

Residential Foreclosure

A Wake Up Call for Real Estate Lawyers

Hennepin County Bar Association

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[Presentation Outline]

- Causes and Effects
- Current and New Laws
- Prevention and Remediation Efforts

Causes of Recent Surge

- Fraud
 - Falsified supporting documents
 - Fraudulent appraisals
- Increased use of sub-prime lending
 - Adjustable rate mortgages
 - Interest-only payment periods
 - Prepayment penalties
 - Stated-income (“no-doc”) loans
- Slowing & decreasing home appreciation
- Frequent refinancing
- Unsophisticated buyers
- Life
 - Medical emergency or illness
 - Change in status (i.e, divorce, death of partner)
 - Loss of Job
 - Financial mismanagement of personal resources

[Causes]

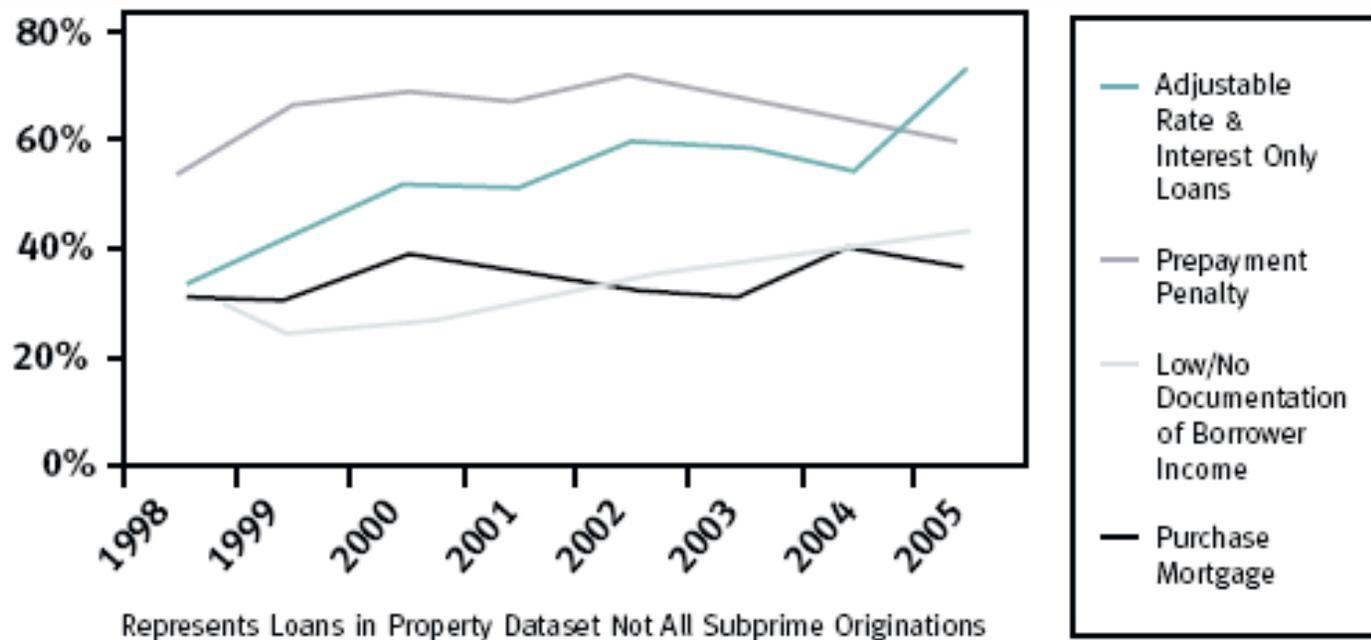
Percentage Increase in Foreclosure Risk for Specific Loan Features by Annual Loan Cohort (Positive numbers indicate higher risk, after controlling for borrower credit scores)

	1998	1999	2000	2001	2002	2003
ARM vs. Fixed-Rate Loan	123.3 ^{***}	86.0 ^{***}	72.0 ^{***}	61.8 ^{***}	77.9 ^{***}	117.1 ^{***}
Balloon vs. Fixed-Rate Amortizing Loan	75.7 ^{***}	51.8 ^{***}	36.0 ^{***}	21.7 ^{***}	14.1 [*]	85.9 ^{***}
Loan with Prepayment Penalty vs. Loan with No Prepayment Penalty	70.4 ^{***}	65.0 ^{***}	52.4 ^{***}	35.8 ^{***}	25.8 ^{***}	18.7 ^{***}
Loan with No or Low Documentation vs. Full-Doc Loan	5.6 ^{**}	19.0 ^{***}	29.0 ^{***}	25.8 ^{***}	44.7 ^{***}	63.7 ^{***}
Purchase Money Loan vs. Refinance Loan	19.3 ^{** *}	20.7 ^{***}	28.5 ^{***}	37.9 ^{***}	61.0 ^{***}	102.0 ^{***}

Confidence levels: * = 95%, ** = 99%, *** = 99.9%. Detailed results available upon request.

