Submitted via email to Congressman Ellison's staffer at Karl.Haddeland@mail.house.gov and to fsctestimony@mail.house.gov on August 7, 2007.

August 7, 2007

U.S. House of Representatives
Committee on Financial Services
2129 Rayburn House Office Building
Washington, DC 20515

Dear Chairman Frank and Members of the Committee on Financial Services of the United States House of Representatives,

Thank you for the opportunity to provide a joint written statement to supplement the oral testimonies we provided at the August 9, 2007, hearing on "The Effect of Predatory Lending and the Foreclosure Crisis on Twin Cities' Communities and Neighborhoods." During oral testimony, Minneapolis Mayor R.T. Rybak described the growing foreclosure crisis as it affects his City and our region's coordinated response to this housing crisis – the Foreclosure Prevention Funders Council. Saint Paul Mayor Chris Coleman described his City's horrific experiences with foreclosure and the resultant vacant homes – describing it as a "disinvestment domino effect." Mayors Rybak and Coleman described possible Federal-level solutions.

Based on our collective experiences in each of our Twin Cities, this written statement builds on our oral testimony by setting out six potential Federal-level solutions as well as provides specific comments on the Federal bills that have already been introduced. If passed into law, the solutions set out below would dramatically affect the ability of our Cities and partners to respond to this foreclosure crisis at the local-level.

FEDERAL-LEVEL SOLUTIONS

1. Modify Regulations on the Issuance of Tax-Exempt Mortgage Revenue Bonds (Section 143 of the Internal Revenue Code of 1986)

Tax-exempt mortgage revenue bonds ("MRBs") are a tool that is continually used by both Minneapolis and Saint Paul. Specifically, MRBs are issued to fund the pool for our CityLiving Program. CityLiving offers financing for the purchase, purchase/rehabilitation and refinance/rehabilitation of homes, primarily by first time homebuyers, of one- to four- unit homes in the cities of Minneapolis and Saint Paul. In the current program, most borrowers are required to take pre-purchase home-buyer training, and in the future this will be a requirement for all borrowers. Income and purchase price limits apply as well. The default rate on CityLiving

loans is approximately two percent, a percentage well-below the national average which exceeds four percent.

However, due to the limitations of federal tax law, there are limits on the usefulness of the CityLiving Program. Three changes in the regulations relating to MRBs would dramatically increase the usability of this proven method to ensuring stable, long-term homeownership. The first useful change would be to permit the use of proceeds of MRBs to permit loans to be made to refinance homes owned by homeowners who are at risk of default or foreclosure, either because the loan product they originally used was inappropriate or because circumstances have changed. The second change would be to reduce the minimum rehabilitation requirement for "qualified rehabilitation loans" from 25% of the adjusted basis in the residence to $5,000, for loans made for refinancing and rehabilitation to non-first-time homebuyers. The third change would be to expand the definition of targeted areas to permit the broader use of MRBs to encourage the redevelopment of distressed areas of the Cities. Each of these changes is discussed in greater detail below.

Refinancing. Federal tax law currently allows proceeds of MRBs to be used to refinance existing loans only (i) when the homeowner has acquired the home with a contract for deed and has an income under 50% of the area median income, (ii) when the homeowner will be doing substantial rehabilitation, and (iii) in the context of a construction or bridge loan. The contract for deed requirement is an obsolete provision in Minnesota since contracts for deed are seldom used today to finance homes. In order to be able to use MRB proceeds to refinance existing unsustainable loans, Section 143 would need to be amended to permit refinancing of homes for homeowners with certain distressed loans.

Minimum Rehabilitation Requirement. Federal tax law currently permits proceeds of MRBs to be used to refinance and rehabilitate homes by non-first-time homebuyers if the rehabilitation meets certain requirements, including a requirement that the cost of rehabilitation exceed 25% of the borrower's adjusted basis in the residence. This formula for calculating minimum rehabilitation is cost prohibitive for most borrowers and frequently property values do not justify that level of rehabilitation. We recommend adjusting the minimum cost of rehabilitation for "qualified rehabilitation loans" to $5,000.

Targeted Areas. Federal tax law currently permits higher income limits for homebuyers, higher purchase prices and financing by non-first-time homebuyers in "targeted areas" defined in the law. In order to make MRBs a more effective tool to encourage redevelopment in specific areas of the Cities, the definition of targeted areas should either be broadened generally, or authority should be given to issuers of MRBs to define targeted areas within their specific jurisdictions in order to achieve local policy objectives.

