THE MORTGAGE CRISIS

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"1 in every 10 home loans are in default"[1]

The mortgage crisis is a serious problem for the homeowner, the banker, the investor, the American citizen and, ultimately, the world citizen. No matter what your interest in the crisis, the result may well be difficult to manage. For bankruptcy lawyers, the crisis is a source of business, but it also is a source of frustration and helplessness.

This paper will discuss briefly the history of the crisis, the future of the crisis and what it may be useful for bankruptcy practitioners to know about proposed solutions to the crisis.

I. The Facts

How did we get to this point? There are approximately $11 trillion of home mortgages in the United States. Of those, $ 1 trillion are subprime mortgages, $1 trillion are Alt-A mortgages, and $500-600 billion are option ARMS. Between 2008 and 2011, most of these mortgages will have interest rates that will have reset at levels above the original interest rate. If mortgagors cannot pay the increased payments, or, if they default before the interest rates reset, there will be foreclosures of those mortgages or the mortgages will have to be modified. Many people relied on the fact that, since the Great Depression, home values have never gone down, only up. This crisis has caused so much concern that some investors are insuring against the entire monetary system of the United States collapsing.[2]

A. Structure of the Loans

Most of the subprime, Alt-A and option ARM mortgages were sold to investors in the form of securities - asset-backed securities or ABS. These loans were also called mortgage-backed securities or MBS. The loans were sold by the original issuing bank to a Wall Street underwriter. The loans were pooled with hundreds or thousands of other loans and interests in the pool were sold as securities to investors. Some of the loans were divided into strips or tranches which were sold as securities. The tranches had differing risks based upon the piece of the mortgages that the tranche held. For instance, if an investor held the right to the first 3 or 5 years of payments on the mortgages in the pool, that tranche would have a high likelihood of

[1] Mortgage Bankers Association, December 2008.

[2] The mortgage crisis has created greater fear than ever before that countries themselves may default on their debts. As of November 2008, the Bespoke Investment Group reported that the cost of insuring against a default by the U.S. Government rose from $8 per $10,000 in January 2008 to $66.90 per $10,000. This is a 87.4% increase. Prieur du Plessis, *Credit Crisis Watch: Signs of Progress*, SafeHaven, *available at* http://www.safehaven.com/showarticle.cfm?id=12162 (December 24, 2008).

being fully paid. That tranche was rated AAA by the rating agencies and sold at a high value. The lowest tranche, rated B, might include all payments in the last 5 years of the mortgages pooled. Since the risk of default by the mortgagors before that date would be the highest risk in the pool, that tranche would sell at a substantial discount, but, if a significant number of the mortgagors paid their loans in full, the investors would make a substantial profit.

Securitization of mortgages is a relatively new phenomenon. Prior to the pooling or securitization of mortgages, a lender would sell mortgages to Fannie Mae (FNMA) or Freddie Mac (FHLMC). Then the loans were sold to investors who relied on the collateral for value as well as the guarantees provided by FNMA and FHLMC. In 1995, the first ABS or MBS was issued. Due to the high ratings of the pools by the rating agencies such as Standard & Poor=s and Moody=s, the MBS market exploded. In the last 13 years, this market has gone from 0 to $3.5 trillion of ABS issued.[3] The market=s appetite for ABSs was so great that the lenders, with the aid of mortgage brokers, became careless. Loans were granted to almost any borrower regardless of the borrower=s financial wherewithal. Loans were granted with little or no financial information from the borrower at all. Such loans were called “liar loans” or “ninja loans.” (No income, no job or assets).

B. Types of Loans

There are two main forms of MBS that are causing problems: subprime mortgages and Alt-A mortgages. Option ARMS are a subset of Alt-A mortgages. They are discussed separately in this paper due to the different dates of reset and additional troubling features. Subprime mortgages are, in general, loans that do not meet Fannie Mae or Freddie Mac guidelines. The credit score of a subprime borrower is usually 500-620 of a possible 850 points. About 25% of the population=s credit scores are subprime.[4] Alt-A loans are loans whose quality is worse than prime loans that meet Fannie Mae and Freddie Mac guidelines but whose quality is better than subprime loans. Alt-A loans “are made to persons with relatively good credit histories but have features that render them non-conforming.”[5] The types of features that might make a loan non-conforming include

> (1) a lack of financial documentation of income and assets; (2) a debt-to-income ration or a loan-to-value ratio that is too high, considering the borrower=s credit, assets, and the type of property that will be financed; (3) a credit history with too many problems to qualify as prime, but not so many as to qualify as subprime; or (4) the loan structure, such as (a) an Option ARM, which allow the borrower to elect to pay less than the full amount of interest due, so that the loan negatively amortizes as the unpaid interest is added to the principal (b) a piggy-back “80-20” loan, whereby the first priority loan of 80% of the value is combined with a

[3] Thompson Financial

[4] Cohen, Ezra, *Mortgage Meltdown Overview: Causes, Crisis and Current Status*, Institute of Continuing Legal Education in Georgia, August, 2008, at 6.

