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MORTGAGE FORECLOSURES, MORTGAGE MORALITY, AND MAIN STREET:

WHAT'S REALLY HAPPENING?

JENNIFER M. SMITH*

A bank is a place where they lend you an umbrella in fair weather and ask for it back when it rains.[1]

INTRODUCTION

The American economy is in the tank. Millions of citizens are without jobs, overwhelmed with credit card debt, and losing their homes. The brighter side is that as a result, America has finally embraced financial reform,[2] and the unstable economy is stabilizing marriages.[3] Nevertheless, the United States remains in the midst of a housing crisis, and the ending

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1 Robert Frost, Brainy Quotes, http://www.brainyquote.com/quotes/quotes/r/robertfros163221.html (last visited Feb. 10, 2011).

2 Wall Street and Consumer Protection Act of 2010, Pub. L. No. 111-203 (2009-10) ("A bill to promote the financial stability of the United States by improving accountability and transparency in the financial system, to end 'too big to fail,' to protect the American taxpayer by ending bailouts, to protect consumers from abusive financial services practices, and for other purposes.").

3 DANNY SCHECHTER, PLUNDER, INVESTIGATING OUR ECONOMIC CALAMITY AND THE SUBPRIME SCANDAL 165 (2008) (reporting that divorce filings are down 20 percent, about the same percentage as the drop in real estate values (18 percent) for the same period in 2007).

remains uncertain.

By the end of 2009, more than 11 million residential properties with mortgages were "underwater" (that is had negative equity).[4] This equates to roughly 24 percent of the nation's total homes.[5] As a whole, the national picture appears dim; however, the concentration of these homes that are underwater is in five states: in Nevada, 70 percent of homes are underwater; in Arizona 51 percent are underwater; in Florida 48 percent are underwater; in Michigan 39 percent are underwater; and in California 35 percent of homes are underwater.[6] These were also the states with some of the most expensive and thus, unaffordable homes in the country, so they made the best locations for new and exotic loans that formed the basis of the subprime loan industry.[7]

Earlier in 2009, it appeared that mortgage delinquencies were down, perhaps suggesting that the default crisis was peaking. But, by December 2009, foreclosure filings had increased, even though there was an alleged effort to suspend these filings during the holidays. Presently, the states with the highest foreclosure filings include: Nevada, Arizona, California, and Florida.[8] New York City was the nation's leading city for mortgage fraud in 2009.[9]

In 2009, 22 percent of foreclosures - roughly one-fourth of all foreclosures—were strategic,[10] meaning that the homeowner had no financial hardship other than the fact that the home was underwater.[11] That figure has increased in 2010 to about 31 percent.[12] Currently, there are 16

[4] Steve Cook, *One Quarter of Mortgage Holders Sink Underwater*, REAL ESTATE ECONOMY WATCH (Feb. 23, 2010), http://www.upi.com/Real-Estate/2010/02/23/One-Quarter-of-Mortgage-Holders-Sink-Underwater/9061266952157/ ("Negative equity, or 'underwater' or 'upside down,' means that borrowers owe more on their mortgage than their homes are worth. Negative equity can occur because of a decline in value, an increase in mortgage debt or a combination of both.").

[5] *Id.*

[6] *Id.*

[7] *See* Patricia A. McCoy, Andrey D. Pavlov, & Susan M. Wachter, *Systemic Risk Through Securitization: The Result of Deregulation and Regulatory Failure*, 41 CONN. L. REV. 493, 505 (2009); *see also* MARK ZANDI, FINANCIAL SHOCK: A 360° LOOK AT THE SUBPRIME MORTGAGE IMPLOSION, AND HOW TO AVOID THE NEXT FINANCIAL CRISIS 34 ("More than one-third of the loans made in 2006 in the Central Valley of California and throughout south Florida were subprime."); Lisa Gibbs, *Drowning in Debt*, CNN Money, http://money.cnn.com/2010/05/05/pf/home_debt.moneymag/index.htm (last visited Feb. 10, 2011); Brent White, *Underwater and Not Walking Away: Shame, Fear, and the Social Management of the Housing Crisis*, 45 WAKE FOREST L. REV. 971 (2009).

[8] *June U.S. Foreclosures -2.8% vs. May; -7% Y/Y*, REALTY TRAC, July 14, 2010, http://imarketnews.com/node/16482.

[9] Megan Mollman, *America's Mortgage Fraud Capital? New York, N.Y.*, AOL REAL ESTATE, Apr. 27, 2010, http://realestate.aol.com/blog/2010/04/27/new-york-is-nations-no-1-for-mortgage-fraud/.

[10] Diana Olick, *BofA: Mortgage Walkaways Have Huge Incentive*, CNBC, June 2, 2010, http://www.cnbc.com/id/37471499/BofA_Mortgage_Walkaways_Have_Huge_Incentive.

[11] White, supra note 7, at 979-80.

[12] Olick, *supra* note 10.

million homes with negative equity, and about ten million of those homes are underwater by 20 percent or more.[13] As of 2007, lenders filed over six million foreclosures against home owners and that number is projected to double by 2010; more than one in four home owners owe more for their property than what it is worth; and one in nine home owners are seriously delinquent on their mortgage.[14]

There has been a media blitz about the housing crisis and Wall Street – corporate interests, but much less about the actual impact of the housing crisis on Main Street – America's working class people and small business owners. This article will also provide insight into what is really happening with the mortgage crisis and to Main Street America, why it is happening, and what can be done to save Main Street.

I. BACKGROUND

A. Tulips, Houses, and Bubbles

"Tulipmania," an obsession that the Dutch had with the tulip trade in the first four decades of the Seventeenth century,[15] has been compared with the current housing crisis.[16] Whether this comparison is appropriate depends upon whether "Tulipmania" is "fact or artifact";[17] it has been described as both.[18]

Modern references to Tulipmania begin with a recitation of the legend of Holland's tulips from Clarence Mackay.[19] Originating in Turkey, diffused

13 Calculated Risk, *Negative Equity Breakdown*, http://www.calculatedriskblog.com/2010/07/negative-equity-breakdown.html (July 31, 2010).

14 Center for Responsible Lending, *Snapshot of a Foreclosure Crisis: 15 Fast Facts*, March 17, 2010, at 1, http://www.responsiblelending.org/mortgage-lending/research-analysis/snapshot-of-foreclosure-crisis.pdf.

15 Scott Horton, *The Bubble Bursts*, HARPER'S MAGAZINE, Jan. 27, 2008, *available at* http://www.harpers.org/archive/2008/01/hbc-90002258.

16 ROBERT SHILLER, THE SUBPRIME SOLUTION, HOW TODAY'S GLOBAL FINANCIAL CRISIS HAPPENED, AND WHAT TO DO ABOUT IT? 62 (2008) ("What has changed since the 1990s to make us suddenly avid speculators in homes in so many different places? Trying to answer that question requires that we go back to consider the forces that generate bubbles. Why, for example, was there a tulip mania in Holland in the 1630s – and why has the speculative fascination with tulips since left our collective consciousness?"); *see also Bubble and Bust*, WASH. POST, Aug. 11, 2007, *available at* http://www.washingtonpost.com/wp-dyn/content/article/2007/08/10/AR2007081001912.html; Horton, *supra* note 15.

17 Earl A. Thompson and Jonathan Treussard, *The Tulipmania: Fact or Artifact* (2002), http://www.dklevine.com/archive/thompson-tulips.pdf; ANNE GOLDGAR, TULIPMANIA: MONEY HONOR, AND KNOWLEDGE IN THE DUTCH GOLDEN AGE 5-6 (2007).

