward within a reasonable period, the state or municipality could order it to move forward expeditiously.[43] Failure to do so forfeits the creditor's right to foreclose, and the state could obtain a court order transferring the creditor's interest to the state. The state could then take such action as it deemed appropriate, either foreclosing or negotiating with the homeowner.[44] Alternatively, the state or municipality could take possession and quiet title on the failure of any interested party to redeem within 90 days of notice.

Action Step 3: Encourage creditors to pursue alternatives to foreclosure

Foreclosure is often the worst possible outcome for the borrower. It is also often a poor outcome for the creditor. The cost of foreclosure is high, while the length of the process and the antagonism it creates between creditor and borrower often lead to a lower value for the property by the time the creditor takes title.

The available alternatives fall into two broad categories: (1) refinancing or modifications to the existing loan that permit the owner to remain in the house, and (2) conveyance of the property in ways that enable the owner to avoid the stigma of foreclosure.

Loan modifications vary widely. In some cases, servicers may offer a borrower a short-term rate freeze, adding the "lost" interest to the principal of the loan or tacking it onto the back end. Such modifications rarely do more than put off the day of reckoning. In other cases, servicers have negotiated more substantive modifications, such as converting ARMs into fixed-rate mortgages on terms that the borrower can afford. A common conveyance option that can avoid foreclosure is a short sale, in which borrowers sell the property for an amount that is less than what they owe, and the creditor agrees to forgo the balance. A second option is for the borrower to relinquish the deed in lieu of foreclosure.

States cannot compel creditors to negotiate with borrowers, but they are not without leverage. Both states and local governments have the ability to link bank deposits to lender's commitments to negotiate sound alternatives with borrowers and to dispose responsibly of properties taken through foreclosure. This approach could offer states, particularly major ones, significant leverage against the many mortgage lenders and servicers that are subsidiaries of depository banks.

Several states and the federal government have entered into voluntary agreements under which servicers agree to negotiate with certain borrowers under certain conditions. In an agreement negotiated by the state of California, four major servicers agreed to freeze the interest rate for borrowers meeting certain conditions for up to five years on subprime ARMs scheduled to reset. The borrowers must show that they are owner-occupants, have made their payments on time, and can show they cannot afford payments with the higher interest rate. The plan negotiated by the federal government with servicers and announced by President Bush in December 2007 is similar, although the eligibility criteria in that plan are narrower.

It is unclear how valuable these agreements will be. These freezes are not permanent, and they are predicated on the uncertain assumption that home prices will rise enough in five years to enable borrowers to sell or refinance without large losses. The Center for Responsible Lending estimates that only 7 percent of subprime borrowers will be able to take advantage of the federal plan. Still, the Center estimates that as many as 145,000 families may benefit from the federal plan, which is not insignificant. Although the terms of the California plan are somewhat broader, it involves only four servicers, albeit four major ones.

These agreements assume that servicers will act not only in good faith but capably to carry out their side of the bargain. Such an assumption demands that borrowers seeking modifications, and the counselors working with them, can gain ready access to mortgage representatives, and that those representatives will work with borrowers to make timely modifications to their loans. To date, the experience has not been encouraging. Tales are widespread of difficulty getting through to servicers, unresponsive or uninformed representatives, and long delays in getting answers or decisions. If this situation continues, large numbers of borrowers who are potentially eligible for help may never receive it. For all these caveats, agreements with servicers for loan modifications and other solutions, such as a willingness to accept short sales or to convey real estate owned (REO) properties to public or nonprofit entities, are worth pursuing.[45]

Voluntary agreements are not an alternative to legislative action to tighten the rules governing foreclosure, but rather complement such actions. Indeed, the more strongly a state is committed to making legislative changes to protect borrowers and impose obligations on creditors in foreclosure, the more likely servicers will be to consider alternatives.

Action Step 4: Prevent predatory and fraudulent foreclosure "rescue" practices

An unpleasant byproduct of the foreclosure crisis is the emergence of unscrupulous firms preying on at-risk households by offering to "rescue" them from foreclosure. Common practices find people charging fees as bogus foreclosure prevention counselors, when nonprofit organizations offer these service free of charge. Others take advantage of owners' distress by offering to buy their homes at below-market prices, or they induce owners to relinquish their titles in return for bogus commitments to sell owners their own home back to them clear of mortgage debt.

States can regulate these practices under their consumer protection authority. Although it may be impossible to ban them outright, state government can control them significantly by:

- setting clear definitions of permissible and notpermissible activities;
- requiring formal and detailed contracts between the owner and the "rescuer" for any of the activities typically carried out by foreclosure rescuers;
- rescinding such contracts where appropriate, including a mandatory "cooling-off" period;
- licensing "foreclosure consultants" and imposing requirements on them, such as surety bonds, and;
- providing stiff civil and criminal penalties for violations of the law.

A few states, including New Hampshire and Illinois, have enacted statutes to address this issue, principally by requiring detailed contracts and providing for a right of rescission. States should also sponsor education and media outreach in areas where large numbers of foreclosures are taking place, simple strategies that are likely as important as legal remedies.

Mitigating the Impact of Foreclosure on Neighborhoods and At-Risk Communities

Under even the most optimistic scenario, there will still be far too many foreclosures during the next few years. These foreclosures have already begun to ravage cities and older suburbs and are likely to continue to do so—with particularly devastating effects in areas with a weak housing market.[46] To minimize the impact of foreclosures on such areas, public-sector strategies should focus on how the transition of ownership takes place within foreclosure, in three respects:

Action Step 5: Establish creditor responsibility to maintain vacant properties;
Action Step 6: Make the process as expeditious as possible;
Action Step 7: Ensure that the property is ultimately conveyed to a responsible owner.

The best outcome is to get the property into the hands of a new homeowners, at a price and on terms that maximize their ability to remain in the home. That is not always possible in many hard-hit areas, where the number of properties in foreclosure exceeds prospective home buyer demand. In those areas, the goal should be to seek a responsible entity to maintain the homes in the interim or demolish or stabilize them where appropriate, while holding the properties for future reuse.

Whether conditions permit speedy recycling of properties or require "land banking" for a later use, states and localities must find or create entities capable of managing the process. Servicers are unlikely to take responsibility for handling properties in ways that serve community interests. Although a few cities or community development corporations are negotiating with servicers on a small scale, new models and systems are needed to address the issue at a level commensurate with the problem.