[5] *Id.*

> second-priority loan for 20% of the value, so that private mortgage insurance is not required, or home-equity, second-priority loans where the total amount of the first and second mortgages equal 125% of the value of the home.[6]

Option ARMs are adjustable rate mortgages that reset as other ARMs do, but with the added flexibility of different payment plans. The borrower can choose to make (1) a minimum payment at a teaser, low rate (2) a deferred payment where the borrower makes minimal monthly payments and the loan actually negatively amortizes (3) an interest-only payment or (4) a fully amortizing payment. "Up to 80% of all option ARM borrowers make only the minimum payment each month, according to Fitch Ratings."[7] "The option ARM is 'like the neutron bomb,' says George McCarthy, a housing economist at New York=s Ford Foundation. 'It's going to kill all the people but leave the houses standing.'"[8]

C. Housing

In November 2008, sales prices for existing homes fell 13% from November 2007 to $181,300. This is "'probably the largest price decline since the Great Depression,' National Association of Realtors Chief Economist Lawrence Yun said."[9] Sales of existing homes slid to an annual rate of 4.49 million, lower than forecast.[10] The Commerce Department also reported that new home sales fell 2.9% in November 2008 to a 17-year low. The median sales price also declined 11.5% from a year earlier.[11] New housing starts have dropped from 2.3 million in January 2006 to 791,00 in October 2008. This is a post-World War II low.[12] About 12 million homeowners have a mortgage that is higher than the value of their homes.[13] About 29% of those who purchased homes since 2003 are underwater.[14] Gary Shilling, a noted real estate economist

[6] *Id.*

[7] Mara Der Horanesian, *Nightmare Mortgages*, BUSINESS WEEK, September 11, 2006, available at http://www.businessweek.com/magazine/content/06_37/b4000001.htm

[8] *Id.*

[9] Shobhana Chandra, *U.S. Home Resales All; Prices Drop by Record 13.2%*, at http://www.bloomberg.com/apps/news?pid=206010688sid=av.sqUTa2.T084refer=home, (December 23, 2008).

[10] *Id.*

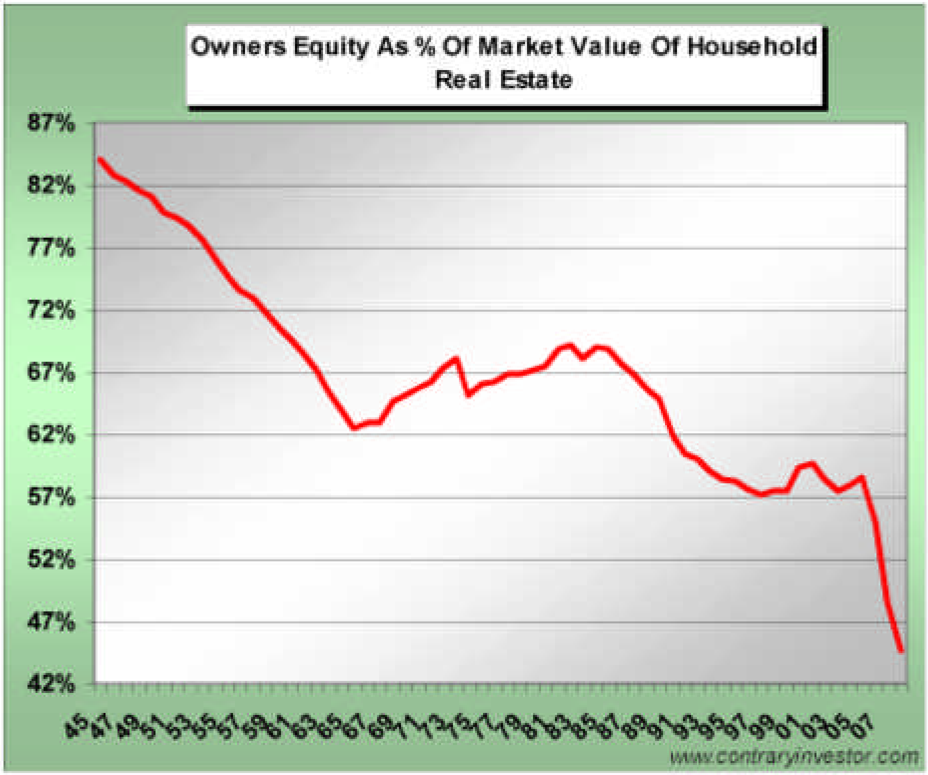
[11] *Id.*

[12] Gary Shilling, *Semi-Annual U.S. Economic Outlook: Collapsing On Schedule*, at http://www.investorinsight.com/blogs/john_mauldins_outside_the_box/archive/2008/12/15/semi-annual -u-s-economic-outlook-collapsing-on-schedule.aspx, (December 15, 2008).

[13] *Id.*

[14] *Id.*

and expert predicts that home prices will decline 37% on average before the crisis is over. That would mean that 25 million mortgagors or 2 of all borrowers would be upside-down in their mortgages.[15] The chart below illustrates the decline in homeowners= equity in their homes.



In Georgia, 23.2% of homeowners have no equity in their homes; in Florida, 29.2% are underwater; in Alabama, 7.4% have negative equity.[16]

II. The Future

Credit Suisse has charted the timing of the monthly mortgage rate resets of subprime, Alt-A and option ARM loans. The graph is shown at the end of this section. The subprime mortgage resets peaked in 2007-2009. The Alt-A and Option ARM resets peak in 2009-2011. This means that the nation and world are only partially through the home loan part of this crisis. If Credit Suisse is correct, over $1 trillion of residential loans will reset from 2009 to 2011. Whitney