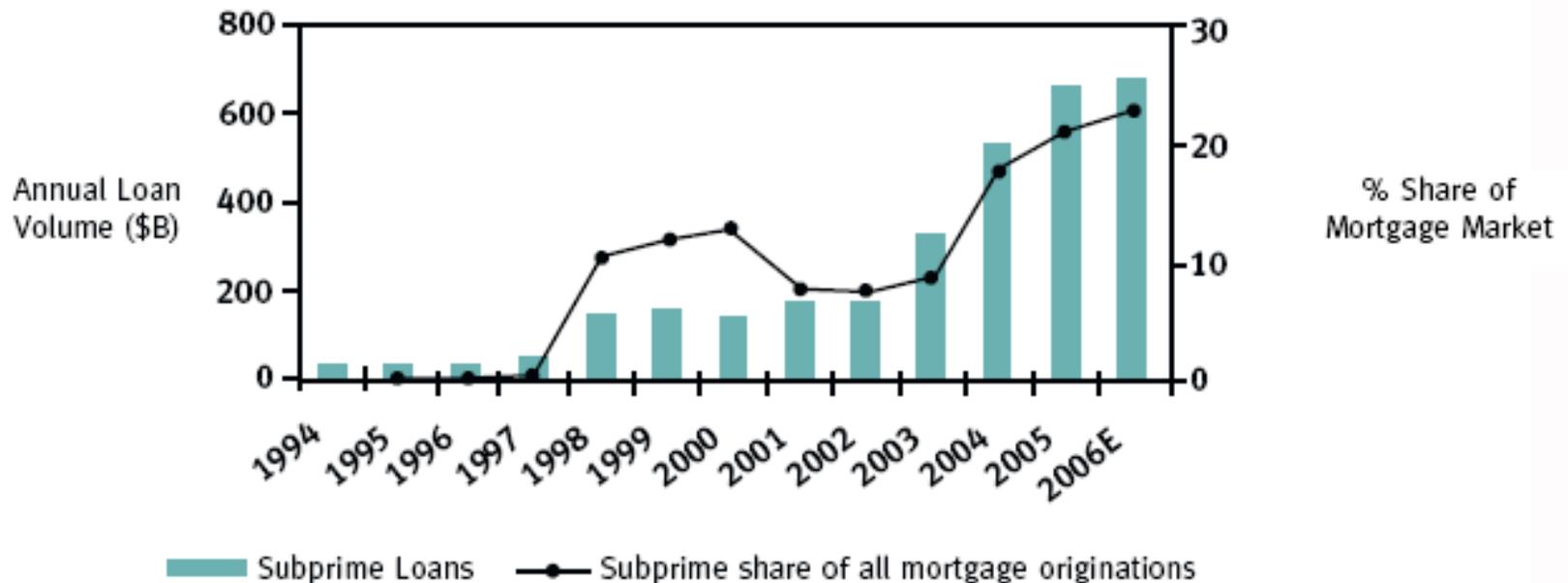
Causes – Increase in Sub-Prime

National Percent of Loans with Sub-Prime Features



Causes – Increase in Sub-Prime

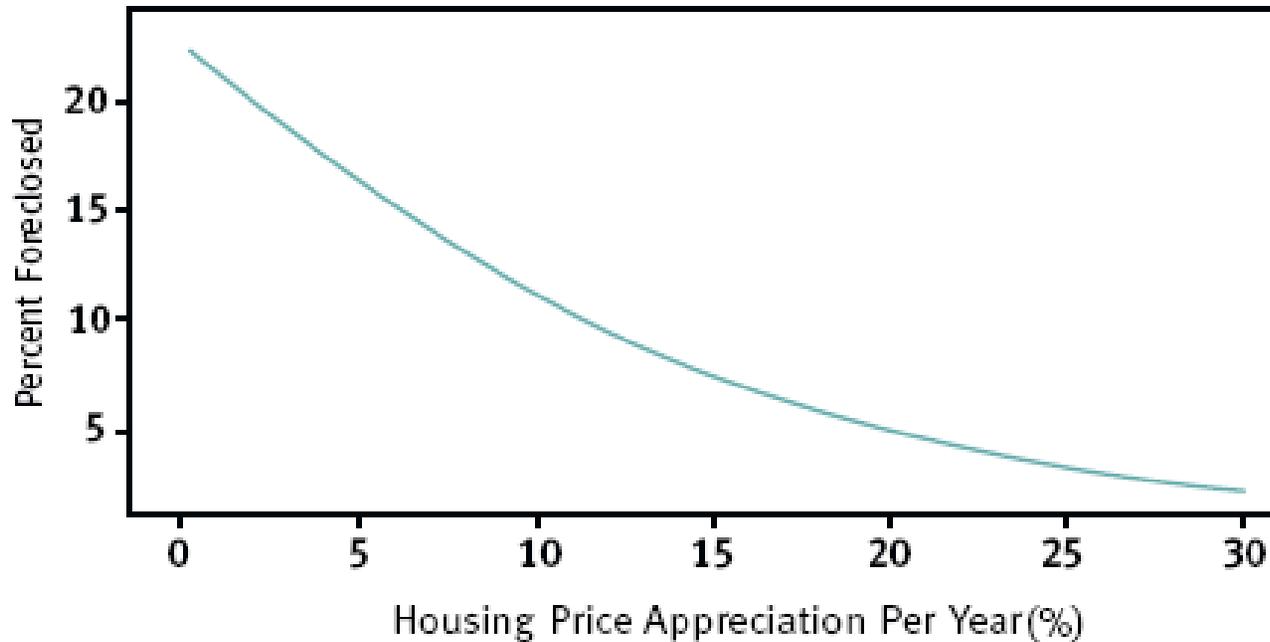
National Sub-Prime Mortgage Market Growth & Share of Total Mortgage Market



Source: Inside Mortgage Finance

Causes – Loss of Appreciation

Impact of Housing Price Appreciation
on Risk of Foreclosure



[Causes - Unsophisticated]

- A surprising 34% of homeowners have no idea what type of mortgage they have
- About 57% of homeowners said they had fixed-rate mortgages
- 9% knew they had some variety of an ARM
 - Of those who knew they had an ARM; 34% said they didn't know what they will do when the interest rate adjusts.

[Causes - Unsophisticated]

What do you plan to do when your ARM readjusts?		Do you worry about making next year's home payments?	
Refinance to a fixed rate	36%	Never	53%
Don't plan to have loan when it readjusts	24%	Rarely	17%
Move	4%	Regularly	15%
Get another ARM	2%	Sometimes	13%
Don't know	34%	Don't know	2%

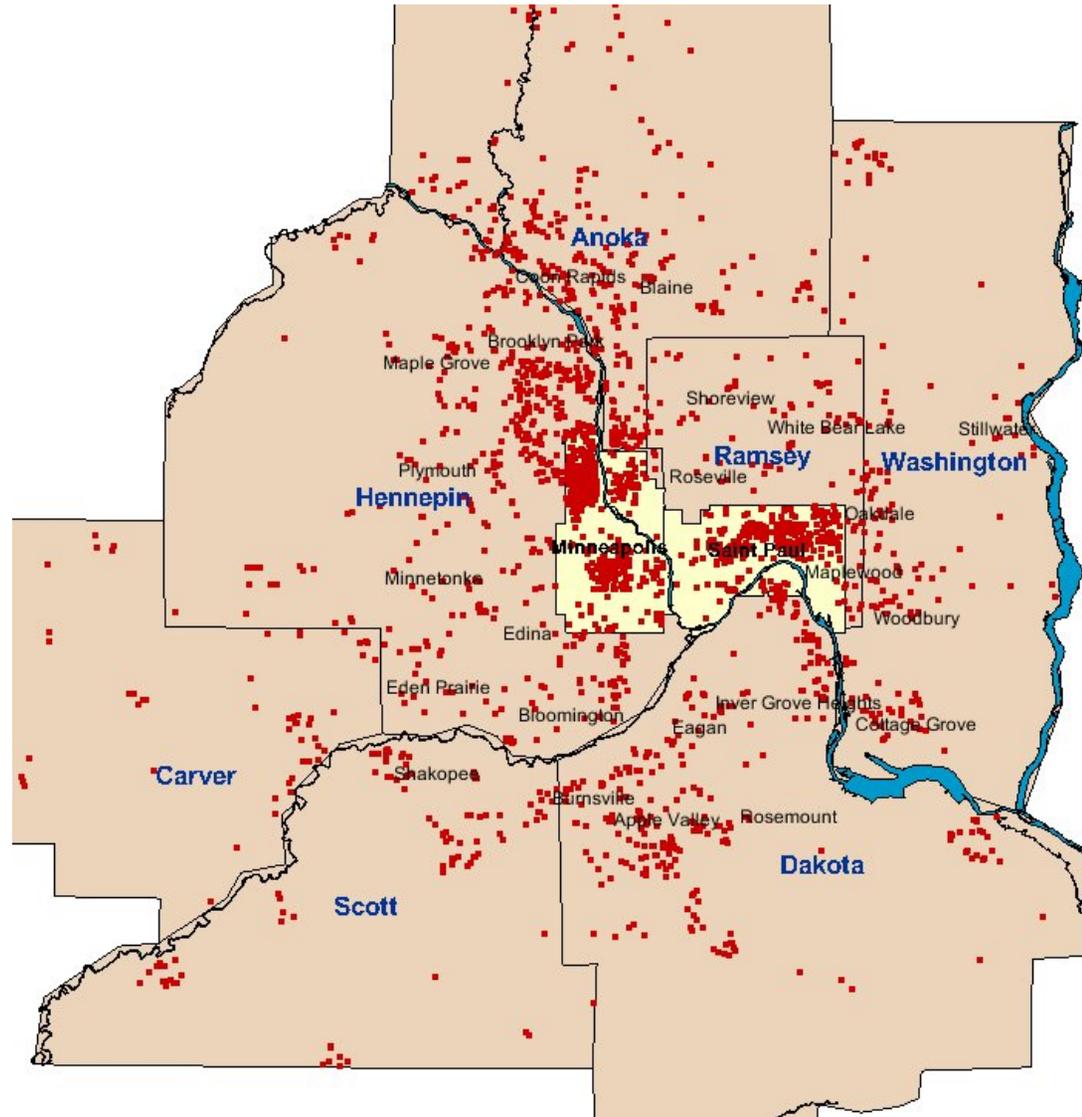
Foreclosure Not Just a TC Problem

MSA	Projected 2006 Foreclosure Rate	Rank (of 378 MSAs)
Duluth, MN-WI	16.2%	283
Fargo, ND-MN	17.9%	129
Grand Forks, ND-MN	17.5%	165
La Crosse, WI-MN	18.9%	75
Minneapolis-St. Paul-Bloomington, MN-WI	20.2%	40
Rochester, MN	18.3%	104
St. Cloud, MN	18.4%	97