Action Step 5: Establish creditor responsibility to maintain vacant properties

Under American law, property ownership implies responsibilities as well as rights. State laws govern property ownership and grant states and localities broad authority to enforce codes, abate nuisances, and take other actions needed to protect the public health, safety, and welfare. Property owners must maintain their properties to state or local codes and must not allow them to become a nuisance to neighbors. If they do not, local officials can take legal action to compel owners to fulfill their responsibilities by imposing civil and criminal penalties, invoking their power to enter on the property to make necessary repairs, and in extreme cases, by compelling owners to forfeit their property. In most states, a city abating a code violation or a nuisance can place a priority lien on the property, and in a few, can collect the costs of the abatement from other assets of the property owner.[47] In all cases, the scope of local action is governed by state law.

Even under normal conditions, this system works unevenly, however. During the foreclosure process, the system often breaks down. It is not unusual for homeowners to abandon their homes prior to foreclosure, leaving them vacant. The foreclosure may not happen for months or years, and in some cases not at all. If the sheriff's sale does take place, the creditor—now the owner—may or may not take responsibility for the property. If the property falls into limbo, it may be many years before it is recaptured, usually through tax foreclosure. By that time, it is likely to be worthless, having been stripped or vandalized, and having done untold damage to its neighbors.

This issue raises two questions. First, where does responsibility fall with respect to property, and second, what are the responsibilities? There is nothing inherent in constitutional law limiting property responsibilities to title owners. Under common law, a lender who has taken steps to exert control over a property in the absence of foreclosure is known as a "mortgagee in possession" and has assumed responsibilities associated with ownership. The New York State Property Maintenance Code, for example, follows "title holder" in the definition of "owner" with the language, "or otherwise having control of the property."[48] Although the New York definition does not explicitly refer to creditors, it can be interpreted as applying to them.[49]

The city of Chula Vista, CA has established an Abandoned Residential Property Program under which mortgage lenders must regularly inspect defaulted properties and take responsibility if the property is vacant.[50] In some states, however, such a municipal ordinance may be legally precluded by state law, while in others it would fall in a gray area.[51] In some cases, even if local courts and municipal officials could hold lenders liable for property maintenance, their enforcement systems may not be strong enough to motivate lenders to act responsibly.

To help ensure that foreclosed properties are properly cared for, states should give municipalities the legal tools to compel creditors who have asserted control over them to assume responsibility for property maintenance and nuisance abatement. Such tools should include the following provisions:

- The "owner" should be clearly defined for purposes of property maintenance, code compliance, and nuisance abatement to include mortgage holders who have issued a notice of default or foreclosure. The law should specify that it applies only to vacant properties where the title holder is no longer occupying the premises.
- Where the mortgagee is not physically present in the county, it must provide a local agent with a 24-hour contact number who will accept service on its behalf.
- Fines for noncompliance should be stiff, and prosecutors should have access to both civil and criminal sanctions for violations.
- Nuisance abatement powers should be broad, with local enforcement officials given discretion to determine whether to repair, renovate, or demolish.
- Repayment of nuisance abatement costs can be sought either by placing a priority lien on the property, by recourse to other assets of the owner or mortgage holder, or both.
- As an ultimate recourse, states and localities should have the authority to use their forfeiture power and seize nuisance properties where the entity in control of the property has been given notice and fails to comply with a court order requiring abatement of the nuisance.[52]

Unfortunately, many cities and towns lack the capacity to fully use these tools. Code enforcement agencies are often understaffed or poorly organized; coordination between prosecutors, courts, and code enforcement personnel may be inadequate; and cases may not be systematically tracked or pursued. States should therefore assist cities with problem properties to upgrade their code enforcement and nuisance abatement capacity. This may take the form of financial or technical assistance, including helping enforcement agencies adopt new technologies that will increase the effectiveness of existing code enforcement operations, or it may include the reorganization or creation of dedicated housing courts.[53]

The faster properties can be recycled and put into the hands of a responsible owner, the better.

Finally, states should explore providing cities money to establish local nuisance abatement revolving funds, from which local officials could draw funds for repairs or demolition, recapturing the money from liens on the property or judgments against the owner or creditor. Such a fund will only revolve, however, if state law permits the city to recapture the funds spent and the city establishes foreclosure and collection procedures to ensure they are recaptured. In cities such as Cleveland or Detroit, because of the limited market value of the properties involved, the ability to obtain a judgment against the owner or creditor is critical.

Action Step 6: Make the process as expeditious as possible

The faster properties can be recycled and put into the hands of a responsible owner, the better. Every day a property sits vacant increases the risk of vandalism and abandonment. Once that has happened, each day brings more damage to neighbors and the community. Foreclosure procedures, particularly for vacant properties, should therefore be as expeditious as possible.

Many states' foreclosure and judicial sale procedures are cumbersome. The Ohio process, for example, is divided between seven separate agencies, each headed by a separately elected public official. Even where the procedure itself is reasonably efficient, backlogs, staffing constraints, or competing priorities can mean waits of months or years before judgments are issued or sheriff's sales held.

To minimize the length of time properties are vacant and increase the likelihood that they can be effectively recycled, states should:

- Make the statutory foreclosure process as expeditious as possible and provide clear, marketable title to the buyer upon recording the deed after sheriff's sale;
- Review their procedures for foreclosure and judicial sale to ensure that practices are efficient and straightforward;
- Provide technical, financial, and staff assistance to remove backlogs and reduce delays in processing foreclosures in the courts and sheriff's offices;
- Establish accelerated sheriff's sale procedures for vacant properties.

Finally, where no one has assumed responsibility for the property, municipalities should be able to move quickly to gain control of the property directly, by enacting statutes authorizing expedited tax foreclosure procedures for vacant properties, vesting title to foreclosed properties in the county or municipality; and enacting statutes permitting "spot blight" eminent domain of vacant properties, permitting them to take such properties and convey them to a responsible entity for reuse.

Michigan has enacted an accelerated procedure for tax foreclosure of vacant properties, which several entities—most notably the Genesee County Land Bank Authority—have used to gain control of problem properties in distressed cities.[54] Several states permit spot blight takings, including Iowa, New Jersey, Ohio, and the District of Columbia.[55]

Action Step 7: Ensure that the property is ultimately conveyed to a responsible owner

Public efforts to preserve neighborhoods facing a foreclosure crisis should place foreclosed properties in the hands of responsible owners for stable reuse, or where market conditions do not permit, to hold them responsibly until long-term reuse is possible. The above activities can create the environment to achieve this goal, but they do not actually achieve it. To do so, direct public intervention is needed.

The national scope of the crisis calls for a federal response, although one that should delegate implementation to state and local entities.[56] The federal government has the greatest access to the resources needed to address this issue, as well as the greatest leverage to negotiate the critical agreements. However, given that meaningful and timely federal action appears unlikely, and local resources are unlikely to be adequate to the task, state government has become the critical arena for addressing the issue.