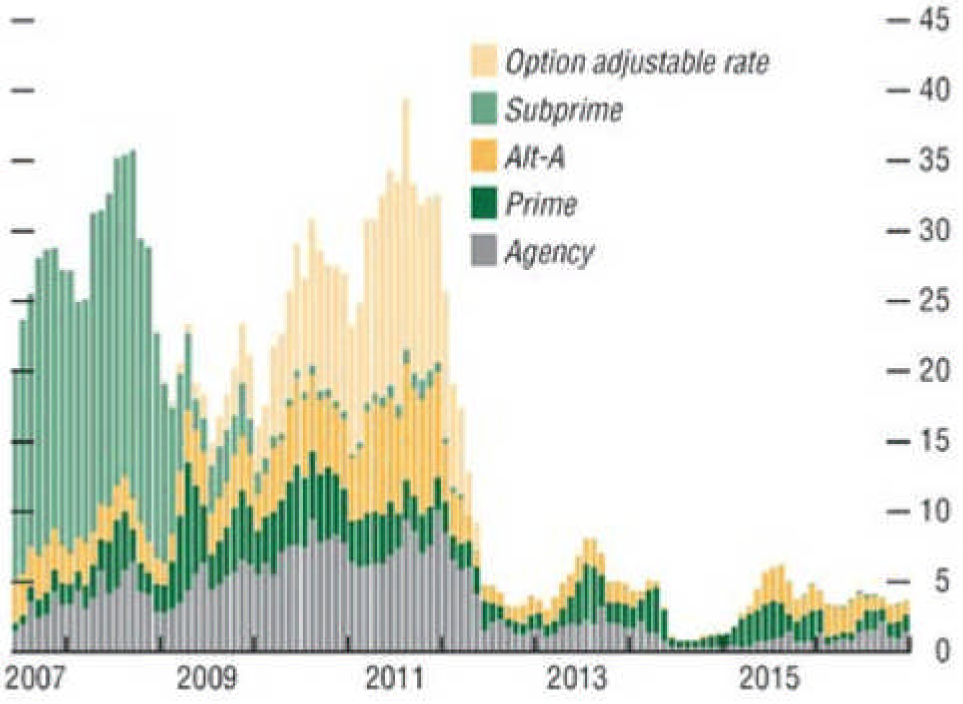
[15] *Id.*

[16] K.A. Turner, *Numbers Tell Economic Tale*, MOBILE ALABAMA PRESS-REGISTER, January 4, 2009 (quoting statistics of First American CoreLogic).

Tilson of Tilson Funds, who predicted the mortgage crisis before it occurred, has opined that the option ARM default rates will be as high as 70%.[17]

Figure 1.7. Monthly Mortgage Rate Resets

(First reset in billions of U.S. dollars)



Source: Credit Suisse.

A. The Fallout

Investors in securitized mortgage pools are suing a variety of parties over the mortgage mess. The early targets were the entities and individuals who were responsible for the loans' existence and pooling and sale. "Possible targets include home buyers who lied about their income, lenders that made bad loans, securities firms that packaged the loans into securities for investors, and credit agencies that graded the securities as safe investments."[18] One suit, already filed, claims that Countrywide Financial misled investors about its financial condition.[19] In

[17] *The Mortgage Meltdown* (Sixty Minutes, CBS News Broadcast, December 14, 2008).

[18] Debra Cassens Weiss, *Suits Follow Mortgage Meltdown*, A.B.A. J., at http://www.abajournal.com/news/suits_follow_mortgage_meltdown/(September 11, 2007).

[19] *Id.*

another, National City Mortgage has been sued on the basis that National City gave loans to buyers whom they knew were poor risks.[20]

Another type of suit is suits by investors against the trustees or managers of the pooling agreements or the servicers of the mortgages. There is at least one suit by investors against Bank of America because it intends to modify mortgages as part of a compromise reached with governmental authorities.[21] Bank of America settled charges made against it by 15 state attorneys general due to Countrywide Financial=s loan portfolio which Bank of America bought. The settlement stemmed from charges that Countrywide Financial had engaged in predatory lending practices. Bank of America, to settle the suit, agreed to modify the mortgages of as many as 400,000 borrowers by reducing interest rates and reducing principal balances of loans. About 75% of the loans are loans in which Bank of America exercises "delegated authority" as provided in investor contracts. Some of the investors are unhappy with the settlement and believe that they should have been contacted before the settlement. They are seeking to have Bank of America repurchase the loans, if modified.[22]

The "delegated authority" agreements usually provided that mortgage servicers or those who manage the pooled mortgages have the authority "to rework loans when it is likely to benefit investors. But just how much authority the mortgage companies have is open to debate."[23] The problem with modifications is that they may benefit some investors while injuring others. The servicer or trustee has a problem serving all interests fairly. The Bank of America suit alleges that the modifications proposed will short investors $8.4 billion.[24] "Investors' voices have been muted in this debate because they speak of an inconvenient truth: Current solutions sacrifice the long-term viability of this nation=s housing finance system for short-term political gain. No matter how noble the intent, it is not in the interest of the United States now, or in the future, to tell its citizens and the world at large that U.S. contract rights may be bent with the political winds."[25]

Bank of America and other servicers and managers of pooled mortgages assert that "modifications designed to yield greater cash flow to investors. . .compared to net liquidation

[20] Tom Bayles, *Investors Bring Suit Against Their Lender*, SARASOTA HERALD TRIBUNE, http://www.heraldtribune.com/article/20080517/REALESTATE/805170631/1438 (May 17, 2008).

[21] Mara Der Hovanesian, *Investor Sues to Block Mortgage Modifications*, BUSINESS WEEK, December 1, 2008.

[22] Ruth Simon, *Investors Hit B of B Loan Modifications*, THE WALL STREET JOURNAL, November 18, 2008.

[23] *Id.*

[24] Der Hovanesian, *supra.*, note 21, at p.6.