18 GOLDGAR, *supra* note 17, at 2-3.

19 Peter M. Garber, *Tulipmania*, 97 J. POL. ECON. 535, 537 (1989)(citing CLARENCE MACKAY, *EXTRAORDINARY POPULAR DELUSIONS & THE MADNESS OF CROWDS* (1852)); GOLDGAR, *supra* note 17, at 5 (citing CHARLES MCKAY, EXTRAORDINARY POPULAR DELUSIONS AND THE MADNESS OF CROWDS

into Western Europe in the mid-sixteenth century, and carried initially to Australia, the tulip became accepted by the wealthy as a rare flower.[20] The market, however, was not for flowers, but for the durable tulip bulbs.[21] The Dutch dominated this tulip market and began developing methods to create varieties of beautiful tulips.[22] These tulip bulbs that resulted in unique patterned flowers commanded high prices, unlike the tulip bulb that produced common flowers.[23]

In 1634, nonprofessionals entered the tulip trade in vast numbers, and the tulip bulbs began to reach enormous prices.[24] By way of example, a Semper Augustus bulb sold for the equivalent of $50,000.[25] In February 1637, the contract prices of tulips were 20 times more than tulip prices in November 1636 and May 1637.[26] As the story goes, foreign monies began entering the market, various economic classes of people liquidated other assets to participate in this tulip trade.[27] Then the mania ended and almost overnight, no market existed for these tulip bulbs, creating a lengthy economic distress.[28] "A crash was inevitable. It came in 1637."[29] The collapse of this market disabled the Dutch economy for years, "establishing a cautionary model of speculative excess that investors have learned from, and ignored, in a seemingly endless cycle of bubble and bust ever since."[30]

In the 1950's, the legend of Tulipmania was revived in respected economic journals discussing the development of the capital theory.[31] In

(1852)) (pointing out that most of the modern-day images of the tulip are from Mackay's book).

20 *See* Garber, *supra* note 19, at 537.

21 *Id.*

22 *Id.*

23 *Id.*

24 *Id.*

25 *See id.* at 537; *Bubble and Bust*, *supra* note 16 (reporting that In 1637, at the peak of tulip mania, tulip bulbs were selling for the equivalent of roughly $76,000 each, and tulip options were trading on markets all over Europe); *but see* GOLDGAR, *supra* note 17, at 225 (noting discrepancies in the price levels).

26 Thompson, *supra* note 17, at 2.

27 Garber, *supra* note 19, at 538.

28 *Id.*

29 Horton, *supra* note 15; GOLDGAR, *supra* note 17, at 224.

30 *See Bubble and Bust*, *supra* note 16; *see also* Thompson, *supra* note 17 (concluding that "tulipmania was not a bubble because bubbles require the existence of mutually-agreed-upon prices that exceeded fundamental values. The 'tulipmania' was simply a period during which the prices in futures contracts had been legally, albeit temporarily, converted into options exercise prices"); GOLDGAR, *supra* note 17, at 7 ("Tulipmania did not destroy the economy, or even the livelihoods of most participants. But that does not mean that tulipmania was not a crisis. It might not have been a financial crisis, but it was a social and cultural one. In tulipmania, Dutch burghers confronted a series of issues that in any case gripped their culture: novelty, the exotic, capitalism, immigration, the growth of urban societies, and all the problems and excitement such issues raised").

31 Garber, *supra* note 19, at 537.

the 1980's, Tulipmania appeared in financial literature.[32] And in 2007, Tulipmania resurfaced as a comparison to the current housing bubble.

Prior to the housing bubble was the housing boom, which lasted from the mid-1990s through the early 2000s, wherein there was a strong housing demand by buyers desiring to keep their homes and a well-disciplined new housing supply.[33] "The boom had been based on solid demand and supply fundamentals: things such as affordable homes, strong incomes, and ample household savings."[34] Then, the housing bubble, born out of the housing boom, arrived without warning roughly around mid-2003.[35] "The bubble developed when Americans started buying not simply because they needed someplace to live, but because they thought housing was a great investment."[36] Then, the housing bubble began showing signs of leaking in the second quarter of 2006 when real estate speculators left the market, subprime loans were beginning to default, and adjustable rate mortgages' (ARM) teaser rates were expiring.[37] By the summer of 2007, the subprime crisis was in full swing, and it was now news that the housing market had crashed.[38]

This housing bubble bust has placed America's residential housing market in a critical state, and the housing bubble has impacted countries other than the United States and includes residential as well as commercial real estate.[39] "[S]ubprime home buyers unable to make good on their mortgage payments set off a financial avalanche in 2007 that pushed the United States into a recession and hit major economies around the globe."[40] The U.S. economy was unstable by early 2008.[41] "The bursting of the housing bubble and the waves of mortgage defaults that followed brought on the subprime shock; conversely, the shock and subsequent credit crunch accelerated the housing crash."[42]

32 *Id.*

33 *See* ZANDI, *supra* note 7, at 159 (explaining the housing boom of the 1990's and early 2000's).

34 *Id.* at 161.

35 *See id.*

36 *Id.* at 161-62.

37 *See id.* at 165-66; John Hull, *Derivatives and Risk Management, The Financial Crisis of 2007: Another Case of Irrational Exuberance, in* THE FINANCE CRISIS AND RESCUE, WHAT WENT WRONG? WHY? WHAT LESSONS CAN BE LEARNED? 17, 19-20 (2008).

38 ZANDI, *supra* note 7, at 167-68.

39 Christopher Mayer, *Housing, Subprime Mortgages, and Securitization: How Did We Go Wrong and What Can We Learn So This Doesn't Happen Again?* 5-6, http://www.1010data.com/media/4317/chris_mayer_1010.pdf (last visited Feb. 18, 2011).

40 *See* ZANDI, *supra* note 7, at 9; HERMAN M. SCHWARTZ, SUBPRIME NATION 200 (2009); *see also*, Martin Wolf, FIXING GLOBAL FINANCE 3 (2008).

41 ZANDI, *supra* note 7, at 213.

42 *See* ZANDI, *supra* note 7, at 215; ADAM B. ASHCRAFT AND TIL SCHUERMANN,

The subprime mortgage crisis has been compared to Tulipmania.[43] Subprime mortgages are loans "made to someone with a weak or troubled credit history."[44] Initially, it was believed that the poor, largely minorities, were the main targets of these high interest loans; however, research has shown that thousands of middle class, and even upper class, Americans with strong credit histories also became victims of this subprime scam. "Hundreds of billions of dollars worth of these paper commitments have been made, gathered together and resold as bonds to hedge funds and banks all over the world – which in turn have used them as collateral to obtain more loans, so they can buy more bonds, and so on."[45] The subprime market grew from $150 billion in 2000 to $650 billion in 2007 – approximately 25 percent of the total mortgage market.[46] Then when housing prices began to fall and borrowers began defaulting, the subprime business began unraveling, and the world entered "the grip of a liquidity crisis."[47] "The subprime mortgage crisis threatens this country with its greatest economic downturn in the last 30 years, and perhaps since World War II."[48]

B. Theories of the Housing Crisis

a. Background

Economists and other financial professionals have theorized that the causes of the housing bubble have included "lack of regulation to too much regulation; from political pressure on banks to extend mortgages to unqualified buyers; to the greed of extravagantly compensated and arrogant Wall Street financiers who created exotic financial instruments designed to avoid capital requirements and attain extreme leverage; from conflicts of interest on the part of appraisers, auditors, and rating agencies, to incompetent regulators; and from the greed of homeowners to the greed of

UNDERSTANDING THE SECURITIZATION OF SUBPRIME MORTGAGE CREDIT 27 (2008) (stating that subprime borrowers typically declared bankruptcy in the last 5 years, and had a low credit bureau risk score (FICO), high debt service t- income, a prior repossession, charge off, or foreclosure, or two or more delinquencies in the past year or two); *see also* FIRST FOCUS: THE SUBPRIME CRISIS 77 (2008).

43 *Bubble and Bust*, *supra* note 16; Horton, *supra* note 15.

44 ZANDI, *supra* note 7, at 9.

45 *Bubble and Bust, supra* note 16.

46 Brian E. Robison, *Litigation in the Wake of the Subprime Lending Collapse: What Has Happened and Where We Are*, *in* FIRST FOCUS: THE SUBPRIME CRISIS 59 (2008).

47 *Bubble and Bust*, *supra* note 16; Donald R. Kirk, *How to Prepare for Subprime-Related Litigation*, *in* FIRST FOCUS: THE SUBPRIME CRISIS 67 (2008) (the subprime mortgage affected U.S. and global financial markets).

