nerej CELEBRATING 55 YEARS

Correcting market abuse: Congress gets into the act

December 29, 2007 - Spotlights

Residential markets have taken hard hits as result of lower demand, oversupply in some markets, and grave concerns about lending practices and their effect on homeowners and their markets. No ready correction is in sight. All signs point to a period where many markets will not show a positive trend and may show rather alarming negative signs.

Of course, things could change overnight. This could all be at the end and come the new year, all will be forgiven and good times will be ahead of us. However, there is nothing that suggest that salvation is yet at hand. Just like in other downturns, a return to something we can call stability may be on a distant timeline over a long horizon.

The effects of the sub prime meltdown are continuing to be felt. Just as many homeowners could take advantage of cheap credit, prices are not co-operating and lenders are making it more difficult to obtain what was previously easy money.

Many areas of the country, including New England, are suffering from vacancies, foreclosures, and other difficulties resulting from the housing downturn and the credit squeeze. Oversupplied condos and new construction homes are a problem but there is a troubling amount of existing home inventory. Some of this is due to natural oversupply, and some is due to the effects of speculation, and some is due to fraud.

As noted in previous articles, the current situation offers challenges for real estate professionals and especially for appraisers. Appraisers have the opportunity to dispel some of the bad press received for overvaluations and willing/unwilling participants in legal, not so legal, and simply illegal schemes.

Congress has gotten into the act. The problem has become prominent enough for action on the federal level.

As of October 22, reps. Brad Miller (D-NC), Mel Watt (D-NC) and Barney Frank (D-MA) introduced comprehensive legislation to combat abuses in the mortgage lending market, and to provide basic protections to mortgage consumers and investors. Based on the press release, the bill, H.R. 3915, the "The Mortgage Reform and Anti-Predatory Lending Act of 2007" proposes mortgage practice reforms in three areas.

First, the bill will establish a federal duty of care, prohibit steering, and call for licensing and registration of mortgage originators, including brokers and bank loan officers. Second, the new legislation will set a minimum standard for all mortgages which states that borrowers must have a reasonable ability to repay. Third, the legislation attaches limited liability to secondary market securitizers who package and sell interest in home mortgage loans outside of these standards. However, individual investors in these securities would not be liable. Finally, the bill expands and enhances consumer protections for "high-cost loans" under the Home Ownership and Equity Protection Act and includes important protections for renters of foreclosed homes.

According to the press release, "Barney Frank, Mel Watt and I see protecting vulnerable homeowners from predatory mortgage lenders as a core, defining Democratic value. When a family's home is a stake, lenders had better play by a fair set of rules," said Miller.

"This bill represents a significant step forward to clean up and prevent a number of the questionable practices that, unfortunately, took hold in the mortgage lending industry in the last several years. I hope the industry will embrace the changes and allow the bill to move forward quickly," said Watt.

The bill also contains foreclosure protections for renters. As the press release states, "in case of foreclosure, any successor who takes over the property will have to honor preexisting leases." The press release goes on to say, "tenants without a lease will have at least 90 days before being required to vacate." In addition, the bill will incorporate recommendations by rep. Melissa Bean (D-IL) to require counseling for certain first time home buyers; and rep. Chris Murphy's (D-CT) anti-steering legislation.

To this end, Frank has been active in developing the beginnings of a governmental response to the mortgage problems. In response to the lack of progress in helping at-risk homeowners prevent foreclosure, the congressman who is chairman of the house committee on financial services, announced that he will host a workshop at the Federal Reserve Bank in Boston on October 26 at 9:30 a.m., with banking regulators, mortgage lenders, banks, credit unions, housing advocates, community groups and others, to facilitate discussions on how to best to help homeowners with troubled mortgages. Congressman Frank will be joined by invited state and local elected officials. The workshop will not be open to the press.

On a higher level, a group of banks is proposing a private fund to help bailout investors who have gotten into trouble with high yield, high risk loan pools. The fed acting decisively several weeks by lowering benchmarks which in turn allowed mortgage and other debt rates to trend lower, thus providing some relief in markets.

There has been discussion of involving the FHA/HUD in helping out borrowers under financial duress. States have also been active in attempting to convince lenders to work with borrowers.

Many problems have been exacerbated by the many lenders who have gone out of business. The result of this is that many borrowers have nowhere to go.

The "resets" of many variable instruments are coming due. This has the potential of creating a new wave of potential problem loans as borrowers will not be able to afford the higher rates created under these variable rate mortgages.

Where this will all end is a matter of some conjecture. The matter is serious for the ordinarily slow wheels of government to begin attempt some remedy of the problem.

William Pastuszek, Jr., MAI, SRA, is the principal of Shepherd Associates, Newton, Mass.