[25] *Id.*, quoting William Frey, the named plaintiff in the Bank of America suit.

proceeds from a foreclosure are not only legally permitted, they are arguably required of the servicer. In a market environment where loss severities on foreclosures exceed 50%, loan modifications are not only a useful tool in protecting investors, but they also keep homeowners in their homesBtruly a win/win result."[26] The servicers also allege that acting in the best interest of the investors standard, the standard to which servicers are held, means that they are to act in a manner that is best for the entire pool of investors, regardless of how the decision may impact any one class of investors.[27]

Investors are using the "sanctity of contract" and "preservation of the mortgage markets" arguments against lenders in their suits. The lenders have used the same arguments over the years in their discussions with Congress as to why home loans should not be crammed down (the amount of the mortgage reduced to the market value of the home) in chapter 13 bankruptcy cases. "The favorable treatment of residential mortgagees was intended to encourage the flow of capital into the home lending market."[28] The special protections given home loans have allowed and encouraged the residential mortgage industry to create riskier mortgage products because the risk of the loans fell mainly on the homeowners in a market of rising real estate values. However, in a market of declining real estate values, the risk of the loans also falls on the lenders. Now their investors want protection, just as the lenders did from homeowners' bankruptcies.[29]

III. The Fix

A. Troubled Assets Relief Program

Congress established the Troubled Assets Relief Program (TARP) as a part of the Emergency Economic Stabilization Act of 2008 on October 3, 2008. The Department of the Treasury was empowered to manage the TARP through a new agency called the Office of Financial Stability. Neel Kashkari heads the OFS. Initially, $250 billion was set as the spending limit for TARP. That amount could be increased to $350 billion upon the President=s certification to Congress that an increase was necessary. That request was made by President Bush. By December 19, with the lending of funds to 2 of the Big 3 automakers, the $350 billion

[26] *Id.*, quoting Paul Koches, general counsel for Ocwen, the largest subprime mortgage servicing company.

[27] *Id.*

[28] *Nobelman v. American Savings Bank,* 508 U.S. 324, 332 (1993)(concurrence by Justice Stevens).

[29] When the present Bankruptcy Code was enacted, "almost all home loans were conventional, 30-year mortgages with fixed interest rates. Prices were stable and didn't widely rise or fall in value. Constant refinancing was also rare. At the time, the banking industry demanded some financial protection as Congress sought to encourage banks to make loans so that thousands could gain 'the American dream' and own their own homes." Michael Zielenziger, *Please, Judge, Save My House*, AARP BULLETIN, January-February 2009.

limit was reached. Treasury Secretary Paulson was weighing whether to ask Congress for the remaining $350 billion before the close of the year.[30] As of the writing of this paper, it appears that President Bush will request the funds and leave to President Obama how to spend them.

The TARP was established to operate as a revolving purchase facility. It would purchase toxic or troubled assets from banks and other financial institutions and purchase whole loans and make direct equity investments in banks themselves. As of December 19, 2008, none of the money had been used to buy troubled assets. $290 billion had been used for equity infusions into various banks. Forty billion had been used to infuse equity into AIG. The remainder was used for the "bailout" of General Motors and Chrysler.

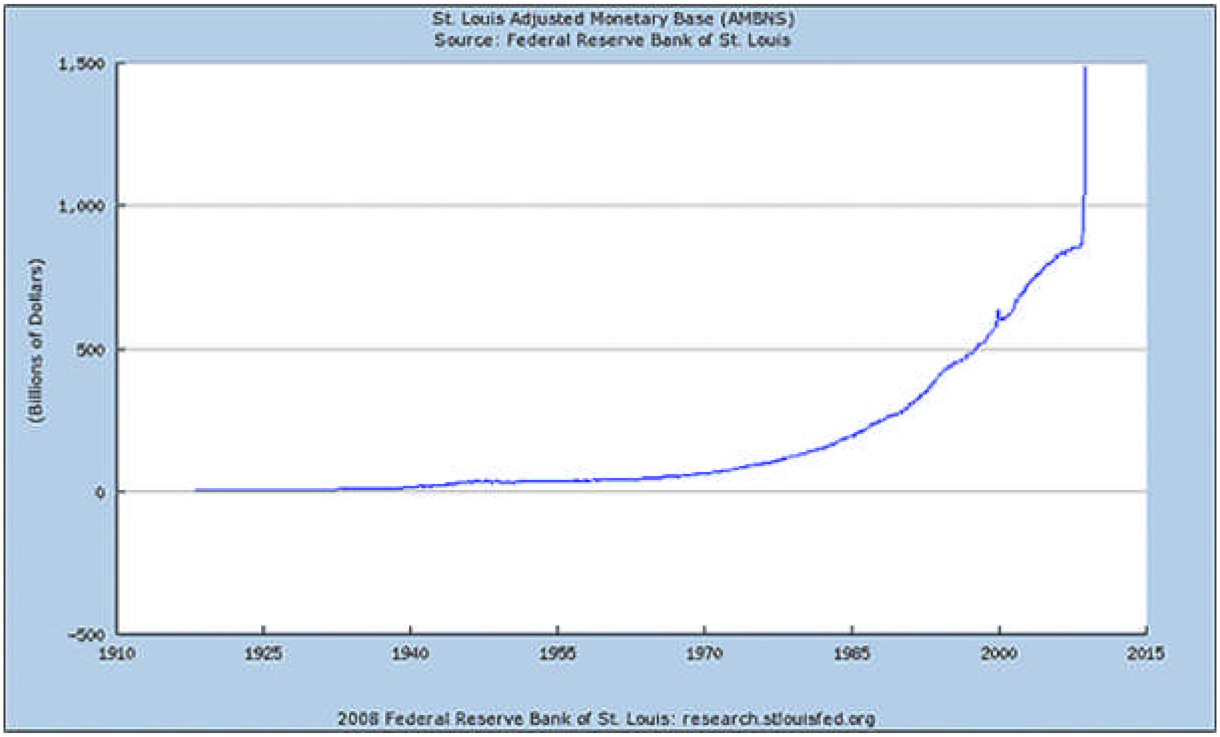
The 21 banks that received at least $1 billion each of the $290 billion infusion have refused to disclose anything about the status of the money and whether it was used for mortgage related activities. They were asked 4 questions. (1) How much of the money have you spent? (2) What did you spend the money on? (3) How much of the money is being held in savings? (4) What is the plan for the rest of the money? No bank answered any of the questions.[31]