48 William R. Martin and Kerry Brainard Verdi, *The Subprime Mortgage Crisis: Somebody Has to Pay*, *in* FIRST FOCUS: THE SUBPRIME CRISIS 107 (2008).

lenders."[49] The Center for Responsible Lending (a pro consumer group) reported that key financial experts primarily rest the housing crisis on poor and risky mortgage products due to lax underwriting standards, coupled with selfish, unethical lenders:[50]

Ben Bernanke, Chairman of the Federal Reserve Board:

> That conclusion suggests that the best response to the housing bubble would have been regulatory, not monetary. Stronger regulation and supervision aimed at problems with underwriting practices and lenders' risk management would have been a more effective and surgical approach to constraining the housing bubble than a general increase in interest rates. (*"Monetary Policy and the Housing Bubble," a speech given at the annual meeting of the American Economic Association in Atlanta, Georgia – January 3, 2010*).
>
> Although the high rate of delinquency has a number of causes, it seems clear that unfair or deceptive acts and practices by lenders resulted in the extension of many loans, particularly high-cost loans, that were inappropriate for or misled the borrower." (*Written statement by Chairman Bernanke, July 14, 2008*).

Alan Greenspan, former chairman of the Federal Reserve Board

> The big demand was not so much on the part of the borrowers as it was on the part of the suppliers who were giving loans which really most people couldn't afford." (*Jon Meacham and Daniel Gross, "The Oracle Reveals All," Newsweek online, interview with Greenspan*).

Speaker Jon Husted, Ohio House of Representatives (R)

> We as a nation have $9.5 trillion in debt. This is $31,500 per consumer. We have a consumer debt that is $8,300 per capita. That is crippling our economy as a result. We have witnessed

49 Robert Hardaway, *The Great American Housing Bubble*, 35 U. DAYTON L. REV. 33, 34-35 (2009); *see* Hull, *supra* note 37, at 28 (stating that several factors contributed to the financial crisis: relaxed lending standards, complex products, products created to transfer the credit risk to investors, and others); *see also* Michael Krimminger, *"It's Alive!" – Mortgage Risk Reborn: Issues and Possible Solutions*, 17 J. AFF. HOUS. & COM. DEV. L. 259, 261 (2008) ("The current disruptions in the mortgage markets can be traced fundamentally to poor underwriting"); James H. Carr & Katie Davidoff, *Legislative and Regulatory Responses to the Foreclosure Crisis*, 17 J. AFF. HOUS. & COM. DEV. L. 283, 284 (2008) ("Studies and reports on subprime loans have revealed problems in almost every aspect of the subprime lending process. Inappropriate loan products, inadequate underwriting, bloated appraisals, abusive prepayment penalties, excessive broker fees, steering of borrowers to high-cost products, and servicing abuses have been widely reported.").

50 Center for Responsible Lending, *What Caused the Financial Crisis? Quotes by Bankers and Other Experts*, at 1, http://www.responsiblelending.org/mortgage-lending/tools-resources/Quotes-What-Caused-Crisis.pdf (last visited Feb. 18, 2011).

> irresponsible lending as a major factor in slowing our economy. It's not just consumers, but its very large banks and firms on Wall Street. (*http://california.newamerica.net/blogposts/2009/a_free_market_republicans_take_on_payday_lending-24660*).

Brian T. Moynihan, CEO and President, Bank of America

> Over the course of this crisis, we as an industry caused a lot of damage. Never has it been clearer how mistakes made by financial companies can affect Main Street, and we need to learn the lessons of the past few years. (*Testimony to Financial Crisis Inquiry Commission (FCIC) Washington, D.C. – January 13, 2010*).

In addition, in 2008 leaders of the Group of 20 advanced the following as reasons for the crisis:

> During a period of strong global growth, growing capital flows, and prolonged stability earlier this decade, market participants sought higher yields without an adequate appreciation of the risks and failed to exercise proper due diligence. At the same time, weak underwriting standards, unsound risk management practices, increasingly complex and opaque financial products, and consequent excessive leverage combined to create vulnerabilities in the system. Policy-makers, regulators and supervisors, in some advanced countries, did not adequately appreciate and address the risks building up in financial markets, keep pace with financial innovation, or take into account the systemic ramifications of domestic regulatory actions. (Declaration of the Summit on Financial Markets and the World Economy dated 15 November 2008).[51]

Thus, while various theories continue to float and while the blame game is played,[52] what seems clear from the financial experts with various

[51] Housing.com, *Subprime Mortgage Crisis*, http://www.housing.com/categories/foreclosures/foreclosure-survival-guide/subprime-mortgage-crisis.html (last visited Feb. 18, 2011).

[52] SHILLER, *supra* note 16, at 175 ("The aftermath of the subprime crisis has involved considerable finger-pointing."); ZANDI, *supra* note 7, at 126 ("Of all the places you can point the finger for the housing bubble and subprime financial shock, perhaps the most deserving is the removal of responsibility from the financial system."); Mark A. Flessner, *The Subprime Crisis: Are Predatory Lenders to Blame?*, *in* FIRST FOCUS: THE SUBPRIME CRISIS 181 (2008) ("It is clear that these predatory lenders deserve the blame for the current subprime crisis."); Brian E. Robison, *Litigation in the Wake of the Subprime Lending Collapse: What Has Happened and Where We Are*, *in* FIRST FOCUS: THE SUBPRIME CRISIS 60 (2008) (stating that lenders and borrowers gambled on the risky, high-reward subprime loans).

backgrounds and political foci is that, the subprime housing crisis is due in large part to the lax mortgage underwriting standards and deceptive lending practices by banks and other financial companies to borrowers at both ends of the economic spectrum – the poor and the rich. As a result, defaults are occurring rapidly and contagiously.[53] In fact, U.S. housing values are now roughly mid-way down to their pre-bubble levels.[54]

Subprime lending, however, has not been cited as the only cause; many theories as to the cause of the actual housing crisis and subsequent recession have been advanced.[55] What led to the subprime financial shock? The theories of the leading causes have included government regulation, government deregulation, and securitization.[56]

b. Government Regulation

The Community Reinvestment Act of 1977 ("CRA")[57] has been cited by the political right as a primary cause of the housing crisis.[58] The CRA, a federal law, mandated that financial institutions had to reinvest deposit funds into the communities in which they operated.[59] "The CRA is based upon the underlying notion that institutions have a continuing and affirmative obligation to help meet the credit needs of the local

53 SHILLER, *supra* note 16, at 29.

54 *Id.*

55 ZANDI, *supra* note 7, at 29 ("Imagining how something as obscure as a subprime mortgage loan could have brought the global financial system to its knees and pushed the U.S. economy into recession might be hard."); *id.* at 4-5 ("Even after mortgage loans started going bad en masse, the confusing mix of federal and state agencies that made up the nation's regulatory structure had difficulty responding. After regulators finally began to speak up about subprime and the other types of mortgage loans that had spun out of control, such lending was already on its way to extinction. What regulators had to say was all but irrelevant. Yet even the combination of a flawed financial system, cash-flush global investors and lax regulators could not, by itself, have created the subprime financial shock. The essential final ingredient was hubris: a belief that the ordinary rules of economics and finance no longer applied."); Christopher A. Richardson, *An Economic View of the Housing Crisis*, 41 CONN. L. REV. 1133, 1137-38 (2009) (noting one cause of the mortgage crisis was "weak mortgage underwriting standards"); Mayer, *supra* note 39, at 7 ("While subprime lending alone may not easily explain the pattern of house price appreciation up to 2005, it surely was a strong contributing factor to the housing bubble that developed in many U.S. cities afterwards.").

56 *See* Michael Aleo & Pablo Svirsky, *Foreclosure Fallout: The Bank Industry's Attack On Disparate Impact Race Discrimination Claims Under the Fair Housing Act And the Equal Opportunity Act*, 18 B.U. PUB. INT. L.J. 1 (2008) (providing an insightful cause of the crisis); Ellen Harnick, *Entrepreneurship in the Global Economy: The Crisis in Housing and Housing Finance: What Caused it? What Didn't? What's Next?*, 31 W. NEW ENG. L. REV. 625, 626 (2009) (explaining what securitization is and theorizing that it has changed the traditional relationship between borrower and lender).