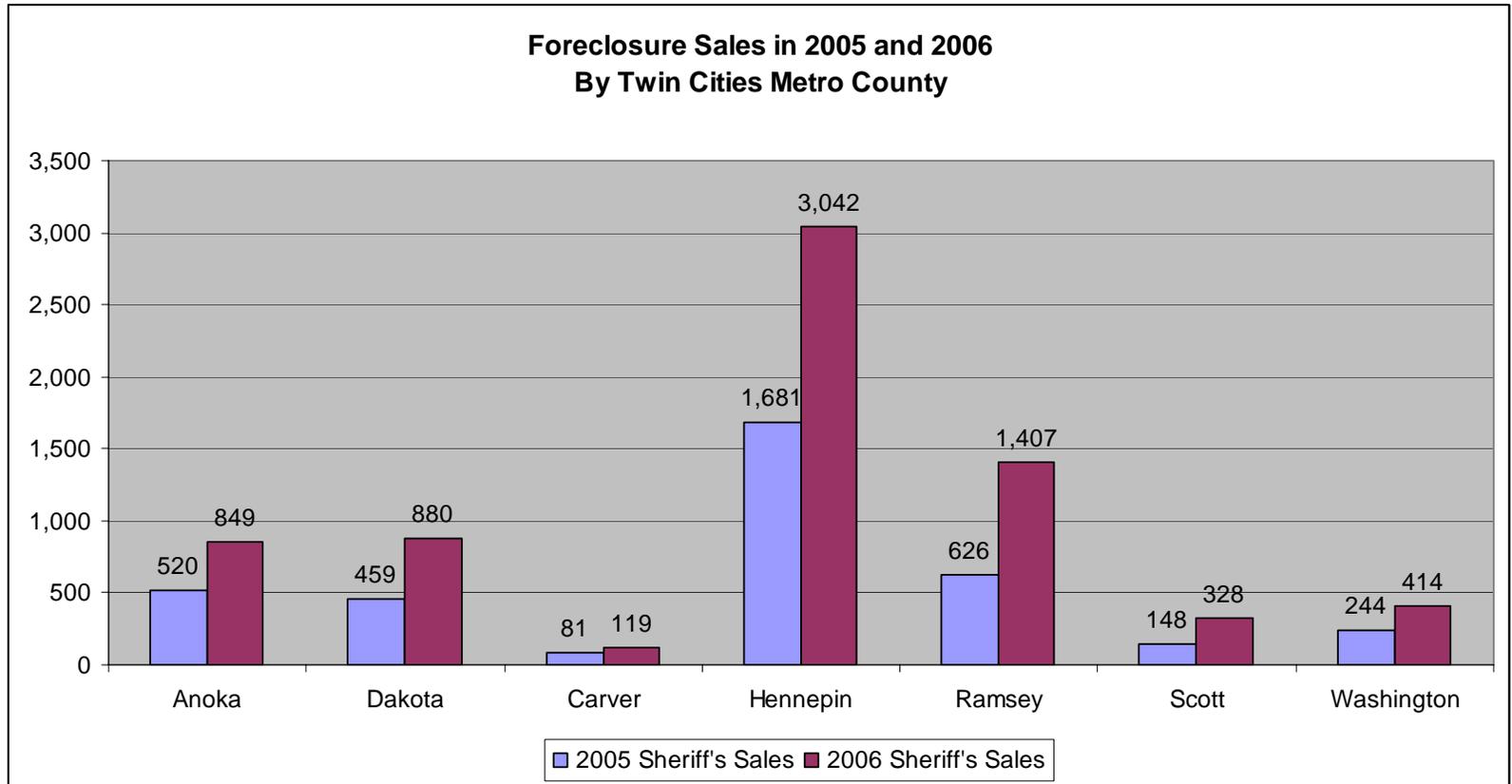
Source: Center for Responsible Lending

[Metro Foreclosures]

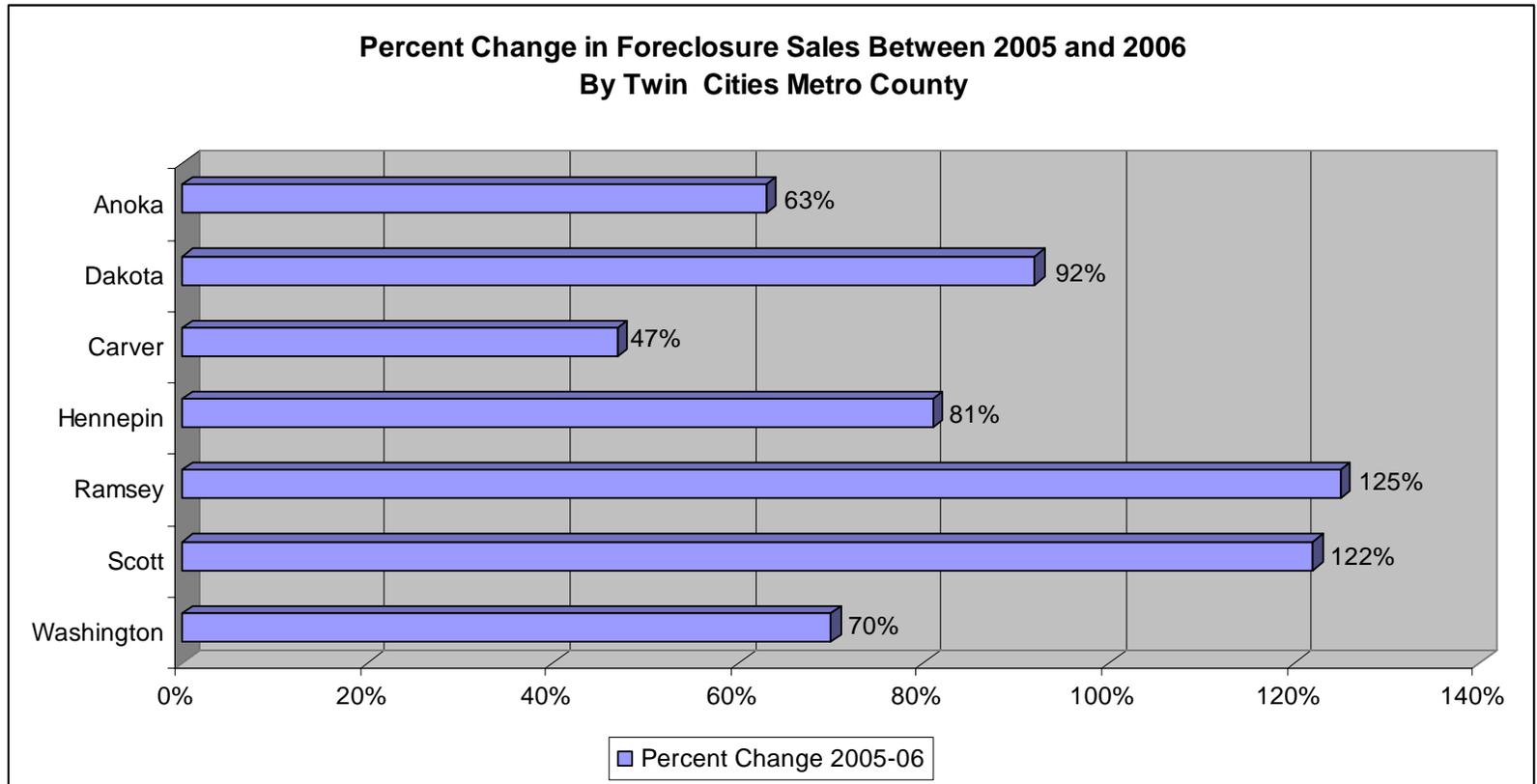
2,360 foreclosures
from Jan 2005
through Aug 2006