The TARP, by infusing equity in banks, was supposed to improve the banks= balance sheets and liquidity. This infusion was also coupled with several other programs to help the markets. These programs include "$350 billion in FDIC guarantees on bank-issued debt, $1.3 trillion from the Fed to buy frozen commercial paper, $540 billion to buy commercial paper and other short-term debt form money market funds to stop the run on them, $200 billion Term Asset-Backed Securities Loan Facility (TALF) to back credit card, auto, student aid and small business loans, and $600 billion to buy mortgage-backed securities and GSE debt."[32] This has rapidly expanded the amount of money (all paper dollars and coinage) in existence. The amount of money in existence has gone from $800 billion to $1.5 trillion from October 2008-December 2008.

[30] Caren Bohan, and Richard Cowan, *Paulson Said Weighing Bailout's Next $350 Billion*, REUTERS, December 3, 2008.

[31] Cary Clack, *Banks Won=t Say Where Money Went*, SAN ANTONIO EXPRESS-NEWS, January 6, 2009. The banks answers ranged from "We've lent some of it. We've not lent some of it. We're not giving an accounting of 'here=s how we=re doing it.' We have not disclosed that to the public." JP Morgan Chase, recipient of $25 billion in funds. "We=re not providing dollar-in, dollar-out tracking." SunTrust Banks Inc., recipient of $3.5 billion in funds.

[32] Gary Shilling, *Semi-Annual U.S. Economic Outlook: Collapsing On Schedule*, *available at* http://www.investorinsight.com/blogs/john_mauldins_outside_the _box/archive/2008/12/15/seim-annual -u-s-economic-outlook-collapsing-on-schedule.aspx, (December 15, 2008).



The government is using the Federal Housing Administration as a source of loans since many of the banks have not used their cash infusions to issue new loans. In fact, the government has authorized the FHA to offer an additional $300 billion in loan guarantees to borrowers who qualify. As part of the ability to qualify for such a guaranteed loan (which offers a lower interest rate), a borrower must use an FHA authorized lender. A lender is authorized by a unit of the FHA. Two of the five authorized slots on the board are vacant. The board, even in light of its understaffing, has doubled the number of approved lenders since 2007. According to several sources, some of the approved lenders are the same parties that were involved in the creation of the bad paper already in existence.[33] "Within the next 12 to 18 months, there is going to be FHA-insurance Armageddon," stated Gary Lacefield, a former federal mortgage investigator-turned-consultant.[34]

B. Hope for Homeowners Program

Congress also approved a program called "Hope for Homeowners" (H4H) in the Economic and Housing Recovery Act of 2008 on July 30, 2008. The program began operation on October 1, 2008 and will end September 30, 2011. The program will "refinance mortgages for borrowers who are having difficulty making their payments, but can afford a new loan

[33] Froma Harrop, *The Mortgage Thieves Return*, CREATORS SYNDICATE, INC., *available at* http://www.creators.com/opinion/froma-harrop/the-mortgage-thieves-return.html (January 11, 2009).

[34] *Id.*

insured by HUD's Federal Housing Administration."[35] H4H offers 30-year fixed rate mortgages to borrowers for their primary residences.

The initial requirements for borrowers who wished to utilize the program were:

1. The home being refinanced was their primary residence, and they had no second mortgages.

2. Their existing mortgage was originated on or before January 1, 2008, and the borrowers have made at least six payments.

3. They were not able to pay their existing mortgage without help.

4. As of March 2008, their total monthly mortgage payment was more than 31 percent of their gross monthly income.

5. They certified they have not been convicted of fraud in the past 10 years, intentionally defaulted on debts, and did not knowingly or willingly provide materially false information to obtain their existing mortgage(s).[36]

The maximum loan for which a mortgagor could receive H4H relief was $550,440. The new mortgage could not be in an amount that was more than 90% of any new appraised value including any financed "Upfront Mortgage Insurance Premium." The mortgage premium was set at 3% and the annual mortgage insurance premium was 1.5% of the mortgage balance. The holders of existing mortgage liens that were being taken out had to waive all prepayment penalties and late payment fees. The existing lender, being taken out in the refinance, had to accept the H4H loan proceeds in full satisfaction of its (their) debt. The borrower had to share with the FHA any equity created at the beginning of the mortgage and any future appreciation in the value of the home. A borrower could not take out a second mortgage for the first five years of the loan except under certain conditions for emergency repairs.[37]

On November 19, 2008, the President issued another press release announcing new flexibility in the H4H loan program. The modifications increased the loan to value ratio from 90% to 96.5% for some loans. It simplified the process to remove subordinate liens by permitting upfront payments to lienholders and it allowed lenders to extend mortgage terms from 30 to 40 years.[38] The 96.5% loan to value ratio will be allowed for borrowers whose mortgage payments represent no more that 31% of their monthly gross income and household debt is no

[35] Press Release, President G.W. Bush, Hope for Homeowners, October 1, 2008, *at* www.hud.gov/news/release.cfm?content=pr08-150.cfm.