For property recycling strategies to be effective, states first must help build property recycling entities (PREs). These entities must be empowered with the ability to gain control of properties—both REO properties and those at risk of foreclosure—and recycle them for immediate or long-term reuse in ways that help maintain stability or revitalize affected neighborhoods in the future.

In some cases, states should create new state-chartered private corporations or adapt existing ones, combining valuable features of both public and private entities. Where they exist, states should support nonprofit entities rather than creating new ones. A statewide entity may often be most appropriate, but there may be cases—particularly in states with one or more large cities with strong institutional infrastructure—for which the state should support regional or metropolitan PREs rather than a single statewide one.

A PRE can focus entirely on acquiring REO properties, or it can acquire both REO property and mortgage paper. What to do with the properties will depend on several variables, and the job of the PRE is to carry out the most appropriate strategy for each, as shown in Table 1. The PRE itself should be an intermediary rather than a landlord, lender, or developer, working with local lenders, community development corporations, realtors, contractors, and local governments to carry out its mission. Its sole long-term role may be to act as a land bank, holding properties for long-term reuse where the housing market is weak and no other capable land-holding entity exists.

Table 1: Potential Property Recycling Scenarios

Property Status	Borrower Situation	Other Considerations	Strategy
Occupied	Owner has adequate income to continue to pay mortgage in future[57]	Amount of mortgage not in excess of property value	Sell loan at par to local lender
Occupied	Owner is responsible with adequate credit, but cannot sustain mortgage payments, particularly with recent or forthcoming ARM reset		Assist borrower to refinance with local lender based on lower mortgage amount that owner can sustain
Occupied	Owner unable to carry any realistic mortgage amount, but maintains home adequately		Assist borrower to exit from mortgage by arranging short sale or deed in lieu of foreclosure. Convey property to responsible owner. Possibly permit owner to remain in property as tenant.
Occupied	Owner is irresponsible, either as a borrower or with respect to property		Foreclose and evict borrower. Recycle property as vacant property.
Vacant	Not applicable	Property in good condition with fair to good market value	Sell through realtor on private market
Vacant	Not applicable	Property in good condition with little market value	Sell to CDC or responsible landlord to maintain as affordable rental housing for Section 8 voucher holders
Vacant	Not applicable	Property in need of rehabilitation with fair to good market value after rehabilitation	Sell to CDC or responsible developer/contractor to rehabilitate and sell either as affordable housing or on private market.
Vacant	Not applicable	Property in need of rehabilitation and little or no market value	Hold, demolish, or stabilize, or convey to local government, CDC, or land bank entity to be held for long-term reuse or land assembly.
CDC = Community Development Corporation			

In addition to legislative or administrative action to create property recycling entities, state government should provide capital for them to acquire properties and mortgages from their holders. This will be costly, given that a substantial number of properties must be acquired to have an effect. Under most of the scenarios in Table 1, however, all or most of the funds should return to the PRE, and ultimately to the state. The price at which the PRE buys paper or properties must be discounted enough from the face value of the debt such that the purchase price, with the additional transaction and holding costs, does not exceed the value of the property when appropriately recycled.

Negotiating such discounts should be possible. Creditors are well aware of the cost of foreclosure and the diminishing value of assets held as REO properties, particularly in distressed neighborhoods. They also know the costs of maintaining them. By requiring servicers to bear those costs, the state can increase their motivation to negotiate reasonably for the sale of their properties and mortgages. Further, by imposing greater creditor responsibility in the foreclosure process, the state also prevents an economic "free ride" by ensuring that creditors—and not just the public sector or neighbors of REO properties—are forced to pay the cost of the externalities they created.

Preventing Future Abuses in the Mortgage Lending System

The preceding sections have focused on how to address the immediate crisis and mitigate its effects on individual borrowers and their communities. Although the practices that led to that crisis are now rare, it is important to ensure that they do not resurface.

Both state and federal governments have moved to limit improper and abusive practices, reflecting the political environment in which such measures, even if not directly resolving the immediate problems, can be more readily enacted. Many bills are pending in Congress, including H.R.3915: Mortgage Reform and Anti-Predatory Lending Act of 2007, which has passed the House of Representatives. In December 2007, the Federal Reserve System, under its authority to regulate federally chartered financial institutions, proposed rules to ban those institutions from pursuing several of the more abusive practices associated with the subprime industry.[58] As the crisis deepens, the resolve to address these issues is likely to grow.

States, meanwhile, are beginning to use their authority to regulate mortgages by lenders and brokers who are not subject to federal regulation. Although all 50 states now regulate mortgage brokers, in many states, the regulations set only minimal industry standards. Although the most egregious practices have been reined in, the situation remains profoundly flawed for an industry that so powerfully affects both consumers and entire communities.[59] Many states, even with stronger licensure laws, devote inadequate resources to industry oversight and provide only "slap on the wrist" penalties for egregious activities. As such, there is significant room for states to improve their current response to the problem by taking steps to:

> *Action Step 8:* Better regulate the mortgage brokerage industry;
> *Action Step 9:* Ban inappropriate and abusive lending practices.

In exploring preventive measures, however, both states and the federal government must distinguish between products—that is, how the loan is structured—and practices. Certain practices associated with subprime lending, such as "no doc" underwriting or yield spread premiums, are abusive on their face and cannot be justified from a public interest standpoint. However, adjustable rate mortgages are not in and of themselves problematic. Making such a loan to a low-income borrower with limited assets may be abusive, while making a similar loan to a high net worth individual may not be. Regulators must be careful to make such distinctions to not unduly constrain the industry while preventing practices likely to lead to future defaults.

Action Step 8: Better regulate the mortgage brokerage industry

Mortgage brokers and their employees underwrite billions of dollars of mortgages to millions of borrowers each year. Performing this activity properly demands that the brokers in charge and their employees show sound judgment and substantial knowledge of complex financial and legal matters. Even though brokers do not put up the funds used to make the mortgage, they must have the financial resources to protect their clients' interests in the event of fraud, misrepresentation, or failure to perform. Responsible licensing laws must address all these issues. Table 2 is a summary of model mortgage broker licensing standards.