57 Community Reinvestment Act (CRA) of 1977, 12 U.S.C. § 2901 (1977).

58 Aleo, *supra* note 56, at 11-13.

59 Christopher A. Richardson, *The Community Reinvestment Act and the Economics of Regulatory Policy*, 29 FORDHAM URBAN L. J. 1607, 1607 (2002); Vern McKinley, *Community Reinvestment Act, Ensuring Credit Adequacy or Enforcing Credit Allocation?*, 17 REGULATION 25, 25 (1994), *available at* http://www.cato.org/pubs/regulation/regv17n4/vmck4-94.pdf.

communities in which they are chartered."[60]

Akin to the CRA are the Equal Credit Opportunity Act ("ECOA"), the Fair Housing Act ("FHAct"), and the Home Mortgage Disclosure Act ("HMDA"), which were all enacted to eliminate discrimination in the lending process.[61] "The [ECOA] prohibits discrimination in any aspect of a credit transaction. It applies to any extension of credit, including extensions of credit to small businesses, corporations, partnerships, and trusts."[62] The FHAct prohibits discrimination in every aspect of "residential real-estate related transactions," including but not limited to "making loans to buy, build, repair or improve a dwelling"; "purchasing real estate loans"; "selling, brokering, or appraising residential real estate"; or "selling or renting a dwelling."[63] The HMDA seeks to restrain "redlining," in which lenders avoid loaning money in certain communities due to their racial or ethnic composition.[64] "The CRA was enacted as a follow-up to the HMDA, in part in response to instances in which a poor white applicant had a significantly better chance of getting a mortgage loan than a wealthy black applicant."[65] The ECOA, FHAct, HMDA, and the CRA were enacted to ensure the availability of credit to all persons, irrespective of income or demographics.[66] As a result of the CRA, access to credit for low-income and minority borrowers has significantly increased.[67] The goals of these laws were to eradicate discrimination in the housing

60 McKinley, *supra* note 59, at 25; THE JOINT CENTER FOR HOUSING STUDIES, HARVARD UNIVERSITY, THE 25TH ANNIVERSARY OF *THE COMMUNITY REINVESTMENT ACT: ACCESS TO CAPITAL IN AN EVOLVING FINANCIAL SERVICES SYSTEM* (2002) [hereinafter ACCESS TO CAPITAL], *available at* http://www.jchs.harvard.edu/publications/governmentprograms/cra02-1.pdf (explaining that the CRA was designed so that banks would help communities); *see generally* REPORT BY THE U.S. COMMISSION ON CIVIL RIGHTS, 1961 UNITED STATES COMMISSION ON CIVIL RIGHTS REPORT (1961) [hereinafter U.S. Commission on Civil Rights Report]., *available at* http://www.law.umaryland.edu/marshall/usccr/documents/cr11961bk4.pdf.

61 McKinley, *supra* note 59, at 26; ACCESS TO CAPITAL, supra *note 60*.

62 FEDERAL DEPOSIT INSURANCE CORPORATION, COMPLIANCE EXAMINATION MANUAL 1.1 (2009), *available at* http://www.fdic.gov/regulations/compliance/manual/pdf/IV-1.1.pdf.

63 *Id.*

64 Allen J. Fishbein, *The Community Reinvestment Act After Fifteen Years: It Works, But Strengthened Federal Enforcement Is Needed*, 20 FORDHAM URB. L.J. 293, 293; Thomas B. Hatch & Richard R. Zabel, *Home Mortgage Disclosure Act Data Spawn Lawsuits by Minorities and Cities*, *in* FIRST FOCUS: THE SUBPRIME CRISIS 143 (2008).

65 McKinley, *supra* note 59, at 26; ACCESS TO CAPITAL, supra *note 60* ("The Act responded to the contention that savings and loans associations and banks were 'redlining' or systematically denying credit to lower-income and minority neighborhoods. CRA advocates argued that by restricting credit access based on neighborhood characteristics as opposed to the creditworthiness of individual loan applicants, the actions of depositories were exacerbating urban decline.").

66 McKinley, *supra* note 59, at 26.

67 Michael S. Barr, *Credit Where it Counts: The Community Reinvestment Act and Its Critics*, 80 N.Y.U. L. REV. 513 (2005).

market, to make affordable housing for a larger group of Americans, and in some respects to streamline the purchasing process. It appears, that in an effort to place blame, these admirable goals and the rationale behind them have been forgotten.

Moreover, in an attempt to place blame and find a cause for the housing crises, some politicians, economists, and others have determined that the CRA is the root cause of the current housing crisis. Specifically, these politicians, economists and others assert that in an effort to eradicate discrimination in mortgage lending, risky financial products were thrust upon low-income and minority borrowers, resulting in the housing crisis.[68] As part of the political game, many right wing analysts place blame on the CRA as an affirmative action – as opposed to an equal opportunity – program in which lenders were forced to increase lending to minority borrowers without assessing independent predatory lending practices imposed upon unsuspecting borrowers due to lenders' own business interests and poor judgment in decision-making.[69] In an effort to purportedly comply with the CRA, however, lenders engaged in affirmative discrimination by granting the majority of subprime home purchase loans to minorities.[70] This is reflected in the chart below:[71]

[68] *See* Stan Liebowtiz, *The Real Scandal - How Feds Invited the Mortgage Mess*, N.Y. POST, Feb. 5, 2008, *available at* http://www.nypost.com/p/news/opinion/opedcolumnists/the_real_scandal_Qjl08vDbysbe6LWDxcq03J (explaining that "the greatest scandal of the mortgage crisis is that it is a direct result of an intentional loosening of underwriting standards - done in the name of ending discrimination, despite warnings that it could lead to wide-scale defaults"); Ron Paul, *Commentary: Bailouts will lead to rough economic ride*, CNN, Sept. 23, 2008, *available at* http://www.cnn.com/2008/POLITICS/09/23/paul.bailout/index; Russell Roberts, *How Government Stoked the Mania*, WALL STREET J., Oct. 3, 2008, at A21; Aleo, *supra* note 56, at 11-13 (discussing the severe political rights' blame of the crisis on the CRA).

[69] Aleo, *supra* note 56, at 11; *see e.g.*, Ann Coulter, *They Gave Your Mortgage to a Less Qualified Minority* (2008), http://www.anncoulter.com/cgi-local/printer_friendly.cgi?article=275.

[70] Mayer, *supra* note 39, at 12 (noting, however, that often the mortgage brokers originating the subprime loans to minorities for approval and acceptance by the banks, as well as many of the appraisers, were often minorities as well).

[71] Richard Marisco & Jane Yoo, *Racial Disparities in Subprime Home Mortgage Lending in New York City: Meaning and Implications*, 53 N.Y. L. SCH. L. REV. 1011, 1020 (2008-09).

Lender	African - Americans	Ratio: African Americans to Whites	Latinos	Ratio: Latinos to Whites	Whites
JP Morgan Chase	15.6%	5.6	12.4%	4.5	2.8%
Citimortgage	1.7%	5.7	1.6%	4.9	0.3%
Wells Fargo	23.0%	17.7	10.9%	8.4	1.3%
HSBC	2.6%	6.4	2.3%	5.7	0.4%
Countrywide	33.7%	3.3	18.4%	1.8	10.8%
Greenpoint	19.7%	3.9	14.3%	2.9	5.0%

Thus, this chart shows that for all major lenders African-Americans and Latinos were much more likely to receive a subprime loan than whites. For example, African-Americans received a subprime loan 17.7 times and Latinos 8.4 times more than whites from Wells Fargo.[72] So lenders "gamed" the CRA for their benefit by imposing risky financial products on their customers and minorities much more often than whites, but as discussed below whites – even wealthy whites – did not escape becoming victims of these sub-prime loans.

Significant evidence shows that indeed the CRA was not that cause of the housing crisis. To begin, the CRA was not responsible because it did not regulate most of the significant subprime lenders.[73] Furthermore,

> studies found that lending to lower-income individuals and communities has been nearly as profitable and performed similarly to other types of lending done by CRA-covered institutions. Thus, a fair reading of the statute and regulations and the long-term evidence shows that the CRA has not pushed banks into extending loans that perform out of line

72 *Id.*

73 *See* Luci Ellis, *The Housing Meltdown: Why Did it Happen in the United States?* 5, fn.6 (Bank for Int'l Settlements, Working Paper No. 259, Sept. 2008), *available at* http://www.bis.org/publ/work 259.pdf?noframes=1; Governor Randall S. Kroszner, Speech at the Confronting Concentrated Poverty Policy Forum: The Community Reinvestment Act and the Recent Mortgage Crisis (Dec. 3, 2008), *available at* http://www.federalreserve.gov/newsevents/speech/kroszner20081203a.htm (claiming that the CRA was in no way causally linked to the foreclosure crisis); Sheila Bair, Remarks to The New America Foundation Conference: Did Low-income Homeownership Go Too Far? (Dec. 17, 2008), *available at* http://www.fdic.gov/news/news/speeches/archives/2008/chairman/spdec1708.html ("CRA as a scapegoat.").

with their traditional businesses.[74]