2. Require Mortgage Industry to Restate/Modify Terms for Distressed Homeowners

Many distressed homeowners selected to use, or were deceived into using, an inappropriate mortgage product. Once the homeowner sees distress on their financial horizon, we encourage them to contact the servicer of their mortgage and non-profit home ownership counselors. When distressed homeowners contact these entities, private solutions are available in many instances. For example, the Minnesota Homeownership Center and Minnesota's statewide network of Mortgage Foreclosure Prevention Providers have been able to assist nearly fifty percent of the homeowners across the State of Minnesota who contact their service providers.

Modifying the terms of an existing loan involves a nominal cost compared with hefty costs and fees for a refinancing, which can add more than five percent to the mortgage amount. If Federal legislation could require the mortgage industry to restate/modify certain homeowners' loan terms prior to offering a refinancing, distressed homeowners could save a great deal of money on unnecessary refinancing fees. Moreover, due to the leveling off of home appreciation, many homeowners are not able to refinance because they do not have any equity in their homes. For these reasons, requiring the mortgage industry to restate/modify loan terms for distressed homeowners as a mandatory first step is a solution to part of the current foreclosure crisis.

3. Provide Community Reinvestment Act Credit to Mortgage Industry When Allow Renters to Continue to Reside in Homes

Currently, under Minnesota law, renters living in foreclosed homes are evicted at the end of the redemption period. This is typically about a year after the foreclosure process begins. After the renter is evicted, the homes often sit vacant. These vacant structures provide an avenue for vandalism, theft, arson, and other community-damaging crimes. For those properties purchased by the lender at the sheriff's public auction, as is the overwhelmingly situation in Minnesota, we would like to partner with the Federal government to amend the necessary laws and regulations in order to be able to encourage those in the mortgage industry by offering Community Reinvestment Act credit to act as "landlords" until the property is sold to a new owner-occupant. If this change is not plausible, an alternative approach could be to provide those in the mortgage industry with Community Reinvestment Act credit for their costs incurred while properly maintaining a home during the period following the sheriff's public auction.

This would benefit the city, community, and lender. When properties are occupied and maintained, city staff is less likely to be called to attend to the various crimes associated with vacant properties. Not only does this lessen the load now placed on city police, fire, and rescue squads, cities can free up additional funds that would otherwise be used to inspect and often demolish the vacant and boarded structures. Communities benefit in that occupied and maintained homes are better than vacant and boarded homes in many ways including, safeguarding the general structure and neighborhood, maintaining property values, and policing and safety. Although lending institutions would be required to function as landlords, and there would be some costs associated with this, overall, the lending institutions benefit in that the home is likely to be more saleable if it (and the other otherwise vacant homes surrounding the property) has been occupied on an on-going basis. Furthermore, by continuing to have an occupant in the structure the lending institution dramatically decreases the likelihood that city regulations would require the demolition, and ultimate loss of any value left in the structure.

For these reasons, if the Federal government could amend its current regulations to provide Community Reinvestment Act credit to those in the mortgage industry that would be willing to act as landlords when the home would otherwise sit vacant, this would benefit the Cities, the community neighborhoods, and the lender who reacquired the property after the foreclosure sale.

4. Review Tax Consequences for Borrowers who Use Liquidation Options

For many distressed homeowners stuck in inappropriate products, liquidation is the best option. Two options include, for example, a pre-foreclosure short sale and a deed in lieu of foreclosure. In a pre-foreclosure short sale, the lender accepts less than the amount of the mortgage in satisfaction of the outstanding debt. Where a deed in lieu of foreclosure is used, the lender accepts a deed to the home as satisfaction of the outstanding debt.

Although these are solid options for many, current Federal tax law requires these distressed homeowners claim the income generated when using liquidation options. This requirement can function as a disincentive to already financially-stressed homeowners. In order to encourage increased use of these extremely helpful liquidation options, the tax consequences should be eliminated altogether or capped at a set amount. Similarly, homeowners who refinance to take equity out of the home, and later go into foreclosure after the home has depreciated in value, may also face other tax consequences. These tax consequences should also be addressed.

5. Continue to Invest Community Development Block Grants

Community Development Block Grant ("CDBG") funds are very flexible and allow us to invest in both residential and small commercial projects. When the marketplace doesn't value reinvestment into certain neighborhoods, we can use this money to provide low-interest loans with favorable repayment rates or partial subsidies to leverage more private investment. CDBG allows us to make the private marketplace work again for neighborhoods suffering from home foreclosure.

In Saint Paul, the federal commitment to this program in 1975 was over $18.8 million. Today, when we have an arguably more challenging environment for redevelopment in our city, our Federal partners commit $8.2 million in CDBG funds to our work together in the City of Saint Paul. Minneapolis's CDBG entitlement has declined from a high point of $19.9 million in 1980 to $13.8 million in 2006 and 2007.