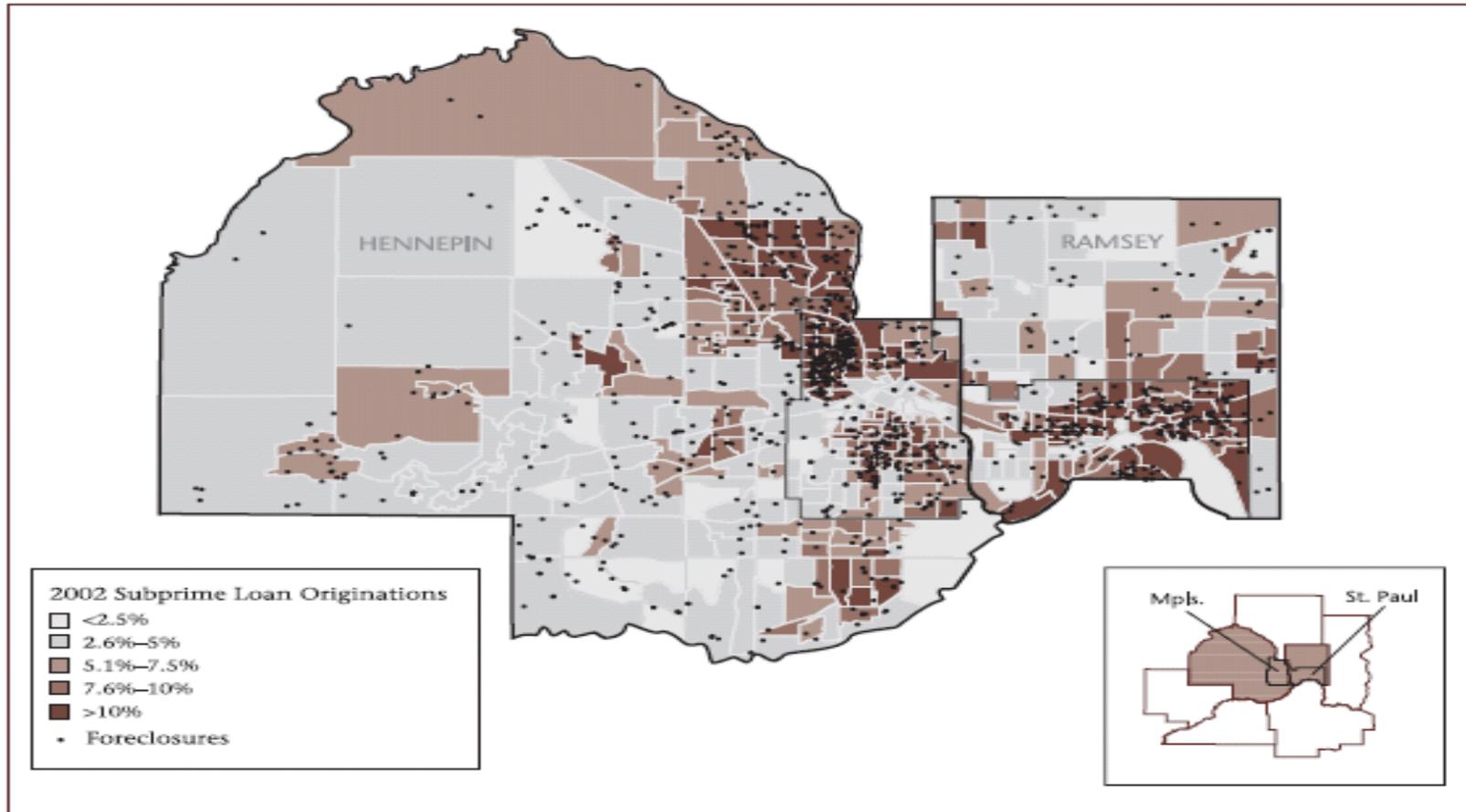
Increase in Metro Sheriff Sales



Increase in Metro Sheriff Sales



Concentration of Sub-prime Loans

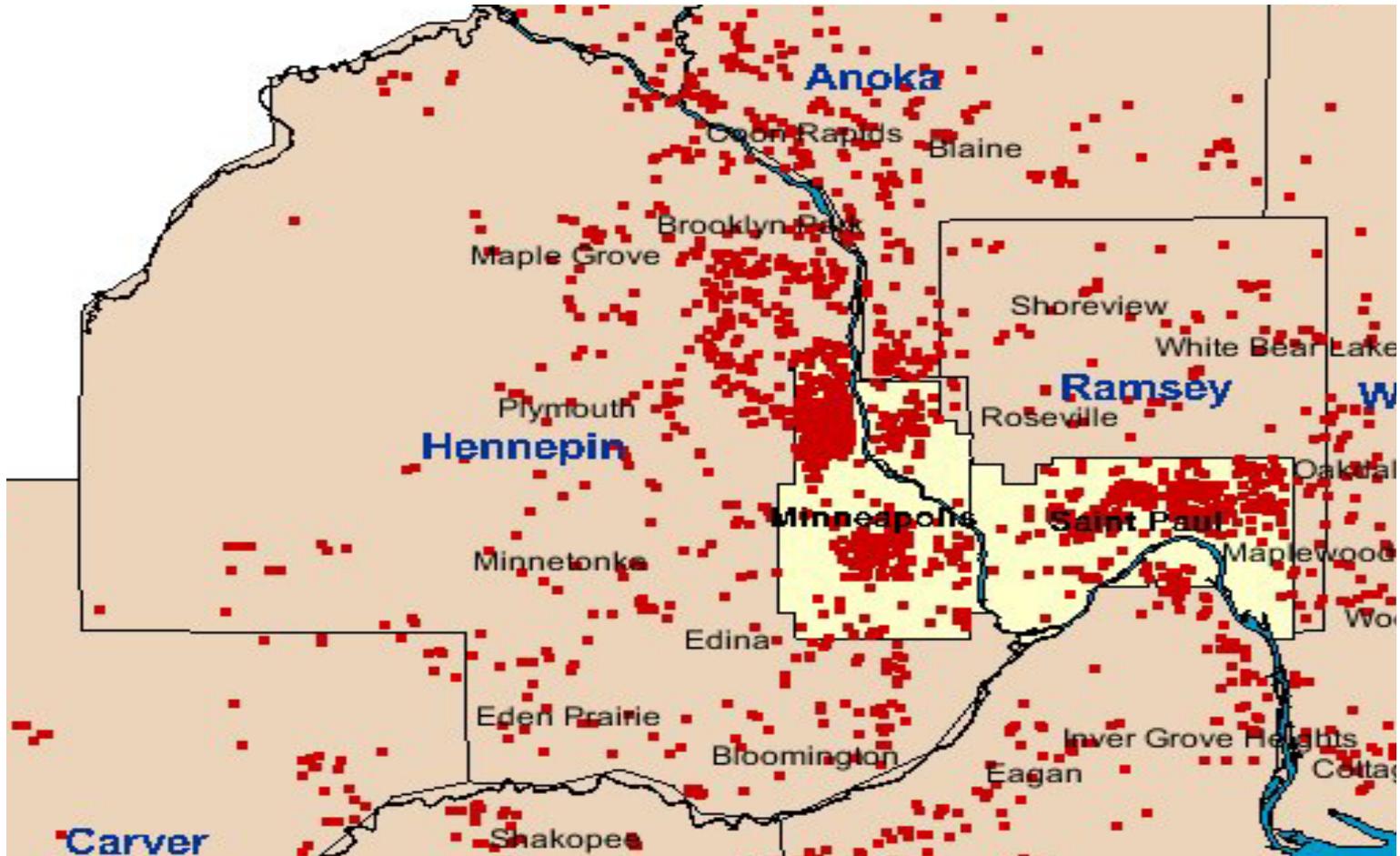


Data Source: Home Mortgage Disclosure Act, 2002; and Hennepin and Ramsey Counties, 2003

Source of Graph: Jeff Crump, *Suprime Lending and Foreclosure in Hennepin and Ramsey Counties: An Empirical Analysis*

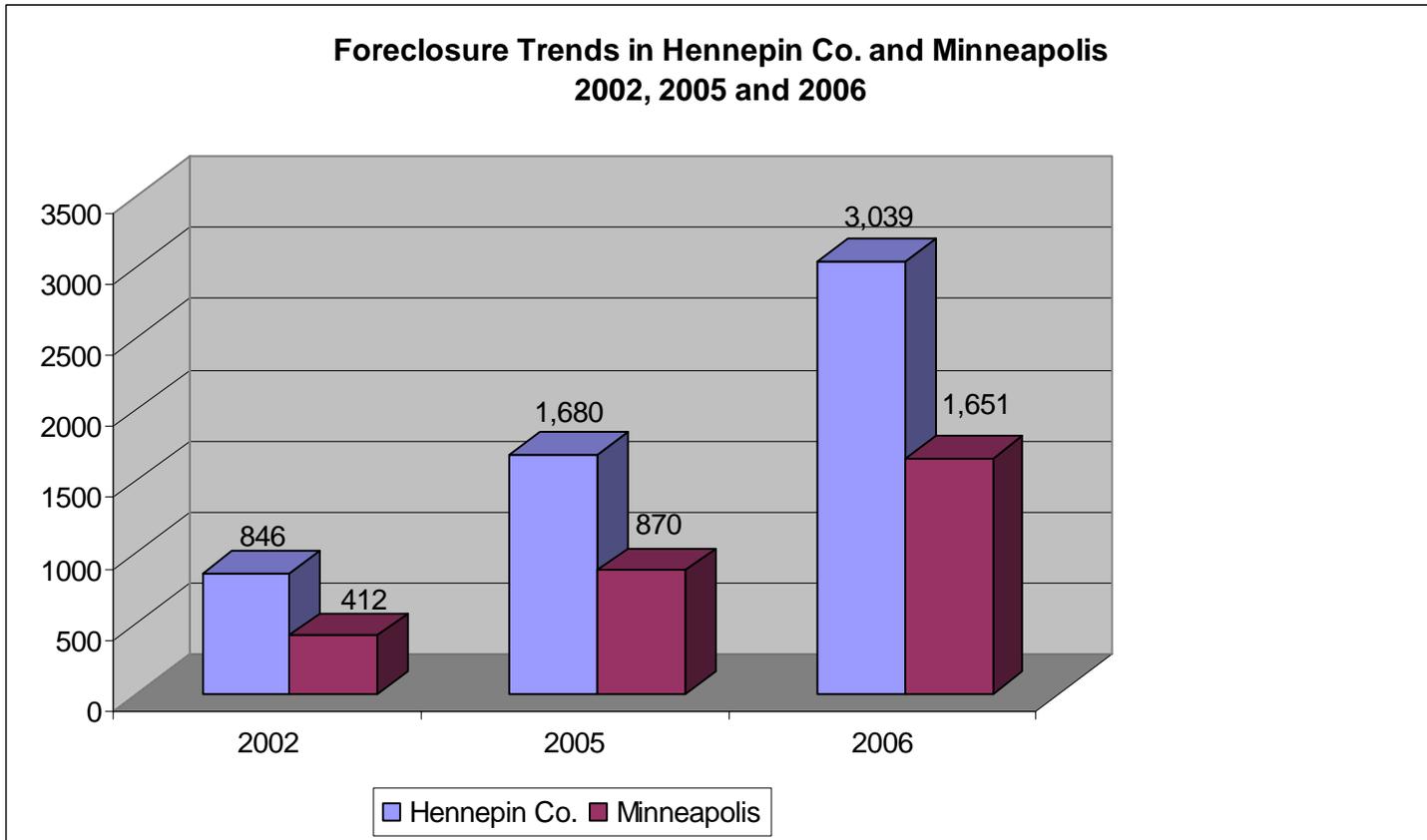
www.cura.umn.edu/reporter/05-Spr/Crump.pdf