Also, lenders imposed subprime loans not only on the borrowers with weak credit histories, but also borrowers with strong credit histories; lenders pushed these loans on the minority communities, as well as wealthy non-minorities.[75] Additionally, economists "analyzed mortgage-related data to assess such arguments and found no empirical evidence to support the claim that the CRA was a major contributor to the subprime crisis."[76] Also, "the subprime crisis did not begin until a quarter century after the enactment of the CRA, and Congress weakened the CRA regulations in late 2004 to exclude small and mid-sized banks from its more stringent requirements - yet the subprime market continued to grow."[77]

Finally, one economist concluded: "The proposition that the Community Reinvestment Act caused all the bad stuff, because government forced helpless bankers into lending to Those People, has been refuted up, down, and sideways. The vast bulk of subprime lending came from institutions not subject to the CRA."[78] Nevertheless, some continue to believe that it is likely that the CRA may have played some minor role in the economic crisis.[79] This conclusion, however, seems more politically charged than

74 Federal Reserve Bank of Philadelphia, *No Evidence of CRA Role in the Crisis* (2010), *available at*, http://www.phil.frb.org/publications/annual-report/2008/no-evidence.cfm [hereinafter *No Evidence of CRA Role*] (quoting Kroszner, *supra* note 73).

75 Rick Brooks & Ruth Simon, *Subprime Debacle Traps Even Very Credit-Worthy*, WALL STREET J., Dec. 3, 2007, available at http://online.wsj.com/article/SB119662974358911035.html; Bernard Condon, *Mortgage Crisis Shuffles Towards Fancier Neighborhoods*, FORBES, Oct. 7, 2009, *available at* http://www.forbes.com/2009/10/07/real-estate-mortgages-foreclosures-personal-finance-crisis.html ("Many of the well-off took out "option-ARM" or "Alt-A" loans. The attraction: Little or no proof of income to qualify for the loans and, often, artificially low payments for five years after they were granted. Problem is, these loans demand higher catch-up payments in later years so even if rates fall, monthly bills will rise.").

76 *See No Evidence of CRA Role*, *supra* note 73; *see also* Center for Responsible Lending, *supra* note 50, at 2, http://www.responsiblelending.org/mortgage-lending/tools-resources/Quotes-What-Caused-Crisis.pdf (quoting John Dugan, Comptroller of Currency: "CRA [the Community Reinvestment Act, a longstanding program for encouraging more lending in minority neighborhoods] is not the culprit behind the subprime mortgage lending abuses, or the broader credit quality issues in the marketplace.").

77 Aleo, *supra* note 56, at 14 (citations omitted).

78 Paul Krugman, *The Conscience of a Liberal: Armey of Ignorance*, N.Y. TIMES, http://krugman.blogs.nytimes.com/2009/11/10/armey-of-ignorance/ (Nov. 10, 2009) (opining also that commercial real estate lending to rich white developers is in much worse shape than subprime home lending); *see* Mayer, *supra* note 39, at 7 (arguing that subprime lending and securitization or any other U.S. specific factor cannot fully explain the housing market boom globally for commercial real estate).

79 *See* Hardaway, *supra* note 49, 36 ("Indeed, there is now little doubt that its progeny in the form of regulations promulgated in the mid 1990s with the purpose of putting teeth into the CRA by setting quotas for mortgage lending to distressed communities and threatening sanctions for banks who did not meet them, played at least some role in the collapse, through the extent of its role remains fiercely debated."); *but see* Randall Kroszner, *Lending to Poor Didn't Spur Crisis*, REUTERS, Dec. 3, 2008, *available at* http://www.reuters.com/article/idUSN0332633420081203 ("[T]he very small share of all higher-priced loan originations that can reasonably be attributed to the CRA makes it hard to imagine

accurate.

c. Government Deregulation

As the political right blames regulation – the CRA as a misguided piece of affirmative action legislation – for the current housing crisis, the political left blames deregulation of the Reagan years for the crisis. In the 1980s, Congress enacted two landmark pieces of legislation that are thought to have played a role in the current economic crisis – the 1980 Depository Institutions Deregulation and Monetary Control Act ("DIDMCA")[80] and the Alternative Mortgage Transactions Parity Act of 1982 ("AMTP"), which is part of the Garn-St. Germain Depository Institutions Act.[81]

The DIDMCA abolished all usury caps on first lien residential mortgages, including state usury caps.[82] Thus, opening the floodgates for loans to riskier borrowers and continuing to allow more low-to-moderate income individuals home ownership.[83] The AMTPA lifted the ban on conventional-only, fixed rate loans to riskier loan products.[84] The types of loans that the AMTPA allowed were: adjustable-rate mortgages,[85] balloon-payment mortgages,[86] interest-only mortgages,[87] and the option-ARM.[88]

how this law could have contributed in any meaningful way to the current subprime crisis.").

80 Depository Institution Deregulation and Monetary Control Act of 1980, Pub. L. No. 96-221, 94 Stat. 132 (1980) (codified as amended in various sections of title 12 of the U.S. Code).

81 McCoy, *supra* note 7, at 501; Timothy Canova, *Financial Market Failure As a Crisis in the Rule of Law: From Market Fundamentalism to a New Keynesian Regulatory Model*, 3 HARV. L. & POL'Y REV. 369, 376-77 (2009).

82 *See* 12 U.S.C. § 1735f-7a(a)(1) ("The provisions of the constitution or the laws of any State expressly limiting the rate or amount of interest, discount points, finance charges, or other charges which may be charged, taken, received, or reserved shall not apply to any loan, mortgage, credit sale, or advance . . . .").

83 SCHECHTER, *supra* note 3, at 6 ("The subprime loan was crafted for this [weak credit poor minority] community and promoted as a reform, a positive way for minorities to become part of the American Dream of homeownership for all").

84 ZANDI, *supra* note 7, at 35 ("The fixed-rate mortgage loan, in which monthly mortgage payments never change, no matter what happens to interest rates or financial markets"); Howard Mulligan, *As Lawmakers Tackle the Subprime Crisis, Professional Vigilance is a Must*, in FIRST FOCUS: THE SUBPRIME CRISIS, 79 (2008).

85 ZANDI, *supra* note 7, at 16 ("ARMs allowed for low monthly payments, at least for a while."); Harnick, *supra* note 56, at 628 (defining hybrid ARMs as risky loans that were also known as the "2/28" or "3/27" because the interest rate was fixed for the first two or three years out of a 28 or 27 year term, and at the end of the fixed period (two or three years) for these loans, the interest rates would increase dramatically); Yuliya Demyanyk & Otto Van Hemert, *Understanding the Subprime Mortgage Crisis*, REV. FIN. STUDIES 8 (2009), http://rfs.oxfordjournals.org/content/early/2009/05/04/rfs.hhp033 .full.pdf (defining hybrid mortgages as having a "fixed rate for an initial period (typically 2 or 3 years) and then the rate resets to a reference rate (often the 6-month LIBOR) plus a margin").

86 Demyanyk, *supra* note 85 (defining a balloon mortgage as one that "does not fully amortize over the term of the loan and therefore requires a large final (balloon) payment").

87 ZANDI, *supra* note 7, at 38 ("Interest-only ARMs allow borrowers to forgo principal payments"); FIRST FOCUS: THE SUBPRIME CRISIS 77 (2008).

These are the kinds of loans that are causing borrowers to default on their mortgages because the initial loan payments significantly increase at some point during the initial years of the loans. These two landmark bills created the deregulatory environment in which these risky loans flourished.[89] "[Subprime loans] were made possible by deregulation lobbied for by financial institutions, credit card companies, and homebuilders, the industries most likely to benefit."[90] Thus, a subprime market was born.

America's housing boom occurred during the years of 2000 through 2006 at which time it began to decline.[91] During this time, obtaining a home was relatively easy. In fact, obtaining a home beyond what a borrower could properly afford was easy and became the norm. The demand for houses increased during this boom, and many people made money at all levels from the sellers to the middle persons to the lenders on Wall Street. As the demand for housing increased, it pushed housing prices to a higher level.[92] Adjustable rate mortgages ("ARM") comprised the lion's share of the subprime lending market. Indeed, 80% of subprime loans were adjustable rate mortgages.[93] Often, the lender assessed the non-creditworthy borrower for a loan as if the ARM was for the entire 30 year mortgage rather than the two or three year "ARM", so when the ARM adjusted, the borrower was unable to continue making the increased monthly payment. For example, during the boom, the initial 8% interest rate would increase two or three years later to 10% or more.[94] When the interest adjusted the borrowers defaulted, and the borrowers who thought they could or tried to sell their home to obtain a release from the subprime loan could not do so because the home values had decreased.[95] In addition,

[88] ZANDI, *supra* note 7, at 38 ("Option ARMs give borrowers a choice; they may make standard interest and principal payments, pay only the interest, or pay only a minimum amount that doesn't even cover the interest due. Interest not paid is added back into the loan principal. This is known as negative amortization"); Mulligan, *supra* note 84, at 77.