[36] *Id.*

[37] *Id.*

[38] Press Release, President G.W. Bush, Hope for Homeowners plan (November 19, 2008), http://www.hud.gov/news/release.cfm?content=pr08-178.cfm.

more than 43%. The prior limits were 90% loan to value with a debt-to-income rations of 38-50%.

After all of the carefully laid out program guidelines, as of December 18, 2008, very few loans have been issued under the program. As of November 17, 2008, less than 115 applications had been received.

C. HOPE NOW

HOPE NOW Alliance is a collaboration of "credit and homeowners' counselors, mortgage servicers, and mortgage market participants . . . formed with the encouragement of the Department of the Treasury and the Department of Housing and Urban Development."[39] It was formed on October 10, 2007, a year before the government "Hope for Homeowners" program. Its purpose is to

> Explore a variety of methods to reach out to at-risk homeowners, including a direct-mail campaign to encourage at-risk borrowers to call their mortgage servicer or a credit counselor.
>
> Work to improve communications between servicers and non-profit counselors to speed outreach and to develop and explain options for at-risk borrowers.
>
> Develop standards with investors to enable counseling sessions for homeowners to be funded by servicing contracts.[40]

HOPE NOW has as members 34 loan servicers, lenders and mortgage market participants. They include

Acquira Loan Services
American Home Mortgage Servicing, Inc.
Assurant, Inc.
Aurora Loan Service
Bank of America
Carrington Mortgage Services
Chase
Citigroup, Inc.
Countrywide Financial Corporation
EMC Mortgage Corporation
Fannie Mae
First Horizon Home Loans and First Tennessee Home Loans
Freddie Mac
GMAC ResCap

[39] HOPE NOW Alliance Created to Help Distressed Homeowners, *available at* http://www.hopenow.com/media/press_release.php (October 10, 2007) .

[40] *Id.*

Home Loan Services, Inc. (d/b/a First Franklin Loan Services & NationPoint Loan Services)
HomEq Servicing
HSBC Finance
Indymac Bank
LandAmerica Financial Group, Inc./LoanCare Servicing Center
Litton Loan Servicing
MERS
National City Mortgage Corporation
Nationstar Mortgage, LLC
Ocwen Loan Servicing, LLC
PMI Mortgage Insurance Co.
Radian Guaranty Inc.
Saxon Mortgage Services
Select Portfolio Servicing, Inc.
State Farm Insurance Companies
SunTrust Mortgage, Inc.
Taylor, Bean & Whitaker
Washington Mutual, Inc.
Wells Fargo & Company
Wilshire Credit Corporation

The American Bankers Association, the Mortgage Bankers Association, the American Securitization Forum, the Consumer Bankers Association and other influential groups are also part of the alliance.

HOPE NOW established a suggested streamlined loan modification program. The program is consistent with the American Securitization Forum=s plan for loans held in securitization trusts. These guidelines include

Contact with borrowers who are 90 days or greater past due. “Member Servicers should consider pausing the foreclosure process, when appropriate, for up to 30 days (or longer if necessary) tp pursue a loss mitigation option.”[41]

Utilize loss mitigation options that may include

1. Forbearance - a temporary agreement allowing borrowers to make partial or not payments for some period of time. This would usually be used Abecause of a temporary and finite hardship.@[42]

[41] HOPE NOW Mortgage Servicing Guidelines, *available at* http://www.hopenow.com/members/members.php at Servicing Guidelines (June 9, 2008).

[42] *Id.*

2. Repayment Plan - an agreement in which the borrower resumes making regular payments plus an additional amount to bring the loan current. This plan would be used in many chapter 13 bankruptcy cases.

3. Modification - an agreement to change the borrowers monthly payments temporarily or permanently by (a) reducing the interest rate; (b) on ARM loans, fixing the interest rate; (c) extending the term of the loan; (d) deferring past due amounts (e) capitalizing past due amounts (f) deferring principal and creating a balloon payment at certain date (g) conditionally forgiving a portion of the debt or (h) forgiving a portion of the debt.[43]

The HOPE NOW Alliance has modified approximately 950,000 loans in 2008. "The group estimates that about 2.2 million foreclosures will have been prevented this year, bringing to 3 million the total averted since the program began in 2007."[44] However, about 55% of the loans that have been modified are now 30 or more days delinquent. "Re-default rates increased each month and showed no signs of leveling off after six months and even eight months."[45]

Attached are web pages of Chase Mortgage and SunTrust Mortgage with whom bankruptcy debtors may have mortgages. These pages are representative of the pages of most other lenders. The pages list possible help or solutions for defaults.