Metro Foreclosures



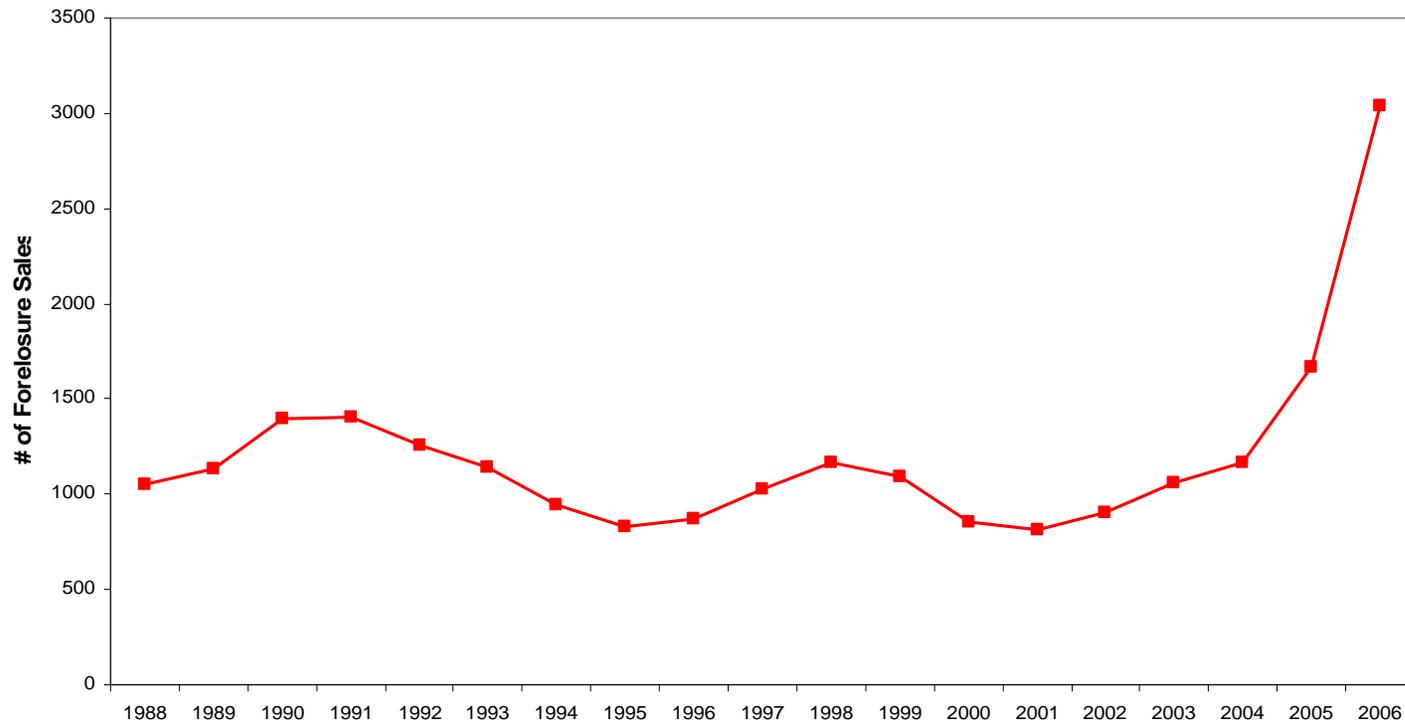
Excerpt from a map published by the *Pioneer Press*, 9/24/06

[City & County Trends]



Dramatic Spike in Foreclosures

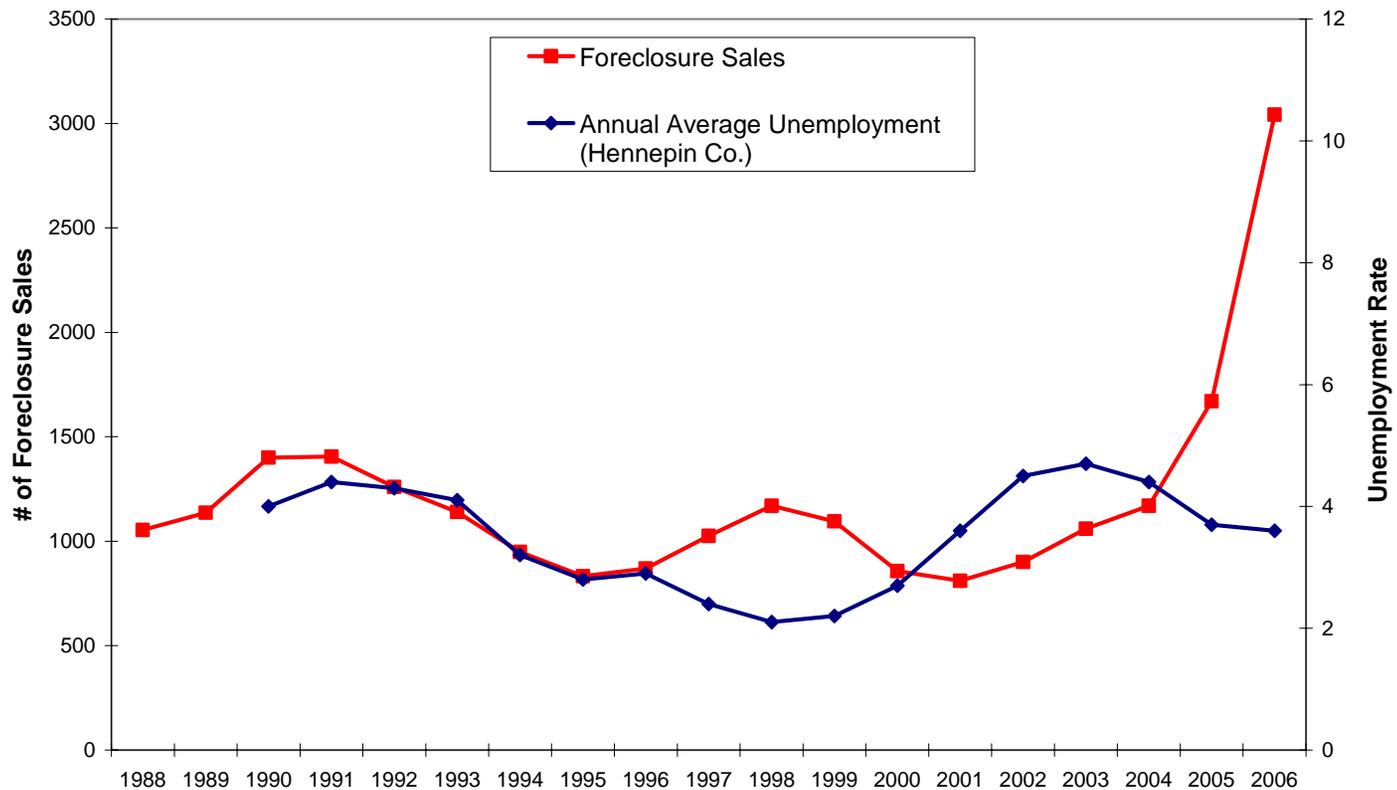
Hennepin County Foreclosures, 1988-2006



Data Source: Hennepin County Sheriff's Office. Chart from a presentation by Prentiss Cox.