[89] *See* Cassandra Havard, *Democratizing Credit: Examining the Structural Inequities of Subprime Lending*, 56 SYRACUSE L. REV. 233, 234 (2006); Todd J. Zywicki & Joseph D. Adamson, *The Law and Economics of Subprime Lending*, 80 U. COLO. L. REV. 1, 6 (2009).

[90] SCHECHTER, *supra* note 3, at 5.

[91] *Will Subprime Mess Ripple Through Economy*? MSNBC-Business, March 13, 2007, http://www.msnbc.msn.com/id/17584725.

[92] Stock Market Investors, *Subprime Mortgage Crisis Explained*, http://www.stock-market-investors.com/stock-investment-risk/the-subprime-mortgage-crisis-explained.html (last visited Feb. 22, 2011).

[93] U.S. Senate Committee on Banking, Housing, & Urban Affairs, *Dodd: Create, Sustain, Preserve, and Protect the American Dream of Home Ownership*, February 7, 2007, http://banking.senate.gov/public/index.cfm?FuseAction=Newsroom.PressReleases&ContentRecord_id=e2e529c0-29ee-43db-a314-ecafb3bdee32&Region_id=&Issue_id=.

[94] Harnick, *supra* note 56, at 628.

[95] *President Bush's Speech to the Nation on the Economic Crisis*, N.Y. TIMES, Sept. 24, 2008, *available at* http://www.nytimes.com/2008/09/24/business/economy/24textbush.html?_r=3&page

refinancing opportunities were curtailed because the housing market was declining.[96] These borrowers could not afford the loans that the lenders offered them, and these borrowers often did not fully understand what they were entering into when they accepted ARM mortgages.[97] To add to this, borrowers were encouraged to refinance and "pull-out" the equity in their homes. This resulted from the belief and expectation that real estate always appreciates. Therefore, a borrower who purchased a home, that he really could not afford, was soon bombarded with opportunities to refinance his home because it had certainly appreciated in the few years since the initial purchase. The refinance now placed the borrower in an even more precarious situation because he now owed even more on a house that was inflated in value when it was initially purchased. This merry-go-round of purchase, refinance, purchase, provided the basis for unscrupulous mortgage companies and banks to continue to flourish.

After this housing boom began to decline in 2007, roughly $1.3 trillion in subprime mortgages were outstanding.[98] During this time, home ownership rose about 5% from approximately 64% in 1994 to 69.2 in 2004.[99]

The housing boom years were golden for many. New homeowners were obtaining loans that they ultimately could not afford, then they were offered home equity lines on top of the first mortgage, and consumers were saving less money.[100] Average household debt rose to $14 trillion in 2008, which reflected a significant increase from $680 billion in 1974, roughly 35 years earlier.[101] In addition, the average household income did not increase in comparison to the rising household debt and housing prices.[102] Unable to

wanted=1&oref=slogin.

96 *Id.*

97 Harnick, *supra* note 56, at 630; Gretchen Morgenson, *Illinois to Sue Countrywide*, N.Y. Times, June 25, 2008, *available at* http://www.nytimes.com/2008/06/25/business/25mortgage.html?_r=1&emc =eta1.

98 *Will Subprime Mess Ripple Through Economy?*, *supra* note 91.

99 Robert R. Callis & Linda B. Cavanaugh, *Census Bureau Reports On Residential Vacancies And Homeownership*, U.S. CENSUS BUREAU NEWS (2007), *available at* http://www.census.gov/hhes/www/housing/hvs/qtr307/q307press.pdf.

100 Tim Iacono, *Home Equity Extraction: The Real Cost of 'Free Cash'* (Apr. 25, 2007), http://seekingalpha.com/article/33336-home-equity-extraction-the-real-cost-of-free-cash (noting that "home sales, home equity loans, and cash-out refinancing – all [...] contribute to what is appropriately (and ironically) termed "free cash").

101 Fareed Zakaria, *There Is a Silver Lining*, NEWSWEEK, Oct. 11, 2008, *available at* http://www.newsweek.com/2008/10/10/there-is-a-silver-lining.html (explaining that "during 2008, the typical USA household owned 13 credit cards, with 40% of households carrying a balance, up from 6% in 1970").

102 Stock Market Investors, *supra* note 92.

refinance and pay a steep prepayment penalty,[103] unable to afford the increased mortgage, and saddled with new and higher debt, borrowers were trapped and began to default. This housing crisis was only a matter of time because the lax regulations and the risky loan products created a housing mess.[104] It is true that Americans borrowed more than they could realistically pay for homes, but American corporations also lent money using unstable and risky financial products.[105] As early as 2006, there was a noticeable increase in the number of homeowners who began to default and ended up in foreclosure as a result of their inability to make mortgage payments.[106] It is anticipated that within the next five years, one out of every six homeowners will end up in foreclosure unless homeowners in distress can restructure their current home loan.[107] "[D]eregulation in effect gave the industry — whose deposits were federally insured — a license to gamble with taxpayers' money, at best, or simply to loot it, at worst. By the time the government closed the books on the affair, taxpayers had lost $130 billion, back when that was a lot of money."[108] Some would argue that deregulation cleared the way for a plundering of America.[109]

d. Securitization

Securitization, a Wall Street innovation,[110] is another leading cause—or perhaps more appropriately an exacerbation—of the foreclosure crisis.[111] "Fundamentally, loans are either financed directly by financial institutions such as commercial banks and thrift institutions, or are repackaged as bonds (that is, securitized) and sold to investors, who keep or trade them in

103 *See* John Farris & Christopher A. Richardson, *The Geography of Subprime Mortgage Prepayment Penalty Patterns*, 15 HOUSING POL'Y DEBATE 687, 689 (2004).

104 Stock Market Investors, *supra* note 92.

105 Harnick, *supra* note 56, at 625.

106 *Foreclosures*, N.Y TIMES, May 6, 2010, *available at* http://topics.nytimes.com/top/reference/timestopics/subjects/f/foreclosures/index.html?scp=3&sq=housing%20boom%20and%20subprime&st=cse.

107 Harnick, *supra* note 56, at 625-26.

108 Paul Krugman, *Reagan Did It*, N.Y. TIMES, May 31, 2009, available at http://www.nytimes.com/2009/06/01/opinion/01krugman.html; *but see* Bill Fleckenstein, *Blame Reagan for Our Financial Mess*, MSN MONEY, June 8, 2009, *available at* http://articles.moneycentral.msn.com/Investing/ContrarianChronicles/blame-reagan-for-our-financial-mess.aspx.

109 *See generally* SCHECHTER, *supra* note 3.

110 Ben Steverman & David Bogoslaw, *The Financial Crisis Blame Game*, BUSINESSWEEK, Oct. 18, 2008, *available at* http://www.businessweek.com/investor/content/oct2008/pi20081017_950382.htm.