D. President Obama=s Plan

Barack Obama's economic agenda includes several mortgage related parts. First, he intends to combat mortgage fraud by creating new criminal penalties for mortgage fraud, requiring the reporting of suspicious activity and providing counseling for homeowners and tenants facing evictions and foreclosures. Second, President Obama will require more explicit disclosures to borrowers at closing. Third, he intends to create a fund to assist homeowners who cannot afford their homes. The fund would help with the cost of selling the homes. Fourth, Obama will work to eliminate the prohibition of cramdown of primary residence mortgage debt. Fifth, President Obama's agenda includes enactment of a "universal mortgage credit" that will allow non-itemizing taxpayers to take a 10% credit for mortgage interest. He estimates this credit will provide each nonitemizing taxpayer or married couple a credit worth about $500 per year.[46]

[43] *Id.*

[44] Alison Vekshin, *More Than Half of Modified Mortgages Fail Again, Regulators Say*, BLOOMBERG NEWS, *available at* http://www.bloomberg.com/apps/news?pid+20670001&refer=&sid=aoXUY1YDL.6c (December 22, 2008)..

[45] *Id.*

[46] Barack Obama, *Barack Obama's Economic Agenda*, *available at* http://BarackObama.com (last viewed on December 21, 2008).

E. Helping Families Save Their Homes in Bankruptcy Act

Senator Richard Durbin of Illinois introduced a bill entitled “Helping Families Save Their Homes in Bankruptcy Act of 2008” on October 3, 2007. To date, the bill is still in the Senate subcommittee. The bill was reintroduced on January 6, 2009, the first day of the 111th Congress by Senator Durbin in the Senate and Representative John Conyers in the House of Representatives.

The bill only applies to principal residence home loans in existence before the enactment of the law. The debtor must certify that he/she has received notice that the mortgagee may commence a foreclosure. It provides for cramdown of primary residence mortgages in chapter 13 and the extension of the loan to 30 years minus the number of years the loan has already been in existence. The bill provides for recapture by the lender of any profit on sale of the home to the extent of the original principal amount of the loan. The bill also exempts a debtor from credit counseling if a foreclosure sale is scheduled at the time of filing of bankruptcy. The bill also provides that no fees, costs or other charges may be added to the loan during the bankruptcy case unless notice is given to the court of the fee or charge and the fees, costs or charges are lawful, reasonable, and provided for in the loan agreement.

As of January 9, 2009, Citigroup had agreed to support the proposal. It is unknown at the time of the writing of this article if other lenders will also support the proposal.

F. Mortgage Forgiveness Debt Relief Act of 2007

The Mortgage Forgiveness Debt Relief Act of 2007 which has been enacted excludes from gross income amounts attributable to a discharge, prior to January 1, 2010, of indebtedness incurred to acquire a principal residence. The excludable amount is limited to $2 million.

G. Barron=s Plan to End the Foreclosure Crisis

Barron=s weekly newspaper published an article in its December 8, 2008 issue that it entitled “How to Solve the Foreclosure Crisis.” Its solution has 4 points.

1. Offer to refinance every American homeowner=s mortgage at 4.5%, to reduce the chances of additional defaults.

2. Make similar low-rate mortgages available to home buyers, as the Treasury proposed this week.

3. Make full use of Fannie Mae and Freddie Mac. They should repackage all the new loans as safe securities for investors.

4. Modify the $500 billion of subprime and Alt-A loans in arrears. Extend maturities to 40 years, and in some cases, pay down principal.[47]

H. Loan-Modification Consultants

Loan-modification firms have sprung up as the mortgage crisis has deepened. The firms use their expertise in the housing and mortgage industries to either negotiate refinancing through the Hope for Homeowners program, or through HOPE NOW, or individually, negotiate with lenders. Many of these firms charge nonrefundable upfront fees of $3,000-5,000.[48]

I. Debtor=s Counsel Loss Mitigation Web Portal

This website was established in conjunction with the "Mortgage Issues Liaison Committee" of the National Association of Chapter Thirteen Trustees. The site is designed to allow debtor's counsel to submit a request for a loan modification, whether their client is in bankruptcy or not. The portal web site is www.dclmwp.com. The service is free and the loan servicers promise rapid responses to requests for modifications. Over 35 loan servicers are working with the Portal. Hundreds of debtors= counsel have signed up to utilize the service in late 2008. The attorney inputs the servicer name and loan information. The site also asks for status of the bankruptcy and the debtor=s financial information which the site allows you to download from the debtor=s bankruptcy file. The site then asks what the debtor wishes to do with the residence. The loan servicers are to respond to the modification request within 7 days.

J. Case Law

The mortgage crisis has caused litigation in the courts raising issues about loans and their servicers.

The bankruptcy courts have had cases dealing with the standing of servicers to file motions for relief from stay, the propriety of fees charged by lenders, the failure of lenders to disclose fees added to accounts during bankruptcy cases, the failure of lenders to provide proper documentation of loan payments, and the filing of false affidavits. As stated in the New York Times, December 28, 2008, "A Mortgage Paper Trail Often Leads to Nowhere,"

> Problems often emerge because these notes–which are written promises to repay the full amount of a mortgage–weren't recorded properly when they were bundled by Wall Street into pools or were subsequently transferred to other holders. How can a loan be modified. . . if the lender cannot prove that it actually owns the note? More and more judges are asking the same thing about

[47] Jonathan R. Laing, *How to Solve the Foreclosure Crisis*, BARRONS, *available at* http://online.barrons.com/article/SB122853114366984933.html?mod=ba_mp_view&page=sp, (December 8, 2008).

[48] Robert Bernier, "*Help" Can Be Costly*, BUSINESS WEEK, November 20, 2008.

> lenders trying to foreclose on borrowers. . . Most loan servicers–the folks responsible for handling all the paperwork surrounding monthly mortgage payments–aren't set up to handle all of the details involved in a modification.