Table 2: Model Licensing Standards for Mortgage Brokers

Category	Rationale	Regulatory Standard
Licensure	Responsibility does not lie in the firm itself, but in the individuals associated with ownership and management of the firm, as well as those involved in mortgage origination	(1) Regulations should cover the individual who is the broker in charge as well as principals in the firm (2) Mortgage originators or salespeople should also be subject to licensure
Education and experience	Brokers need extensive knowledge of financial and legal issues, including the constant changes in laws and practices	(1) Regulations should impose minimum education requirements for licensure (2) Regulations should impose continuing education requirements for license renewal (3) The broker in charge should have prior experience in a related field, such as a bank loan officer
Examination	Brokers and originators should demonstrate that they have the necessary body of knowledge to conduct business responsibly.	Regulations should require that brokers and originators pass an examination prior to licensure
Fitness	Brokers and originators should be of good character and be able to demonstrate sound judgment	Background criminal and credit history checks should be performed on all individuals subject to licensure
Offices	Brokers should be accessible to consumers	Regulations should require that the broker operate an office with regular hours within the jurisdiction in which she is licensed
Financial resources and accountability	Brokers should have adequate financial resources and accountability to ensure that clients' interests are protected	(1) Regulations should require a minimum net worth for brokers (2) Regulations should require that brokers post a surety bond with the amount based on the broker's volume
Records and reporting	Information about broker activity should be accessible to state regulators, and to the public	(1) Regulations should set record-keeping and reporting obligations for brokers (2) Brokers must provide access to records to state regulators during normal business hours (3) The state regulatory agency should publish regular reports on broker activity and post the information on its web site

Although state licensure standards are higher than they were a decade ago, they remain uneven. Some require education, some require experience, some an examination, but few require all three. Although most states require brokers to post a surety bond, the bond amount is usually far too low, only $25,000 and $50,000.[60] Only 13 states require that brokers have a minimum net worth. And only some states require that the broker's employees (originators) be licensed; these are often the only individuals dealing directly with borrowers.

State banking or financial services departments must exercise effective oversight over brokers, and meaningful penalties must exist and be enforced. There has been some recent improvement. A multistate effort to create a uniform database and application for mortgage brokers is underway, with 42 states indicating that they will participate by the end of 2009. However, many states still lack appropriate standards, and they lack resources to conduct proper oversight.[61]

Penalties for violations vary across states. In some states, the power to close an office or bar a firm from doing business in the state may not be a significant deterrent in light of the ease of re-entry. Others have adopted stronger provisions. North Carolina can penalize brokers $10,000 per violation, and in some cases up to $25,000. Illinois recently provided a private right of action for borrowers injured by broker violations of state legal provisions.[62]

To be effective, each state should establish regulation and oversight of mortgage brokerage activities that cover the following elements:

- a state licensure act that includes the elements in Table 2;
- licensure of all mortgage solicitors and originators as well as brokers;
- regular, detailed reporting requirements;
- effective state oversight of mortgage brokers, including regular examinations of brokerage offices funded by a dedicated fee on brokers or transactions;
- stiff penalties for violations of state brokerage laws, including criminal penalties for fraud;
- enforcement, including giving county prosecutors and injured parties the right to bring brokerage violation cases, and providing for attorneys' fees in successful cases.

These provisions are not a substitute for substantive regulation of broker and originator practices. They are needed, however, to ensure that substantive regulations, once adopted, are meaningful and prevent future lending abuses.

Action Step 9: Ban inappropriate and abusive lending practices

Many broker practices conflict with the interests of borrowers acting in good faith to buy a home or refinance an existing mortgage. In recent years, several states, including Ohio, North Carolina, Massachusetts, and Minnesota, have enacted legislation that makes many of these practices illegal and subject to penalties. These practices fall into three distinct categories: (1) improper underwriting practices; (2) inappropriate loan provisions; and (3) other forms of industry conduct that harm borrowers, such as yield spread premiums.

Improper underwriting practices. Subprime loan underwriting is arguably the single area with the greatest abuses. That so many subprime borrowers could have qualified for better loan terms is in itself evidence of pervasive underwriting abuses. To ensure that borrowers' interests are served and that the integrity of the lending process is maintained, states should set certain principles into law.

To begin, states should establish a fiduciary responsibility of mortgage brokers to act in the interest of borrowers, which is necessary in light of the many mortgage options and the extreme information gap in the lender-borrower relationship.[63] This standard appears in some state court decisions, such as California.[64] States should also consider:

- adopting a "suitability" or "best available product" standard for mortgages, requiring the broker to certify that, based on the borrower's credit and other information, the loan suits the borrower's needs or represents the best loan terms for which the borrower qualifies;
- establishing an "ability to repay" standard, barring loans except where the borrower's documentation clearly establishes that he or she will be able to make the mortgage payments;[65]
- requiring that refinancing transactions show a "tangible net benefit" to the borrower.

Such rules can particularly ensure that mortgage refinancings do indeed benefit the borrower and are not simply generating commissions for the mortgage broker. Although the principle of "tangible net benefit" appears vague, it is easily established. The state of Rhode Island has established a six-part test, and if any one of the criteria is met, the loan is deemed to meet the standard.[66]

Second, states should prohibit loans without adequate documentation. No-documentation loans are a pernicious practice that encourages misrepresentation on the part of the borrower and irresponsible underwriting on the part of the lender. A recent report found that "63 percent of brokers [making no-doc loans] said they knew their self-employed clients had 'unreported income' they wanted to keep off the record, while 43 percent said their clients can't qualify under standard [debt-to-income] ratios." In other words, if they documented their income and their monthly bills, the new mortgage debt might represent 50 percent or more of their income, a ratio far beyond what most lenders in the regular market consider acceptable.[67]

Inappropriate loan provisions. In addition to underwriting loans, many subprime loans contain provisions that are harmful to borrowers' interests, or lack certain protections of those interests. States can help curb abuses in several ways.

First, states should enact laws limiting prepayment penalties and provide that any prepayment penalty expires at a reasonable time prior to any payment increase or reset. Prepayment penalties should not bar borrowers from refinancing to avoid higher interest rates triggered by a mortgage reset. They should also limit fees, bar mandatory arbitration clauses, and prohibit the addition of unnecessary and unwanted insurance products into loan balances.

A second, more complex issue that state governments should at least consider is whether any forms of mortgage should *in themselves* be banned as inherently abusive, such as the Option ARM, which has been described as "the riskiest and most complicated home loan product ever created."[68] Instead, states may choose to require additional protections for borrowers taking out such a loan, such as a mandatory "cooling-off" period or a requirement that the borrower obtain third-party counseling prior to entering into the loan.

Other lending practices. Some of the most dangerous practices associated with the subprime industry do not fit neatly into either of the above categories. Yet states can still have significant influence.

First, states should prohibit yield spread premiums, in which lenders offer brokers larger commissions for making higher-interest loans. Such premiums constitute an inherent conflict of interest.