111 Krimminger, *supra* note 49 at, 263 ("Securitization did not create the problem; poor underwriting did. Securitization has contributed to unprecedented levels of homeownership in this country by expanding the availability of credit to lower-income Americans and the liquidity of the credit markets.").

global financial markets. The overwhelming majority of subprime loans have been securitized."[112]

At the start of the twenty-first century, the traditional manner of buying a home changed. Mortgage bankers came on the scene – these mortgage "bankers" are not banks, but instead they are "companies that raise funds they lend, not through bank deposits, but by borrowing money from investment banks or commercials banks, and repaying that money by selling to investors the right to share in the proceeds of the mortgage payments received from borrowers," which process is known as "securitization."[113] This change was significant because traditionally mortgage lenders had a long-term stake in the mortgage loan until the borrower repaid it, but under securitization, the mortgage lender that originated the loan and defined the terms no longer had a stake in the success or failure of the borrower repaying the loan.[114] These securitizations were risky and because the originating lender had no stake in the loan, the lenders increasingly became careless in their lending practices.[115] Securitized mortgages contributed to poor underwriting practices, in that neither the loan originators nor the investors were concerned about whether the loans they originated could be repaid by the borrowers, and borrowers were systematically put into loans that they could not repay.[116] Securitizations ultimately led to "poor quality loans made by originators and brokers with incentives that some of them to lend to anyone who would sign on the dotted line."[117] It is said that Wall Street created all of the subprime mortgage-backed securities.[118]

> Large mortgage finance companies and banks made big bucks on sub-prime loans. Last year, 10 lenders – Countrywide, New

112 ZANDI, *supra* note 7, at 41; SCHECHTER, *supra* note 3, at 7 ("The percentage of subprime mortgage securitized rose rapidly after 2001, reaching a peak value of more than 81 percent in 2005."); Dorit Samuel, *The Subprime Mortgage Crisis*, 2 ALB. GOV'T L. REV. 217, 220 (2009), *available at* http://www.albanygovernmentlawreview.org/articles/2/1/Samuel.pdf ("The bubble that burst began to inflate with mortgage loans made by an array of financial institutions to high risk home buyers; these loans were consolidated into securities packages issued by financial institutions that were then repackaged and sold to other financial institutions and to other investors.").

113 Harnick, *supra* note 56, at 626.

114 *Id.*, at 627; SCHECHTER, *supra* note 3, at 9.

115 Harnick, *supra* note 56, at 627 (explaining that a CEO of one mortgage lender said "the market is paying me to do a no-income-verification loan more than it is paying me to do the full documentation loans...What would you do?"); Hull, *supra* note 37, at 23 ("[T]he question was not 'Is this a credit we want to assume?' Instead it was 'Is this a mortgage we can make money on by selling it to someone else?'").

116 Mayer, *supra* note 39, at 3-4.

117 *Id.* at 30.

118 Harnick, *supra* note 56, at 634 (citations omitted).

> Century, Option One, Fremont, Washington Mutual, First Franklin, RFC, Lehman Brothers, WMC Mortgage, and Ameriquest – accounted for 59 percent of all sub-prime loans, totaling $284 billion.
>
> Wall Street investment firms set up special investment units, bought the sub-prime mortgages from the lenders, bundled them into "mortgage-backed securities," and for a fat fee sold them to wealthy investors around the world.[119]

Securitization continued for years and was highly profitable for lenders and investors, "securitization facilitated a large transfer of wealth to lenders, Wall Street, and global investors, from the most vulnerable segment of the American middle class [Main Street], who are now losing their homes to boot."[120] The most tragic aspect is that most subprime loan borrowers qualified for prime loans with far better terms.[121] Even those borrowers who did not qualify for a prime loan, did qualify for safer loans with far better terms than they were given, such as a thirty-year fixed-rate loan which would have provided a stable mortgage payment.[122] Thus, the fraud perpetrated on the borrowers within these subprime loans was due to the lenders choosing to offer substandard products to their borrowers because of greed.[123]

When federal government regulators intervened in 2007 and proposed that lenders determine whether borrowers would be able to afford their loans after the ARMs ended, lenders resisted.[124] Noteworthy, Countrywide protested in writing and essentially admitted that roughly 60 percent of its borrowers who received subprime hybrid ARM loans in the end of 2006 would not have met the lending qualifications.[125] In fall 2010, Countrywide settled several class action lawsuits in the amount of $600 million that alleged that "Countrywide concealed mounting risks as it loosened its standards for loans."[126] Specifically, "[t]he FTC says Countrywide charged excessive fees for services such as property inspections, inflated

119 SCHECHTER, *supra* note 3, at 9.

120 Harnick, *supra* note 56, at 628.

121 *Id.* at 629.

122 *Id.*

123 SCHECHTER, *supra* note 3, at 23 (quoting millionaire Michael Blomquist who alleges that real estate financiers bilked him out of his money: "Our current credit and housing crisis was not created from low interest rates or 'laxed' guidelines. This crisis was created by unconscionable greed, breaches of fiduciary duties, lack of regulation, embezzlement and fraud.").

124 Harnick, *supra* note 56, at 630.

125 *Id.*, at 631; SCHECHTER, *supra* note 3, at 12.

126 *$600 Million Countrywide Settlement*, N.Y. TIMES, Aug. 3, 2010, at B5, *available at* http://www.nytimes.com/2010/08/03/business/03countrywide.html.

the amount owed when borrowers filed for bankruptcy protection, and didn't tell people when new fees or charges were being added to their loans."[127] This is the largest settlement yet from the subprime mortgage crisis.[128] This settlement followed a $108 million settlement from Bank of America, which has since purchased Countrywide, that was to refund customers who had mortgages from Countrywide.[129] Citibank, Goldman Sachs, AIG, and other Wall Street giants have paid huge settlements for fraudulent conduct related to the subprime mortgage crisis.[130] Thus, it is clear that Wall Street knew the fraudulent games it was playing with Main Street's money, but Wall Street followed greed. Wall Street profited handsomely at the expense of Main Street.

Curiously, Main Street is not the population who comprises the biggest defaulters in this housing crisis. While the crisis appears to have begun in the lower income communities, it moved to the middle class neighborhoods, and now includes the wealthy. The media blitz has Americans believing that poor people caused this subprime crisis, but not one homeowner approved their own loan or appraised their own property; the lenders allowed no documentation loans ("liar loans") because they did not care.[131] Main Street is being blamed for this crisis – specifically, non-creditworthy borrowers have been deemed irresponsible,[132] but in reality the biggest defaulters are the wealthy.[133] Whereas one in 12 of Main Street borrowers are in default, a study shows that one in seven of America's wealthy are in default.[134]

127 Michelle Singletary, *FTC Wins Countrywide Settlement*, WASH. POST, June 10, 2010, *available at* http://www.washingtonpost.com/wp-dyn/content/article/2010/06/09/AR2010060905931.html.

128 *$600 Million Countrywide Settlement, supra* note 126, at B5.

129 Singletary, *supra* note 127.

130 Robert A. Mintz, *Don't Bank on Subprime Indictments Anytime Soon*, HUFFINGTON POST, Aug., 16, 2010, http://www.huffingtonpost.com/robert-a-mintz/dont-bank-on-subprimeind_b_683869.html.

131 SCHECHTER, *supra* note 3, at 7 (reporting that no documentation loans – loans in which the borrower is unable to verify employment, income or other credit related information – increased from 28 percent to more than 50 percent as housing sales boomed).

132 Harnick, *supra* note 56, at 634; SCHECHTER, *supra* note 3, at xxi-xxii (reporting that Hedge Fund Manager John Devaney, CEO of United Capital Markets, was known for calling borrowers "idiots" for entering into loans that he and his colleagues pedaled).

133 David Streitfeld, *Biggest Defaulters on Mortgages are the Rich*, N.Y. TIMES, July 8, 2010, at A1, *available at* http://www.nytimes.com/2010/07/09/business/economy/09rich.html?pagewanted=1&_r=1 ("Whether it is their residence, a second home or a house bought as an investment, the rich have stopped paying the mortgage at a rate that greatly exceeds the rest of the population.").

134 *Id.*

II. MAIN STREET & MORTGAGE MORALITY

Now, Main Street, that is, America's working class and small business owners, is saddled with real estate that is not worth the money owed, and the current creditors who harass them for payment are not the same ones who originated the loan or established any relationship with Main Street. Some homeowners just "walked away"[135] from their homes when the crash hit, but this was not the most common scenario; most homeowners wanted to work harder to stay current on the mortgage and stay in their home, even if it was "underwater."[136] The lenders knew that walking away for many homeowners was probably the best thing they could do for themselves. Indeed "[O]n Freddie Mac's Web site, the company's executive vice president, Don Bisenius, acknowledged that walking away "might well be a good decision for certain borrowers."[137] Yet, lenders said that homeowners who walk away are "trashing their communities."[138] Various property-saving programs have been offered by the government, but they have not had much success.[139]

Main Street is perceived as one of the chief culprits of the housing crisis.[140] "It is now frequently asserted that the housing crisis was caused by borrowers who took on mortgages when they never should have owned homes in the first place."[141] As was said with Tulipmania —that "those doing the investing were the wrong people, those who, because of their low social station, should not have been allowed to submit to the temptation of easy money,"[142] so it is said with the subprime crisis – poorer people

[135] Eric Weiner, *Why Not Just Walk Away from a Home?*, February 13, 2008, http://www.npr.org/templates/story/story.php?storyId=18958049 (defining "walking away" as giving the mortgage and the house back to the bank).