In re Haque, 395 B.R. 799 (Bankr. S.D. Fla. 2008). Court sanctioned Wells Fargo Bank for filing about 45 false affidavits. The affidavits sought payment of "penalty interest," a charge for debtors early payoff of their mortgages. In these cases, Wells Fargo was seeking relief from the stay because the debtors were in default on their mortgages, not seeking to pay them off. Wells Fargo could not explain why the charge had been added to each statement of delinquencies. The judge assessed a sanction of $2,114.10 per affidavit or $95,130.45 for the violation.

Wells Fargo Bank v. Burrier (In re Burrier), 2008 WL 5422646 (Bankr. D. Colo. 2008). The Court set for hearing at a later date whether to sanction Wells Fargo for its failure to provide clear, complete records of debtors= loan payment histories. The burden of proving that a stipulation was not adhered to by the debtors was on Wells Fargo and it could not so prove. The stipulation required the debtors to prove that they had made loan payments that Wells Fargo alleged had not been made. The debtors could not produce cancelled checks showing payment because, per Wells Fargo=s own procedures, it electronically debited the payments from debtors' bank account. Such debiting does not result in a cancelled check. However, the debtors did produce bank statements showing the debits. Wells Fargo had no record of the payments.

The judge stated that the case illustrates three problems with the current loan servicing system.

> First, it reflects a significant and problematic imbalance between a creditor, the mortgage holder, and debtors, homeowners who are timely making their mortgage payments, and who are not knowledgeable about banking procedures and check processing. . . Second, this case illustrates a major lender mortgage company whose operations and collections practices are seemingly disconnected from its own technologies. . . Third, this dispute might portend a widespread abuse of collection practices or creditor overreaching–demanding of debtors what it, the creditor itself, is unable to provide: accurate and reliable record keeping and billing practices.

2008 WL 5422646 at * 1.

Reusser v. Wachovia Bank, N.A., 525 F.3d 855 (9th Cir. 2008). The Court held that it could not address debtors claim that Wachovia Bank had foreclosed and evicted them from their home wrongfully because Wachovia Bank was not a movant in the relief from stay proceeding in bankruptcy court that allowed foreclosure. The issue was not raised when the relief from stay motion was brought nor during the foreclosure process; therefore, it was an untimely defense. The Court did state that "[t]he Supreme Court recently noted that '[b]ankruptcy jurisdiction, at its core, is *in rem*,' such that it >is premised on the debtor and his estate, and not on the creditors." *Cent. Va. Cmty. Coll. V. Katz*, 546 U.S. 365, 362, 269-70 . . .(2006) . . .Thus, a final order lifting an automatic stay is binding as to the property or interest in question–the *res*–and its scope is not limited to the particular parties before the court." 525 F.3d at 861.

In re Kang Jin Hwang, 396 B. R. 757 (Bankr. C.D. Cal. 2008). Bank could not bring motion for relief from stay when it was the holder of the note but it had assigned its rights under the note to another entity. The owner of the note must be joined as a party.

In re Conde-Dedonato, 391 B.R 247 (Bankr. E.D.N.Y. 2008). Servicer of mortgage is a creditor with standing to file a proof of claim. *Accord*, *In re Dye*, 2008 WL 2773549 (Bankr. N.D. Ga. 2008); *In re Woodberry*, 383 B.R. 373 (Bankr. D.S.C. 2008).

In re Vargas, 396 B.R. 511 (Bankr. C.D. Cal. 2008). MERS filed a motion for relief from stay as to a mortgage loan for which it was the mortgagee's agent. Its motion stated it moved for relief on its own behalf and for "its assignees and/or successors in interest." The court held that MERS could not seek relief on behalf of undisclosed parties and denied the motion.

Greer v. O=Dell, 305 F.3d 1297, 1302-03(11th Cir. 2002). A real estate loan servicer is a party in interest with respect to the enforcement of a loan.

In re Hayes, 393 B.R. 259 (Bankr. D. Mass 2008). The movant in a relief from stay proceeding was Deutsche Bank who filed the motion in its capacity as trustee of Argent Mortgage Securities, Inc. Previously, Argent Mortgage Company, LLC filed a proof of claim for the same debt in its capacity as loan servicer for Argent Mortgage Company LLC. At the hearing on the motion for relief from stay, Deutsche Bank did not prove that it was the real party in interest as to the loan. Courts have held that mortgage servicers are parties in interest. However Deutsche Bank could not trace the loan from Argent Mortgage Company, LLC, to it. *Accord*, *In re Jones*, 3008 WL 4539486 (Bankr. D. Mass. 2008); *In re Maisel*, 378 B.R. 19 (Bankr. D. Mass. 2007); *In re Parrish*, 326 B.R. 708 (Bankr. N. D. Ohio 2005).

Nosek v. Ameriquest Mortgage Co. (In re Nosek), 386 B.R. 374 (Bankr. D. Mass. 2008). Ameriquest as holder of a mortgage filed a proof of claim in Nosek=s case. It did this even though it had transferred the note prior to the representation that it was "holder" of it. The court sanctioned Ameriquest and the actual holder of the note $250,000 for the misrepresentations.

State courts and other federal courts have faced issues of standing as well.

In re Foreclosure Cases, 2007 WL 3232430 (N.D. Ohio 2007). The Court, prior to entering foreclosure orders, required each plaintiff-lender "to submit a copy of the Assignment of the Note and Mortgage, executed as of the date of the Foreclosure Complaint. In [these]. . . cases, none of the Assignments show the named Plaintiff to be the owner of the rights, title and interest under the Mortgage at issue as of the date of the Foreclosure Complaint." 2007 WL 3232430 at *2.