Second, states should require that lenders provide escrow services for property taxes and insurance. When mortgage loans were more often held by banking institutions, lenders typically provided escrow services. While it protected the bank's interest, escrow accounts also protected the borrower. It should be required as a consumer protection measure.

Third, states should establish clear standards for appraisals and require arm's length relationships between broker and appraiser. Inflated appraisals, including many where the broker and appraiser shared a common interest or where the broker may have motivated the appraiser to arrive at an unrealistic value, contributed to the foreclosure crisis. Mortgages that reflect unrealistic values not only impose higher costs on the borrower, but prevent refinancing because the debt exceeds the real value of the property.

Finally, many of these provisions are likely to be ineffective unless they are coupled with standards that ensure that brokers fully disclose not only the terms of a mortgage, but all of the options and alternatives that may be available to the borrower. A recent Illinois statute provides, with respect to prepayment penalties, that the broker must offer the borrower a loan without such penalties and disclose the difference in rate between the two. The borrower must decline the offer in writing.[69]

3 Closing Note: Looking Forward to a Rational Housing Policy

Today's foreclosure crisis will pass, although not before damage is done to the lives of millions and the stability of innumerable urban and suburban neighborhoods. If states take the action steps described above, they can significantly mitigate that damage, saving homes for thousands of families and preserving the value and vitality of communities.

Although immediate attention is needed to tackle the crisis at hand, the factors that triggered the crisis point to more fundamental deficiencies in American housing policy that must be addressed, if not today, then in the future. These deficiencies are most evident in two areas: (1) the promotion of homeownership among lower-income families, and (2) an inadequate stock of sound, affordable rental housing. And so we come to our final action step:

> *Action step 10: Establish sound long-term policies to create and preserve affordable housing, for both owners and renters*

> The benefits of homeownership to lower income households only accrue if they can own a home at costs that are not burdensome, and under conditions that foster stability and reduce their risk of losing their home.

The subprime crisis demonstrated the failure of an approach to fostering lower income homeownership that was based on maximizing the availability of credit, with little concern for the affordability of the credit, the appropriateness of the mortgage product, or the sustainability of the homeownership. The benefits of homeownership to lower income households only accrue if they can own a home at costs that are not burdensome, and under conditions that foster stability and reduce their risk of losing their home. Creating those conditions requires rethinking the mortgage instruments available to lower-income homeowners and developing a support system to help them weather the inevitable strains of ownership. Although states may have little role in the larger credit system, they can play important roles in building the support system for future lower-income homeowners.

At the same time, the foreclosure crisis is a reminder that homeownership is not the only housing option. For many years, the United States has had more of a homeownership policy than a housing policy. The rhetoric of homeownership for all has obscured the importance of maintaining a viable rental housing sector for the roughly one-third of all American households who, at any given point, are renters. Preserving and expanding the affordable rental housing sector should become as important a goal of housing policy—at both the state and federal levels—as fostering more stable, sustainable homeownership.

Endnotes

1 Alan Mallach is a Senior Fellow at the National Housing Institute and a Visiting Scholar at the Federal Reserve Bank of Philadelphia.

2 In addition to older industrial cities, the areas with the greatest concentration of foreclosures are fast-growing areas in the sunbelt, including many parts of California, Arizona, and Florida, and Las Vegas. Of the 25 metropolitan areas with the highest rate of foreclosures, measured in ratio of foreclosure filings per number of households, eight were older industrial cities (five of which were in Ohio), and 11 were in California and Florida. Owners facing foreclosure in the sunbelt communities, however, are more often absentee owners or speculators than in the older industrial areas.

3 Because subprime lending is defined by the market it serves, rather than by the product, there is no standard or generally accepted definition of what constitutes a "subprime loan." In proposed amendments to Regulation Z, the Board of Governors of the Federal Reserve has proposed a definition of "higher-priced mortgage loan" that would address this concern.

4 Critical players in this scheme were Standard and Poor's and Moody's, the supposedly independent agencies that issue credit ratings for Wall Street securities. These agencies developed complicated models to justify these securities' high credit ratings, thereby making them marketable to a wide range of investors, including pension funds and public bodies. Since the collapse of these securities, their methods and the substantial fees they secured from the issuers of the securities have come under considerable scrutiny. An excellent case study of the securitization process is Allan Sloan, "Junk Mortgages under the Microscope," *Fortune,* October 16, 2007.

5 *Danielle DiMartino and John V. Duca,* "The Rise and Fall of Subprime Mortgages." *Economic Letter,* Federal Reserve Bank of Dallas, November 2007.

6 This point has been extensively documented. See Calvin Bradford, "Risk or Race? Racial Disparities and the Subprime Refinance Market" (Washington: Center for Community Change, 2002); Marsha J. Courchane, Brian J. Surette, and Peter M. Zorn, "Subprime Borrowers: Mortgage Transitions and Outcomes." *Journal of Real Estate Finance and Economics* 29 (4) (2004): 365–392; Debbie Gruenstein Bocian, Keith S. Ernst, and Wei Li, "Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages" (Durham, NC: Center for Responsible Lending, 2006).

7 Edmund L. Andrews, "Fed and Regulators Shrugged as the Subprime Crisis Spread," *New York Times,* December 18, 2007.

8 Center for Responsible Lending, "Subprime Lending is a Net Drain on Homeownership" (2007).

9 In 2005, there were ten metropolitan areas where more than 50 percent of all refinance lending took the form of subprime loans, five of which were in Texas. Allen J. Fishbein and Patrick Woodall, "Subprime Locations: Patterns of Geographic Disparity in Subprime Lending" (Washington: Consumer Federation of America, 2006). At a finer grain, subprime loans represented between 60 and 74 percent of all lending in 2006 in seven census tracts in Irvington, NJ, a predominately black inner-ring suburb of Newark.

10 The Mortgage Lender Implode-o-Meter, available at http://ml-implode.com (accessed February 16, 2008).

11 RealtyTrac®, "U.S. Foreclosure Activity Up 75 Percent in 2007." Press Release, January 29, 2008. Some properties are the subject of more than one filing.

12 The relation between the initiation of a foreclosure proceeding and the completion of the foreclosure varies widely. According to recent anecdotal sources, in Massachusetts, 85 percent of filings end in foreclosure, while in Baltimore, the figure is 70 percent. A study of 5,000 subprime loans originated between 2001 and 2005 on which foreclosures were initiated found that 50 percent ended up as real estate owned (REO) property, 34 percent had the loans paid off, and in 16 percent the default was cured by the borrower. It is unclear how many of the loans that were paid off involved a short sale or other proceeding resulting in the loss of the home. Anthony Pennington-Cross, "The Duration of Foreclosures in the Subprime Mortgage Market: A Competing Risks Model with Mixing." Working Paper 2006-027A (St. Louis: Federal Reserve Bank of St. Louis,

Research Division, 2006).