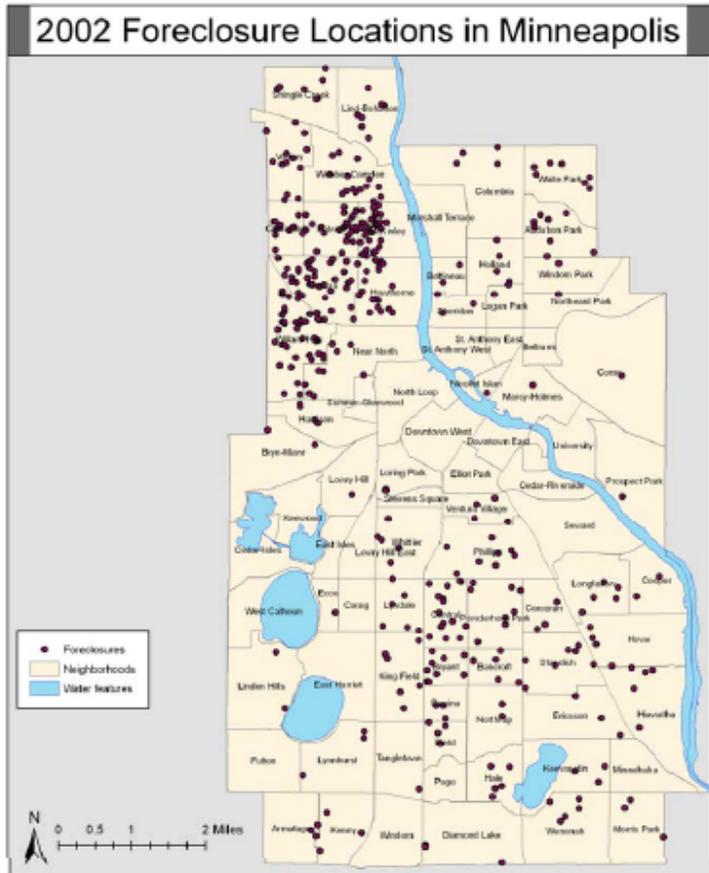
No Obvious Link to Unemployment

Hennepin County Foreclosures and Unemployment, 1988-2006

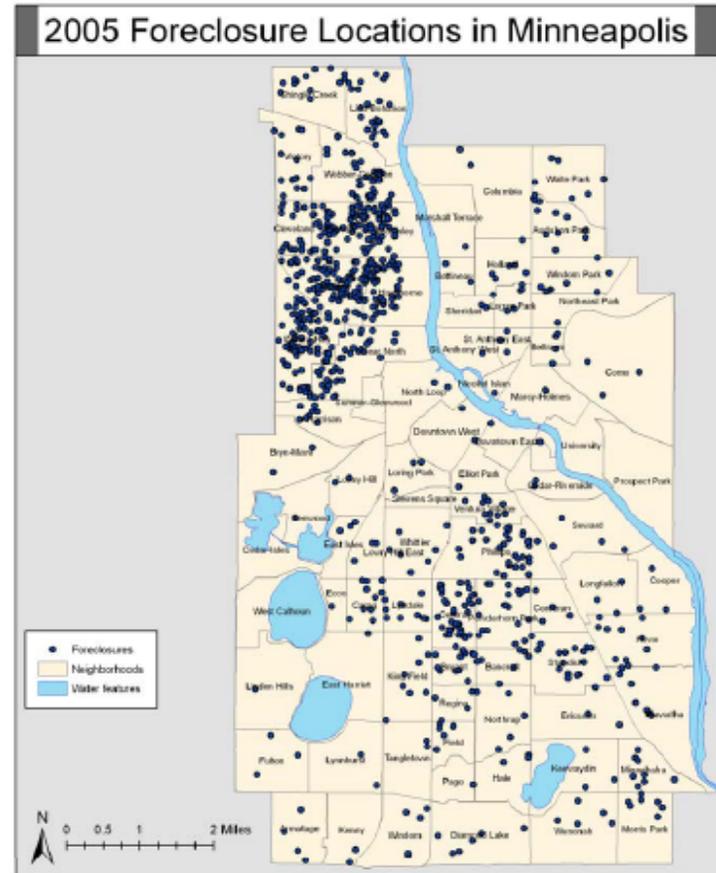


Data Sources: Data from Hennepin County Sheriff's Office, US Bureau of Labor Statistics and Minnesota Department of Employment and Economic Development. Chart by Institute on Race and Poverty, U of Minnesota Law School. Chart from a presentation by Prentiss Cox.

Location of Foreclosures

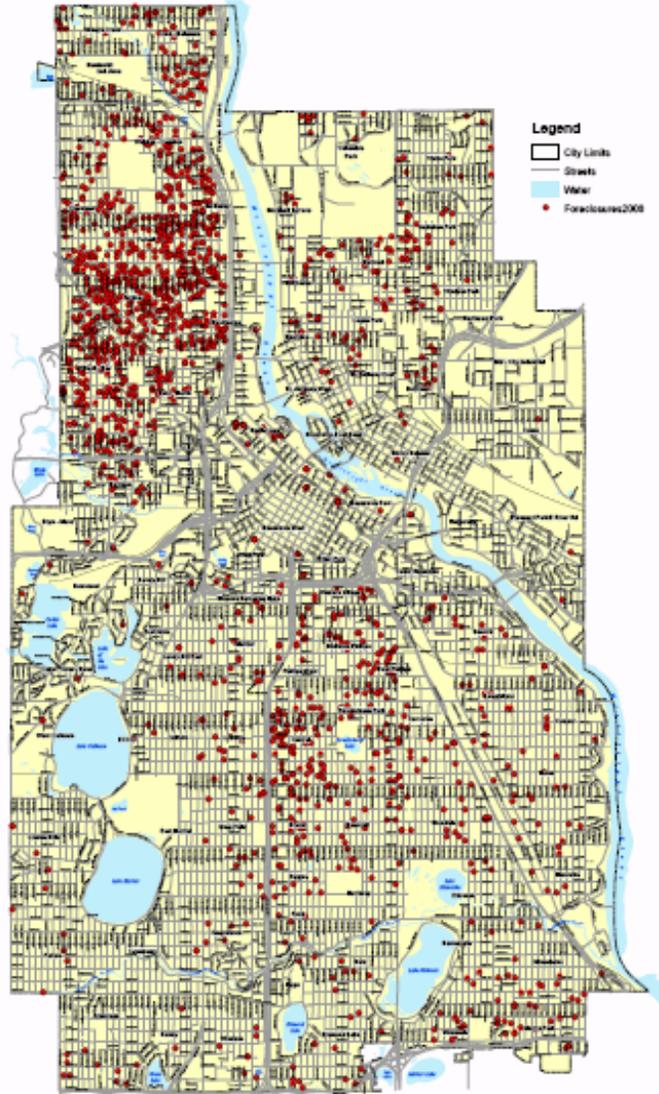


Map Created by: Tim Bates, Fay Cleaveland, Ruth Strickland, Macalester College, April 2006
 Data sources: Hennepin County Sheriff's Office, 2002
 ESRI



Map Created by: Tim Bates, Fay Cleaveland, Ruth Strickland, Macalester College, April 2006
 Data sources: Hennepin County Sheriff's Office, 2005
 ESRI

[Mpls Sheriff Sales (2006)]



[Community Effects]