Cities need a continued stream of these flexible funds in order to properly and adequately address their growing foreclosure crisis.

6. Require Ongoing Registration when Interests are Conveyed

With our increasingly digital age, the mortgage industry has adapted it practices to ease securitization and conveyances of interests in the mortgage. In Minnesota, as in many other states, mortgage documents are recorded with the County Recorder. However, when the homeowner begins to experience distress or enters the foreclosure process, the entity provided on the mortgage documents is seldom the entity that the homeowner should be contacting to discuss retention or liquidation options. Home ownership counselors face a similar challenge when trying to provide assistance to distressed homeowners. A front page *New York Times* story from August 6, 2007, titled "Mortgage Maze May Increase Foreclosures" by Gretchen Morgenson, explains the phenomenon in more detail.

This "lost contact" phenomenon is exacerbated by the mortgage industry's use of the Mortgage Electronic Registry System (MERS) which "simplifies the way mortgage ownership and servicing rights are originated, sold and tracked" in that "MERS eliminates the need to prepare and record assignments when trading residential and commercial mortgage loans." Essentially, MERS acts as a shield to uncovering the necessary contact information for the true holder of the

mortgage in that MERS is often listed on the recorded mortgage documents and foreclosure notices. According to a recent list of recent foreclosures in the cities of Minneapolis and Saint Paul, MERS was listed as the mortgagee on 40-60% of the properties.

The solution is simple: when interests are conveyed, this conveyance (and the affiliated contact information) should be recorded with the relevant County Recorder's Office. This solution is multi-faceted, at a minimum, local and State governments cannot successfully address this lost contact phenomenon because they do not have jurisdiction over many of the relevant mortgage industry entities. Local and State governments need the Federal government to pass legislation that dovetails with local requirements.

Not only will this solution aid the distressed homeowner, but local governments like Minneapolis and Saint Paul will be able to provide better customer service to those seeking to purchase vacant properties as well as be better partners with community development corporations (for example, Habitat for Humanity, Dayton's Bluff Neighborhood Housing Services, the Greater Metropolitan Housing Corporation, and others) who seek to purchase, rehabilitate, and resell foreclosed properties to homeowners with stable, fixed-rate long-term mortgage products.

COMMENTS ON THE FEDERAL BILLS

City staff persons and their partners that work in our housing and legislative departments reviewed the language of the proposed bills listed below. City staff and their partners' comments and concerns are provided below. City staff and their partners continue to review other proposed legislation.

1. HR 1852 - Expanding American Homeownership Act of 2007 (Waters)

A. City staff were troubled that this bill appears to be targeted to first time home buyers only. If this is the case, then it would appear to limit a localities ability to provide homeownership preservation tools and products in the same way as the existing MRB regulations.

B. City staff commented that parts (7)(A)(i) and (ii) of Section 9, Payment Incentives, could be beneficial to homeowners.

C. City staff were concerned that Section 10 appears to make counseling optional. Although opinions differ as to whether mandating counseling will always lead to more stable, long-term decision making by the potential homeowner, city staff and the counselors at the Minnesota Home Ownership Center service providers can bear witness to the direct correlation between pre-purchase counseling and stable homeownership. If mandating homeownership counseling is not favored, it makes sense to require counseling for higher-risk borrowers or borrowers who select to finance any portion of their home purchase through the use of a sub-prime product.

D. City staff suggest that Section 10(iii), Notice to the Mortgagor, should require that the "housing counseling entity" be a HUD certified counselor closest to the location of the home.

E. With regard to Section 258, Pilot Program, the City of Saint Paul already has a program akin to this.

F. Section 10 relating to Protections for Higher Risk Mortgages could be strengthened to require oral as well as written presentations of the required disclosures.

G. With regard to Section 10(bb)III(iii), which prohibits private rights of action for required disclosures, and Section 10(bb)(C)(vii), which prohibits private rights of action for not giving notice of foreclosure prevention counseling, both Sections relating to Protections for Higher Risk Mortgages, City staff recommend not prohibiting private rights of action on required disclosures or notices and counseling. Minnesota's recent predatory lending legislation has added private rights of action to enforce the terms of the legislation. The rationale for prohibiting rights of action in these parts of the legislation may be because they relate to "relatively minor" aspects of the legislation – they relate to notices and disclosures, rather than lending practices themselves. However, it should be carefully considered whether Congress wishes to preclude rights of individuals to follow up on even basic requirements like disclosures, when the ban on private rights of action was one of the commonly cited experiences that interfered with individuals' ability to enforce their rights. Disclosures and notices are one of the basic consumer protections to help consumer avoid hasty and ill-considered decisions, especially important for higher risk mortgages.