13 Center for Responsible Lending, "Subprime Lending is a Net Drain on Homeownership."

14 In a related development, at the end of 2005 the national homeowner vacancy rate reached 2.0 percent, a level that had never even been approached since quarterly tracking by the U.S. Census Bureau began in 1960. In the fourth quarter of 2007, the rate had risen to 2.8 percent. The rental vacancy rate, although high by historical standards, has been dropping since peaking early in 2004.

15 Mortgage Bankers Association, "Delinquencies and Foreclosures Increase in Latest MBA National Delinquency Survey." Press Release, March 6, 2008.

16 The racial disparities in subprime lending are dramatic, and cut across all income categories. Research by the Center for Responsible Lending found that upper income blacks were more than three times as likely to receive either a home purchase or refinancing loan from a subprime lender than upper-income white borrowers. See Center for Responsible Lending, "African-American Homes at Risk" (2004). See also U.S. Department of Housing and Urban Development, "Unequal Burden: Income and Racial Disparities in Subprime Lending in America" (2000); and Bradford, "Risk or Race?"

17 See Alan Greenblatt, "Two Faces of Foreclosure." *Governing,* April 2008, for a report comparing the impact of foreclosures in Dayton, OH, and Las Vegas, NV.

18 Information from GMAC-RFC, cited in Desiree Hatcher, "Foreclosure Alternatives: The Case for Preserving Home Ownership" *Profitwise News and Views,* Federal Reserve Bank of Chicago, February 2006.

19 Temple University Center for Public Policy and Eastern Philadelphia Organizing Project, "Blight-Free Philadelphia: A Public-Private Strategy to Create and Enhance Neighborhood Value" (2001). Similar findings were reported in a recent study, ReBuild Ohio and Community Research Partners, "$60 Million and Counting: The Cost of Vacant and Abandoned Properties to Eight Ohio Cities" (2008).

20 Claudia Colton, Kristen Mikelbank, and Michael Schramm, "Foreclosure and Beyond: A Report on Ownership and Housing Values Following Sheriff's Sales, Cleveland and Cuyahoga County, 2000-2007" (Cleveland: Case Western Reserve University, Center on Urban Poverty and Community Development, 2008).

21 Teresa Dixon Murray and Mark Gillispie, "Housing Price Collapse Steals from All Our Pockets." Cleveland Plain Dealer, March 23, 2008.

22 Jim Rokakis, "The Shadow of Debt: Slavic Village is Fast Becoming a Ghost Town. It's Not Alone." *Washington Post,* September 30, 2007.

23 Mark Whitehouse, "Subprime Aftermath: Losing the Family Home." *Wall Street Journal,* May 30, 2007. There is no question that a neighborhood can deteriorate to the point where the real estate market effectively ceases to exist. I have studied a neighborhood in Buffalo, NY, known as the Broadway-Fillmore area. In 2000, the area, which includes four census tracts, contained 8,425 one- to four-family units, largely in single-family structures. Of these, roughly 25 to 30 percent were vacant. Between 2003 and 2005, only 35 mortgages for home purchase were recorded in this area, an average of 11.6 per year, or 1.3 per 1,000 one-to-four family units. At this point, the likelihood of any given property in this area finding a buyer is so small that there is no economic reason for an owner to retain the property and pay taxes and insurance on it.

24 This point has yet, to my knowledge, to be substantiated by quantitative research, but reflects the observations of local officials, Community Development Corporation staff, and other knowledgable observers in a wide range of cities in the Northeast and Midwest. Examples would include Slavic Village and Mount Pleasant in Cleveland, and Vailsburg and Roseville in Newark, New Jersey.

25 The effects of foreclosure in declining property values and increased crime have been documented in Dan Immergluck and Geoff Smith, "The External Costs of Foreclosure: The Impact of Single-Family Mortgage Foreclosures on Property Values." *Housing Policy Debate* 17 (1) (2006): 57–79; and "The Impact of Single-Family Mortgage Foreclosures on Neighborhood Crime." *Housing Studies* 21 (6) (2006): 851–866. The effects on municipal services are analyzed in William C. Apgar and Mark Duda, "Collateral

Damage: The Municipal Impact of Today's Mortgage Foreclosure Boom" (Minneapolis: Homeownership Preservation Foundation, 2005).

26 In a decision overturning Michigan regulations, *Watters v. Wachovia Bank, N.A ,* 127 Sup. Ct. 1559, the U.S. Supreme Court held early in 2007 that federal pre-emption extended to nonbank subsidiaries of federally chartered banks, whether or not the federal agencies were exercising regulatory oversight over those subsidiaries. State regulators are barred from enacting or enforcing regulations affecting these entities.

27 The possibility exists of future federal action that would preempt state regulation of mortgage brokers, but it does not appear to be probable at this point. Although some versions of H.R.3915 apparently contained preemption provisions, the version passed by the House does not, although it establishes minimum standards for state regulation of mortgage brokers.

28 Mortgage Bankers Association, "Residential Mortgage Origination Channels," *Data Note* (September, 2006).

29 A detailed analysis of this issue is found in Kathleen C. Engel, "Do Cities Have Standing? Redressing the Externalities of Predatory Lending." Research Paper 05-114 (Cleveland-Marshall School of Law, 2005), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=774351.

30 These data come from financial consultant John Mauldin, available at www.2000wave.com (accessed January 14, 2008).

31 Estimates vary widely of the extent to which the various pools of outstanding mortgages are at risk; moreover, these estimates are regularly being adjusted upward as the crisis continues and spreads to loans not generally considered subprime, such as the intermediate Alt-A loans. Estimates of potential risk are as high as 50 percent of ARM resets, or 36 percent of subprime loan portfolios generally. A recent publication, "Subprime Spillover: Foreclosures Cost Neighbors $202 Billion, 40.6 Million Homes Lose $5,000 on Average" (Durham, NC: Center for Responsible Lending, 2008), cites a variety of estimates made by different organizations.

32 In addition to raising state funds for this purpose, states can take advantage of the funds appropriated by Congress to NeighborWorks America (NWA). Late in 2007, NWA received a special $180 million federal appropriation to provide training and make grants to HUD-approved housing counseling intermediaries and to qualifying state housing finance agencies. NWA will provide at least $167.8 million to qualifying organizations providing mortgage foreclosure mitigation assistance, primarily in states and areas with high rates of defaults and foreclosures.