- Three “Victims”
 - Homeowner
 - Neighborhood
 - Larger Community



2700 Penn Ave N



2717 Penn Ave N



2720-2422 Penn Ave N



2724 Penn Ave N

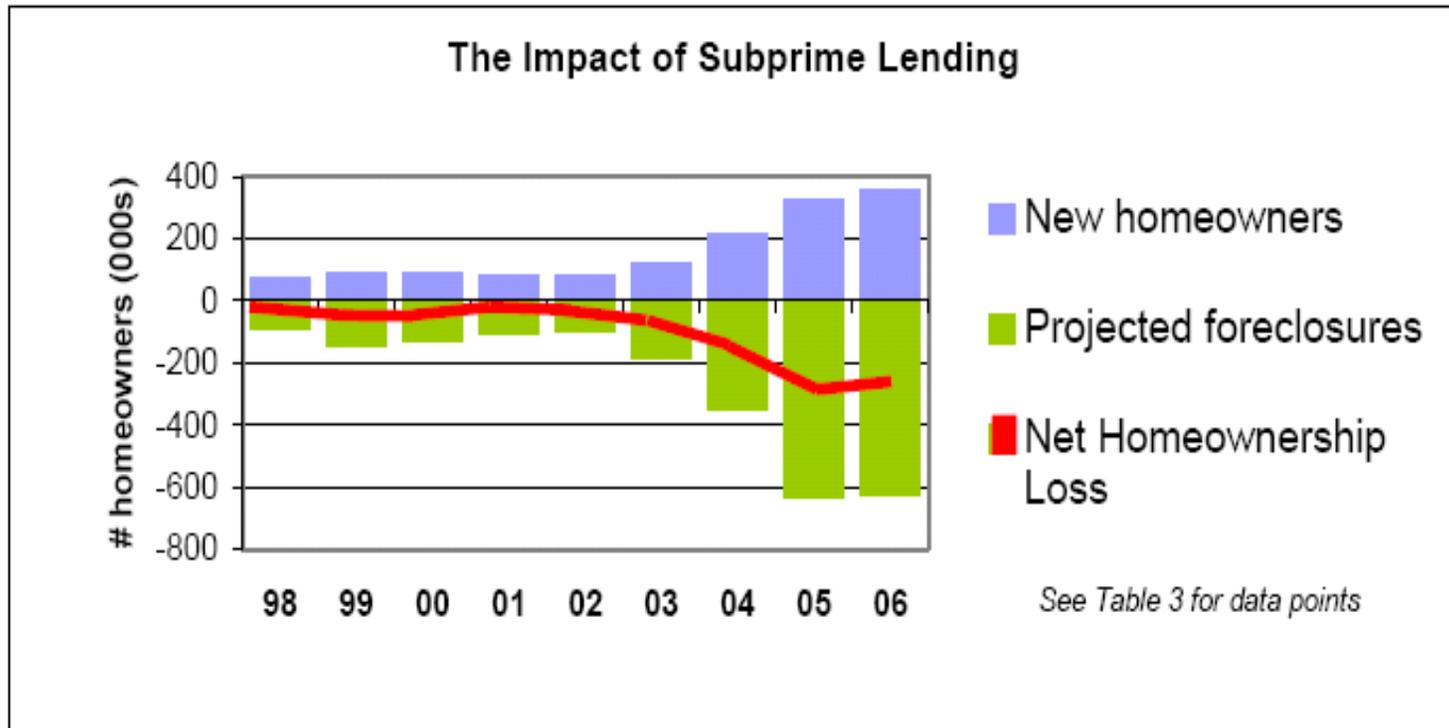
Community Effects- Homeowners

- Housing & Homelessness
- Wealth
- Credit
- Social Capital



Source of Picture: Family Housing Fund

Overall Loss in Homeownership



One Million Lost to Sub-prime

National Net Impact on Homeownership from Sub-Prime Lending

	Estimated Subprime Loans to First-Time Homebuyers (Homeownership Gain)	Projected Subprime Foreclosures (Homeownership Loss)	Net Homeownership Gain or (Loss)
1998	73,253	94,750	(21,497)
1999	89,309	144,567	(55,258)
2000	87,651	133,126	(45,475)
2001	80,856	105,464	(24,608)
2002	85,883	102,252	(16,369)
2003	120,807	181,464	(60,657)
2004	219,180	348,345	(129,165)
2005	324,361	632,302	(307,941)
2006	354,172	624,631	(270,459)
TOTAL 98-06	1,435,472	2,366,901	(931,429)

Community Effects- Neighborhood

- Neighborhood
 - Property Values
 - Crime (police calls)
 - Dangerous conditions (explosions)
 - Divestment
 - Remediation costs



Source of picture: CPED – City of Minneapolis

Community Effects - Neighborhood



- Homes Currently in Foreclosure As Of December 2006 in one section of north Minneapolis.

Source: Community Planning and Economic Development, City of Minneapolis

Community Effects - Community

No Downpayment Necessary

Housing prices and home budgets are no longer constrained by a family's ability to save the once-required 20% downpayment.

No Documentation, Either

Borrowers no longer have to demonstrate their ability to repay a loan with proof of employment, income, financial assets, and credit history. Without that hurdle to clear, homebuyers and mortgage brokers have an

incentive to fudge budgets.

Exotic Mortgages

With a traditional 30-year, fixed-rate mortgage, borrowers must have the income to pay both interest and principal. Loans sold on their monthly minimum payments, such as interest-only loans, lure borrowers into debts they have difficulty repaying.

Rising Debt-to-Income Levels

Mortgage payments, property taxes, and other

homeownership costs once added up to no more than a third of a homebuyer's income. Lenders now routinely allow such payments to consume as much as half of a borrower's income.

The House as Piggy Bank

Overstretched homeowners are still pulling huge piles of cash out of their homes, either through refinancing or home equity loans. These days they're increasingly using the money to pay the mortgage, temporarily escaping foreclosure.

Data: Euro Pacific Capital Inc., BusinessWeek

- **Larger Community**
 - Hurts emerging markets
 - All stretched to respond
 - Increased city service costs