2. HR 2895 - National Affordable Housing Trust Fund (Frank)

A. City staff seeks clarification on the targets and requirements for home ownership.

B. With regard to Section 295(c)(2), Selection Process and Criteria for Assistance, City staff has the following concerns:

1) It appears that these funds are really to be spent in more affluent areas; for example, see (v) "... project ... located ... various incomes" and (xii) "number of families having incomes less than the poverty line is less than 20 percent". This may limit the usefulness for these funds for some of the areas most heavily damaged by the recent foreclosure crisis.

2) Saint Paul City staff persons were apprehensive about Part (vi) in that there are not necessarily significant economic opportunities in the neighborhoods that need these funds for home ownership. More generally, city staff expressed concern as to how "economic opportunities" would be defined.

3) City staff persons were concerned about how "extremely low vacancy rates" would be defined, as it is used in Part (viii). Staff also expressed concern in that often times vacancy rates are high due to dilapidated housing, irresponsible landlords, and other related factors.

4) With regard to Part (xi), city staff noted that the area for "job opportunities" and "community revitalization projects" may not necessarily be in the same location.

C. City staff noted a discrepancy in that Section 296 states that the funds cannot be used for counseling. However, Section 297 requires counseling for home buyers. As you know, most of the counseling entities are non-profits that require grants and legislative allocations in order to provide the necessary services to homeowners. With the recent surge in foreclosures, counseling entities have struggled to increase their capacities to meet the growing demand within their limited budgets. Funding these critical resources is vital to their required capacity-building efforts.

D. City staff was concerned with Section 297 in that requiring that housing meet all requirements for "not less than 50 years" appears to be a sound requirement; however staff was troubled by who would pay for needed improvements over that same time period as well as for the rent subsidy. Staff noted that in another location the bill defines "extremely old housing" as housing that is forty-five or more years old.

E. Section 296's language relating to money for first-time homebuyers disturbed city staff in that it would not appear to keep homeowners in their homes, nor does it appear to help those who have lost their homes due to sub-prime lending return to homeownership.

F. City staff urge Congress to reconsider the 65% area median income ("AMI") affordability standard used in the Affordable Housing Trust Fund as described in Section 297(a)(1)B. The use of a 65% standard precludes its use for units commonly targeted and limited, under the Low Income Housing Tax Credit ("LIHTC") program to households at 60% AMI. If the purpose in having a slightly higher income standard (65% AMI instead of 60% AMI) is to promote production of housing at a more moderate level of income, potentially to reinforce market-building in challenged neighborhoods, perhaps 80% AMI would be a more appropriate standard. Otherwise, the marginal difference in allowable income levels appears to be obviated by the LIHTC program requirements.

3. HR 3081 - Fairness for Homeowners Act of 2007 (Ellison)

A. City staff expressed concern with Ability to Pay, (D) Other Criteria. Staff would prefer increased guidance to clarify what "other criteria ... verified through reasonably reliable methods and documentation" would be necessary and prudent to require.

B. City staff would like there to be a requirement that mortgage applicants receive a copy of any appraisal paid for by the mortgage applicant.

C. City staff partners believe the "duty of agency" for mortgage brokers is one of the most important aspects of this bill. Although it is impossible to know what new "tricks" will be used in coming years, we do know from experience that there will always be predators willing to take advantage of the system and exploit consumers.

D. City staff partners suggest that the bill could also address accountability up the chain to the lenders and investors who create unsustainable and inappropriate loans and supply a market for their resale in the secondary market. Putting accountability back into the system could be accomplished in two meaningful ways.

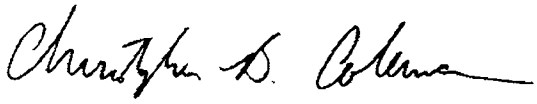
1) Anyone who makes or purchases a loan with certain characteristics could be held responsible for any violations contained in the loan itself or used in the process of making the loan. Stated differently, we need full assignee liability and we need to eliminate the holder in due course defense for mortgage loans.

2) We need to require that loan servicers or those conducting collections and foreclosure proceedings - the entity in contact with the borrower - has the authority to modify the terms of the loan.

Thank you for this opportunity and for your consideration of this vitally important crisis. This national foreclosure crisis is going to require coordination and partnership at all levels. We stand ready to do our part and ask for your federal leadership to end this devastating crisis.

Sincerely,

Mayor R.T. Rybak
City of Minneapolis



Mayor Christopher Coleman
City of Saint Paul

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