33 Given the limited counseling infrastructure in many states, some resources will have to be devoted initially to training additional foreclosure prevention counselors.

34 State of Pennsylviania, "Harvard's Kennedy School Recognizes Three PA Programs among Nation's Most Innovative." Press release, March 2006, available at www.state.pa.us/papower/cwp/view.asp?A=11&Q=450985 (accessed March 22, 2008).

35 Data from First American Loan Performance, cited by Federal Reserve Board Chair Ben Bernanke in speech to the Independent Community Bankers of America Annual Convention, Orlando, Florida, March 4, 2008, available at www.federalreserve.gov/newsevents/speech/bernanke20080304a.htm

36 The state estimates that these funds will enable roughly 500 to 700 borrowers to refinance their loans. According to the Joint Economic Committee of the U.S. Congress, 364,433 subprime mortgages are outstanding in New York State, of which nearly 68,000 are expected to go into foreclosure by the end of 2009. Assuming all 500 to 700 program beneficiaries are at high risk of foreclosure, it will benefit at most one in 100 in need. Given the uncertainties of the process, it is likely that a significant percentage of those who refinance would not have gone into foreclosure; therefore, the actual ratio of beneficiaries to those in genuine need will be substantially worse than the 1:100 best case scenario.

37 A compendium of such programs, entitled "State Mortgage Assistance and Refinance Programs," is available from the National Governors Association Center for Best Practices at www.nga.org/portal/site/nga/menuitem.9123e83a1f6786440ddcbeeb501010a0/vgnextoid=aadc799400526110VgnVCM1000001a01010aRCRD.

38 See the decision of the U.S. Supreme Court in *BFP v. Resolution Trust Corporation*, 114 Sup.Ct. 1757 (1994), which held that the provisions of federal bankruptcy law did not supersede state foreclosure law. State laws provide for two distinct foreclosure procedures, one for foreclosure of liens created through failure to pay property taxes (tax foreclosure), and another for foreclosure of liens secured by mortgages. Except where specific reference is made to tax foreclosure, the discussion in this paper deals with the latter.

39 A broker might argue, of course, that he or she was misled by a "rogue" appraiser. It is unlikely, however, that an appraiser would knowingly misrepresent the value of a property unless encouraged or coerced by a party to the transaction.

40 A similar proposal has been put forward by the Center for Economic and Policy Research, entitled the Subprime Borrower Protection Plan. See www.cepr.net/index.php/op-eds-columns/op-eds-columns/the-subprime-borrower-protection-plan/.

41 The U.S. Supreme Court upheld an open-ended moratorium on foreclosures in *Home Building and Loan Assoc. v. Blaisdell,* 290 U.S.398 (1934).

42 Thus, we no longer have debtor's prisons or permit forced labor to work off debts.

43 Alternatively, if the property was vacant and the creditor had not taken any steps to initiate foreclosure, the state or municipality could obtain a court order requiring it to do so, and pursue it aggressively, or forfeit the right to do so to the state.

44 The legal doctrine of *laches*, in that the creditor, in the ancient phrase, has "slept on its rights," could be seen as relevant to this point.

45 The term "REO (Real Estate Owned) property" or properties is universally used in the real estate and housing industries to refer to the inventory of properties taken and held by lenders, servicers, and similar entities.

46 See, for example, John Leland, "Baltimore Finds Foreclosure Crisis Snags Women." *New York Times,* January 15, 2008 describing the crisis in the city's Belair-Edison neighborhood.

47 New Jersey has the strongest such state statute, which provides that the municipality shall have recourse to collect for the costs of nuisance abatement or receivership against "any asset of the owner of the property if an individual, any asset of any partner if a partnership, and against any asset of any owner of a 10 percent interest or greater if the owner is any other business organization or entity recognized pursuant to law" (N.J. Statutes Annotated 55:19-100).

48 The full language of the definition is as follows: "Any person, agent, operator, firm or corporation having a legal or equitable interest in the property; or recorded in the official records of the state, county or municipality as holding title to the property; or otherwise having control of the property, including the guardian of the estate of any such person and the executor or administration of the estate of any such person if order to take possession of real property by a court." Sec. 202, 2006 New York State Property Maintenance Code.

49 On that basis, the Housing Court in Buffalo, NY, has held that that the letters banks send owners threatening foreclosure show "that they have begun to assert some measure of control" on the basis of which they can be ordered to correct violations, and, failing to do so, be fined by the court. Michael Orey, "Dirty Deeds." *Business Week,* January 3, 2008.

50 The lender must exercise the abandonment clause in the mortgage, register the property with the city, and immediately begin to secure and maintain the property to the neighborhood standard. The lender must also hire a local company to inspect the property weekly and handle maintenance and security of the property. The company must have a 24-hour contact number, which must be posted on the property. The program, which is similar to that in other California cities, was established pursuant to Chula Vista Ordinance No. 3080, adopted August 7, 2007. See www.chulavistaca.gov/City_Services/Development_Services/Planning_Building/Default.asp.

51 For instance, New Jersey, where the state nuisance abatement statute defines "owner" as the "holder or holders of title in fee simple" (N.J. Statutes Annotated 40:48-2.4).

52 This has been the practice since 1999 in Wayne County, MI (which includes the city of Detroit). The county identifies nuisance properties, files a suit in Circuit Court

alleging the property is a nuisance, and notifies the owners. If the owner fails to repair the property, enter into an agreement with the county to repair the property, or sell the property to someone who agrees to repair it within a certain time, the county takes title to the property through a default judgment. The county then sells the property to an entity that agrees to repair the property and maintain it in habitable condition. See Andrew Dick, "Blight Fight," *Planning* 73 (6) (2007).

53 Two cities that have made concerted efforts to address these issues, Cleveland and Buffalo, both have dedicated housing courts served by full-time specialist judges, although in Buffalo the housing court exists by virtue of a particular judge's efforts, rather than—as in Cleveland—by statute.

54 The Michigan accelerated foreclosure process was enacted as Public Act 123 of 1999. For further information, see "Genesee County Land Bank Property Acquisition Process" available at www.thelandbank.org/prop_acquisition.asp.

55 The Iowa statute is short and to the point: "for the purposes of [the statutory provisions governing eminent domain] a city may condemn a residential building found to be a public nuisance and take title to the property for the public purpose of disposing of the property […] by conveying the property to a private individual for rehabilitation or for demolition and construction of housing." (Iowa Code Annotated, Title IX, Chapter 364.12A). This provision was enacted in 1996.