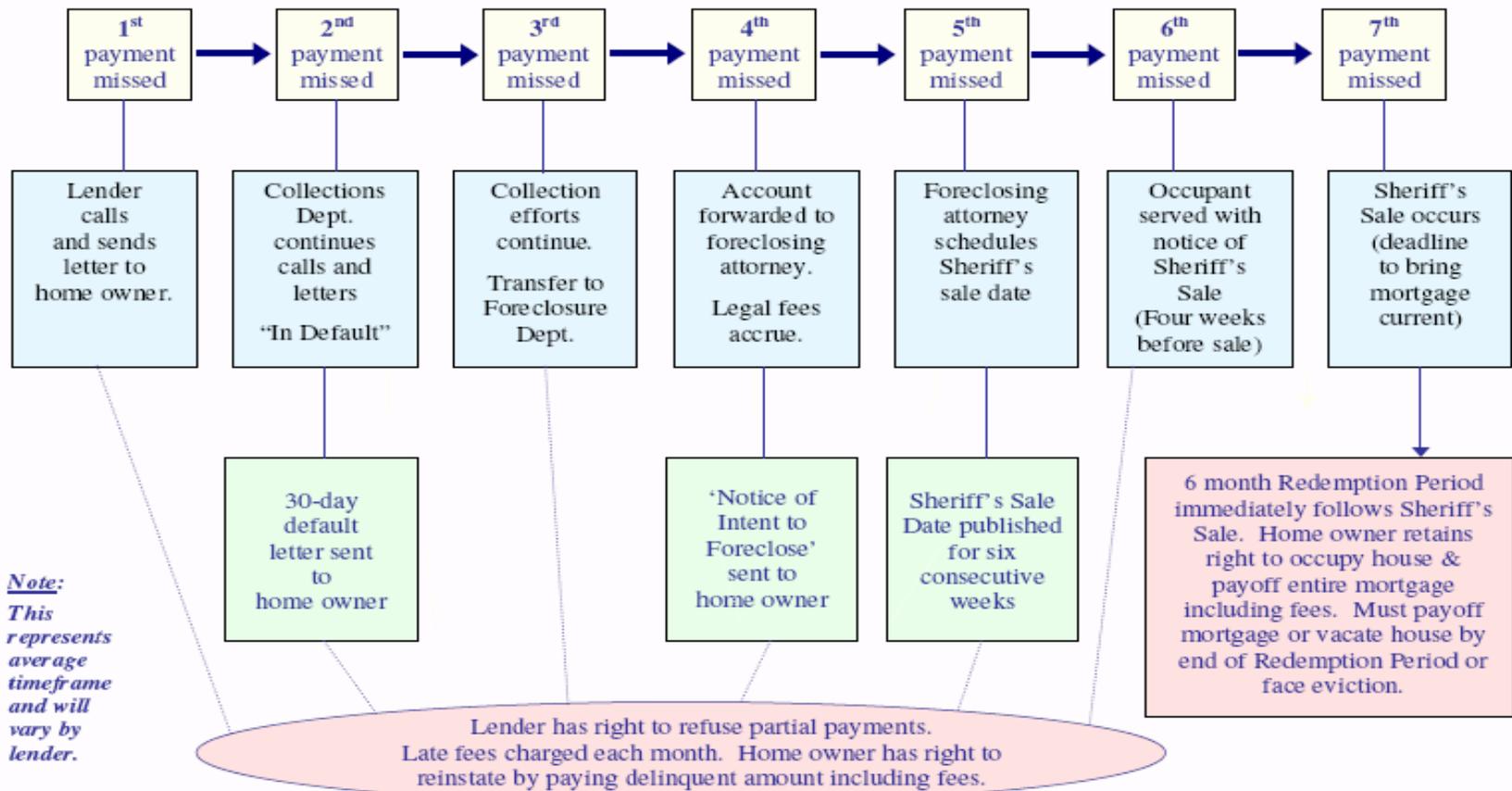
Community Effects – City Costs

Characteristics	Direct Municipal Cost	Number of Agencies Involved
Foreclosure, Sold at Auction, Never Vacant	\$ 27	5
Foreclosure, Sold at Auction, Vacant/Secured	\$ 430	7
Foreclosure, Sold at Auction, Vacant/Unsecured, DOAH	\$ 5,358	9
Foreclosure, Sold at Auction, Vacant/Unsecured, Housing Court	\$ 7,020	8
Foreclosure, Sold at Auction, Vacant/Unsecured, DOAH, Modest Criminal Activity	\$ 5,673	10
Foreclosure, Sold at Auction, Vacant/Unsecured, DOAH, Significant Criminal Activity	\$ 6,753	10
Foreclosure, Sold at Auction, Vacant/Unsecured, Fast Track, Modest Criminal Activity	\$ 13,452	9
Foreclosure, Sold at Auction, Vacant/Unsecured, Demo Court, Modest Criminal Activity	\$ 13,324	9
No Foreclosure, Vacant/Unsecured, Modest Criminal Activity, Structure Demolished	\$ 19,227	11
Severe case with Fire	\$ 34,199	12

[Primer on the Process]

- Processes in Minnesota
 - Non-Judicial Foreclosure (580.01 *et seq*)
 - Judicial Foreclosure (581.01 *et seq*)
 - Voluntary Foreclosure (582.32)
- Reinstatement Period (580.30)
- Sheriff Sale
- Redemption Period
 - Five weeks for vacant/blighted property
 - Two months for voluntary foreclosure
 - Six months generally
 - Twelve months for agricultural property

Missed Payment Timeline



[New Law]

- HF1004 (was substituted for SF809) passed the Senate floor (60 yes, 0 no) on April 13, 2007
 - Governor signed on April 20, 2007
 - *Laws of Minnesota*, Chapter 18
 - Amends
 - Sec. 58.02, by adding a subd.
 - Sec. 58.13, subd. 1
 - Sec. 58.137, subd. 1
 - Sec. 58.15
 - Sec. 58.16, subd. 1

[New Law]

- HF1004 (subs't for SF 809) key provisions:
 - Defines “fully indexed rate”
 - Lender must verify borrower’s ability to repay loan
 - Prohibits knowingly making a loan that does not provide a tangible net benefit to borrower (“churning”)
 - Prohibits negative amortization loans
 - Requires oral disclosures about the actual or anticipated payment amount if terms exclude taxes and insurances
 - Added yield spread premium to 5% cap on financed fees (3rd party fees excluded)
 - Mortgage broker “duty of agency”
 - Effective date: August 1, 2007

[Other Bills to Watch]

- HF931 (Mullery)/ SF988 (Higgins)
 - Predatory mortgage lending practices enforcement provisions
 - Defines sub-prime
 - Prohibits refinancing a “special mortgage” in some instances
 - Prohibits prepayment penalties on sub-prime loans
 - Creates a private right of action for those injured by acts under sections of Chapter 58
 - Defines and prohibits “residential mortgage fraud” and establishes criminal penalties
 - Provides private right of action for injuries under Chapter 82B

Other Bills to Watch

- HF1209 (Mullery)/ SF1533 (Pappas)
 - Amends M.S. Ch. 325N
 - Amends definitions for “foreclosure consultant”, “foreclosure reconveyance”, “residence in foreclosure”, “foreclosure purchaser”, “closing”, and “consideration”
 - Changes requirements related to delivery of notice of cancellation of a foreclosure consultant contract
 - Clarifies that it is a violation for a foreclosure consultant to offer a loan secured by the residence in foreclosure or any other real or personal property
 - Clarifies the compliance requirements for a foreclosure purchaser
 - Requires a court hearing an eviction action against a foreclosed homeowner to issue an automatic stay in some instances, providing a \$500 penalty for a frivolous claim or defense, expiration of the automatic stay, and sanctions
 - Eliminates December 31, 2009 expiration date for Chapter 325N

[Other Bills to Watch]

- HF2249 (Clark)/ SF357 (Berglin)
 - Regulates property transfers between low income and moderate income housing developers and local units of government
 - Requires that if a nonprofit organization receives funding from the agency for a project to construct or rehabilitate low-income or moderate-income housing, and a city, a county, or an agency of a city or a county is transferring property to the organization for the project, the city or county must convey or otherwise transfer the property to the organization for a consideration no greater than the cost to the city or county for acquisition of the property
 - City or county must also waive all development and other fees related to the project that it would otherwise impose

Other Bills to Watch

■ HF211 (Zellers)/ SF241 (Limmer)

- Prohibiting consumer reporting agencies or other business entities from selling or exchanging the existence of credit inquiries arising from mortgage loan applications, exceptions; increasing the dollar amount of the homestead exemption and providing for inflation adjustments
- Modifying limitation provisions relating to homestead property
- Modifying the statute of limitations on civil actions for damages based on services or construction to improve real property
- Requiring the executing creditor to obtain a court order directing a sale of the real property including a homestead prior to service of the notice of execution
- Prohibiting real property from being subject to execution under certain conditions
- Requiring a judgment creditor to record a certified copy of the order directing sale of real property
- Modifying service on judgment of debtor provisions
- Requiring sheriff to file a report of the sale with the court, providing for confirmation and resale provisions
- Modifying certificate of sale of realty and redemption of realty provisions

[Other Bills to Watch]

- Appropriations in omnibus bills

Non-Legislative Prevention Efforts

■ Foreclosure Prevention Funders Council

- Family Housing Fund initiative
- Council members:
 - Cecile Bedor, City of Saint Paul – PED
 - Tom Fulton, Family Housing Fund
 - Mike Haley, Minnesota Housing
 - Shawn Huckleby, Emerging Markets Homeownership Initiative
 - Colleen O'Brien, HousingLink
 - Carolyn Olson, Greater Metropolitan Housing Corporation
 - (CHAIR) Elizabeth Ryan, City of Minneapolis – CPED
 - Mark Ulfers, Dakota County Comm. Dev. Agency
 - Linda White, Fannie Mae
 - Julie Gugin, Home Ownership Center
- Project Coordinator, Melissa Manderschied

Non-Legislative Prevention Efforts

- Working with Data Collectors
 - Sheriff's Associations
 - Center for Urban and Regional Affairs (CURA)
 - City of Minneapolis Early Warning System
 - Employ cost-effective, timely use of indicators
 - Delinquent on utility or tax payments
 - Several, close in time, refinances
 - Increase in deferred maintenance
 - City of Saint Paul

[Non-Legislative Prevention Efforts]

- Working with Lenders
 - Discussing use of liquidation options
 - Focusing initial remediation efforts on priority areas
 - Increased coordination with homeownership counselors (i.e., dedicated call line)
 - Counselor education on loss mitigation procedures

[Non-Legislative Prevention Efforts]

- Working with Funders
 - Developing dedicated pool of funds for strategic acquisition
 - Developing new tools and refining existing tools to address pre and post foreclosure situations
 - Using early warning system

Prevention Efforts

- Working with Counselors
 - Data collection efforts
 - Increase understanding of various lenders' loss mitigation procedures
 - Dedicated call lines
 - Increase community awareness of counselor's availability (i.e., working with utility companies to advertise counseling services; inserts in property tax bills; inserts in water bills; etc)

[Non-Legislative Prevention Efforts]

- Working with Media
 - Developing a multi-language DVD explains homeowner rights and obligations
 - Developing PSAs for TV and radio
 - Advertising counselor services in community newspapers

[For More Information]

- Elizabeth Ryan
 - City of Minneapolis
 - 612.673.5127
- Melissa Manderschied
 - Kennedy & Graven
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This presentation will be posted on the CPED website.