56 Both the savings and loan crisis of the late 1980s and the foreclosure crisis during the Great Depression triggered federal responses in the form of the Resolution Trust Corporation, which took over and recycled nearly $400 billion in savings and loan assets between 1989 and 1995, and the Home Owners' Loan Corporation (HOLC), created in 1933 to refinance mortgages of homeowners at risk of foreclosure. The history of the HOLC offers useful lessons for the current crisis. The HOLC was initially authorized to issue $2 billion in bonds, which are worth from $30 billion (based on the Consumer Price Index) to $468 billion (based on share of gross domestic product) in 2007 dollars. During its lifetime, the HOLC made more than one million refinancing loans, equivalent to roughly 20 percent of all the mortgage loans in the United States. When the bonds were paid off and the HOLC dissolved in 1951, it had generated a $14 million surplus, which it paid to the U.S. Treasury. A discussion of the HOLC that draws parallels between the situation then and now, is in Alex J. Pollock, "Crisis Intervention in Housing Finance: The Home Owners' Loan Corporation" (Washington, DC: American Enterprise Institute for Public Policy, 2007). The Center for American Progress has proposed a plan, the "Save America's Family Equity" or SAFE plan, modeled on the HOLC. See Michael Barr, "Strengthening Our Economy: Foreclosure Prevention and Neighborhood Preservation" (Washington: Center for American Progress, 2008), available at www.americanprogress.org/issues/2008/01/barr_testimony.html.

57 Although this scenario is not problematic, it is included because if a PRE acquires properties wholesale from servicers, its pool is likely to include at least a few where the mortgage and the borrower are not at risk.

58 The regulations would apply to "higher-priced mortgage," a category that, as defined by the Federal Reserve, would cover nearly all subprime loans. The proposed regulations, which take the form of an amendment to Regulation Z, 12 CFR 226, were published in the *Federal Register* on January 9, 2008.

59 For an invaluable comparison of the state laws dealing with regulation of mortgage brokers, see Cynthia Pahl, "A Compilation of State Mortgage Broker Laws and Regulations 1996–2006" (Minneapolis: Community Affairs Department of the Federal Reserve Bank of Minneapolis, 2007).

60 A surety bond is a form of insurance under which a third party, typically an insurance company, guarantees that the mortgage broker will carry out his or her legal obligations to her clients. In the event that the broker fails to perform or defaults on an obligation, the insurance company is obligated to make the clients good up to the maximum amount of the bond.

61 Recently, the Massachusetts State Auditor issued a report calling on the state to give the state's Division of Banks more resources to deal with the increase in the number of mortgage brokers, noting that during the first nine months of 2007, the division was able to examine only 16 percent of the licensed mortgage brokers in the state. See Massachusetts State

Auditor, "DeNucci Says Division of Banks Needs More Resources to Strengthen Oversight of Mortgage Industry." Press Release (November 27, 2007). Similarly, a 2005 newspaper article in Ohio noted that, "State oversight is tepid. Brokers are paying less in fines even as state officials document more wrongdoing. Millions in state licensing fees, meant for enforcement, have been spent instead on keeping the state budget afloat." See Geoff Dutton, "Ohio's Disgrace: No. 1 in Home Foreclosures," *Columbus Dispatch,* September 18, 2005.

62 205 Illinois Compiled Statutes 635/4-16 enacted in 2007.

63 The industry has resisted states' efforts to adopt a fiduciary standard, for fear of the potential legal liability that it might impose on brokers who failed to act in their borrowers' best interests. This has led to compromises in Ohio and Colorado, where bills that originally set fiduciary standards were amended to require "good faith and fair dealing." This is sometimes characterized as a "duty of care" standard.

64 See the decision of the California Supreme Court in *Wyatt v. Union Mortgage Co.,* 24 Cal.3d 773, 598 P.2d 452 (1979). Also see Peter J. Hong and Marcos Reza, "Hidden Costs to Homeowners: The Prevalent Non-Disclosure of Yield Spread Premiums in Mortgage Loan Transactions," *Loyola Consumer Law Review,* 18 (2) (2005): 131–150.

65 In the case of ARMs, the borrower must be able to make payments at the fully indexed rate of the loan.

66 The fully indexed rate is the sum of the index used to determine the interest rate, and the margin between that index and the interest rate charged the borrower. If the index is LIBOR, and LIBOR is at 6.5 percent and the margin is 4 percent, the fully indexed rate is 10.5 percent.

67 The criteria are as follows: (1) The new monthly payment must be lower than the total of all monthly obligations being financed, taking into account costs and fees; (2) there must be a beneficial change in the amortization period; (3) the borrower receives cash in excess of the costs and fees as a part of the refinancing; (4) the previous note rate of interest is being reduced; (5) there is change from an adjusted rate to a fixed rate loan; or (6) the refinancing is necessary to respond to a bona fide personal need, or an order of a court.

68 Kenneth R. Harney, "The Lowdown on Low Doc Loans." *Washington Post,* November. 25, 2006.

69 Mara Der Hovanesian, "Nightmare Mortgages." *Business Week,* September 11, 2006. Option ARMs permit the borrower to choose for a limited period from a variety of payment choices, including some that result in negative amortization; that is, the payments cover less than the interest on the loan, and the difference is added to the principal. Ultimately, usually within a short time, mortgage payments rise dramatically, even more than with conventional ARMs.

70 205 Illinois Compiled Statutes 635/5-8.

Acknowledgments

The author wishes to acknowledge Frank Ford, Neighborhood Progress, Inc.; Kermit J. Lind, Esq., Cleveland-Marshall School of Law; Dan Immergluck, Georgia Tech; Dede Myers, Federal Reserve Bank of Philadelphia; Joe Schilling, Virginia Tech; and Harold Simon for their insightful comments on early drafts of this paper.

The Brookings Institution thanks the Surdna Foundation, the Ford Foundation, the F. B. Heron Foundation, the Charles Stewart Mott Foundation, and the Kresge Foundation for their generous support of this work.

For More Information

Alan Mallach
PO Box 623
Roosevelt, NJ 08555
amallach@comcast.net

Jennifer Vey
Metropolitan Policy Program
Brookings Institution
202-797-6143
jvey@brookings.edu

For General Information

Brookings Institution Metropolitan Policy Program
(202) 797-6139
www.brookings.edu/metro

BROOKINGS

1775 Massachusetts Avenue, NW
Washington, DC 20036
telephone 202.797.6000
fax 202.797.6004
web site www.brookings.edu

Metropolitan Policy Program
at BROOKINGS

telephone 202.797.6139
fax 202.797.2965
web site www.brookings.edu/metro