[136] *Id.*

[137] Streitfeld, *supra* note 133, at A1.

[138] *See id.* (quoting Freddie Mac's company executive); *see also* News Release, Fannie Mae, Fannie Mae Increases Penalties for Borrowers Who Walk Away: Seven Year Lockout Policy for Strategic Defaulters (June 23, 2010), http://www.fanniemae.com/newsreleases/2010/5071.jhtml (quoting Terence Edwards, Fannie Mae executive vice president for credit portfolio management: "Walking away from a mortgage is bad for borrowers and bad for communities and our approach is meant to deter the disturbing trend toward strategic defaulting.").

[139] *Double-Dip Drama*, THE ECONOMIST, June 24, 2010, at 35, *available at* http://www.economist.com/node/16438759; *see also* Lita Epstein, *Underwater Borrowers Get a Lifeline on Sept. 7*, http://realestate.aol.com/article/experian/_a/underwater-borrowers-get-a-lifeline-on-september-7/201009020001 (reporting a new government program that starts September 7, 2010 and ends December 12, 2012 in which a borrower may be able to obtain a fixed-rate FHA loan with a principal reduction of ten percent of the unpaid balance of the first mortgage, but the borrower's lien holders must consent to for the borrower to participate in the program, called the FHA Short Refinance Option).

[140] Harnick, *supra* note 56, at 633.

[141] *Id.*

[142] GOLDGAR, *supra* note 17, at 5.

should not have pursued the American dream of home ownership. Blaming the "irresponsible" borrower who should never have bought a home in the first place "allows justification for a harshness toward the individuals concerned."[143] Yet, this harshness is misplaced as most subprime borrowers qualified for better (prime[144] or a less costly thirty year loan), but "these borrowers were taken advantage of by mortgage brokers and lenders who were happy to pass the risks onto far-flung investors."[145] Mortgage lenders created cultures that "encouraged [their] sales personnel to engage in deceptive and fraudulent conduct."[146] Financial institutions targeted the poor and working class who wanted to improve their lives and own new homes.[147]

Evidence flies in the face of the assertion that subprime loan borrowers obtained risky loans to obtain mansions because the average subprime loan was $205,700 and this included the high-priced California market,[148] and "the overwhelming majority of subprime mortgages made from 1998 through 2006 went to borrowers who already owned their own homes", thus "subprime lending actually resulted in a net *reduction* in homeownership."[149] Furthermore, subprime products offered to subprime borrowers were intentionally very complicated and thus there was great room for misrepresentation and misunderstanding.[150] As a result, there was excessive predatory lending[151] and excessive predatory borrowing.[152] Predatory loans typically include excessive fees, abusive prepayment

143 Harnick, *supra* note 56, at 634.

144 *See* ZANDI, *supra* note 7, at 31 (defining a prime borrower as "someone lenders are eager to do business with because the person has a good history of debt repayment."); *see also* Linda Finely & Frederick Salvo, *Consumers Were the Real Victims of Georgia's Predatory Law, in* FIRST FOCUS: THE SUBPRIME CRISIS 171, 171 (2008).

145 Harnick, *supra* note 56, at 634.

146 Robert Ridge & Lauren D. Rushak, *Identifying the Categories of Disputes Emerging from the Subprime Meltdown, in* FIRST FOCUS: THE SUBPRIME CRISIS 1, 12-13 (2008) (quoting New York Attorney General Andrew Cuomo who stated that Ameriquest had created such an environment; noting that Washington Mutual used appraisers who would inflate the home values).

147 SCHECHTER, *supra* note 3, at 77.

148 Harnick, *supra* note 56, at 634 (citing data collected from the Home Mortgage Disclosure Act for loans made in 2006).

149 *Id.* (citing Center for Responsible Lending, http://www.responsiblelending.org/mortgage-lending/research-analysis/Net-Drain-in-Home-Ownership).

150 ASHCRAFT & SCHUERMANN, *supra* note 42, at 32; SCHECHTER, *supra* note 3, at 20 (reporting that subprime loans were carefully engineered and designed to fail).

151 ASHCRAFT & SCHUERMANN, *supra* note 42, at 101 (defining predatory lending as having at least one of these: "[m]aking unaffordable loans based on the assets of the borrower rather than on the borrower's ability to repay an obligation; [i]nducing a borrower to refinance a loan reportedly in order to charge high points and fees each time the loan is refinanced ("loan flipping"); or [e]ngaging in fraud or deception to conceal the true nature of the loan obligation, or ancillary products, from an unsuspecting or unsophisticated borrower").

152 *Id.* at 21 (explaining implications of predatory lending).

penalties, kickbacks to brokers, loan flipping, unnecessary products, mandatory arbitration, and offers of subprime products when borrowers qualified for prime products.[153]

In the early 1800's Thomas Jefferson remarked: "I believe that banking institutions are more dangerous to our liberties than standing armies."[154] The blame game has fallen back on Main Street, when the real culprit is Wall Street – Wall Street "trashed [American] communities." Wall Street has acknowledged that the easy money was too hard to pass up, and the well-being of the borrowers was ignored. Lenders and brokers intentionally deceived borrowers by offering complex products, knowing the borrowers did not understand the terms and that the borrower could not repay the loan.

> The truth is that many of us in the industry were deeply distressed by the growing practice of pushing high risk loans on borrowers who had no reasonable expectation of being able to repay the mortgage. Disclosures were often less than adequate, and faced with a bewildering array of loan terms, borrowers tended to trust their mortgage banker or broker. The broken trust that resulted has damaged borrower confidence in the mortgage industry. I liken the situation to that of a doctor and patient dealing with a medical procedure. The patient bears some reasonable risk. But they don't bear the risk of malpractice by the doctor. In our industry, we have frankly seen too much mortgage malpractice. (*Testimony of Scott Stern, CEO of Lenders One before the Senate Banking Committee Washington, D.C. April 10, 2008*).[155]

> During the lending boom, the industry developed products that were "extremely risky that were pushed by everybody up and down the food chain," Mr. Robbins said. "We forgot about our customers, and making money and our commission checks were more important," he said. (*Kate Berry, "Wachovia Alum Has Tips for an Industry Rebound," American Banker (September 15,2008) quoting John Robbins, long-time industry executive and former chairman of the Mortgage Bankers Association*).[156]

153 *Id.* at 104 (citing the Center for Responsible Lending, *supra* note 50).

154 Laurence Booth, *Subprime, Market Meltdown, and Learning from the Past*, *in* THE FINANCE CRISIS AND RESCUE 35 (2008) (quoting Thomas Jefferson in The Debate over the Re-charter of The Bank Bill (1809)).

155 Center for Responsible Lending, *supra* note 50.

156 *Id.*

Now, Wall Street is withdrawing the initial support offered to help borrowers restructure the subprime loans; the economy has not bounced back; and foreclosures are increasing.[157] Main Street advisors say "walk away" from the obligations made with Wall Street and others that originated these loans,[158] and Wall Street and others in America say that is irresponsible and immoral. Main Street, they say, must honor its mortgage loan obligations because that is what those Americans committed to do when they entered into the loan.[159]

What Wall Street did to Main Street showed America that: "This is business not personal."[160] "Lending to American homebuyers had been one of the least risky and most profitable businesses a bank could engage in for nearly a century."[161] But Wall Street got greedier than usual.[162] Wall Street intentionally defrauded Main Street because Wall Street's goal was to make money at any cost, even at the cost of America's working middle class.[163] This crisis has essentially eviscerated the middle class, which for so long had increased their economic status through home ownership.[164]

157 *See* Allyson Gold, *Interpreting the Protecting Tenants at Foreclosure Act of 2009*, 19 J. AFF. HOUSING & COM. DEV. L. 205, 205 (2010).

158 *See generally* White, *supra* note 7 (discussing how many homeowners are abandoning their mortgage payments); Streitfeld, *supra* note 133 (explaining how in certain instances "walking away" might be a good decision for some borrowers).

159 Streitfeld, *supra* note 133 ("Fannie Mae and Freddie Mac, two quasi-governmental mortgage finance companies that own most of the mortgages in America with a value of less than $500,000, are alternately pleading with distressed homeowners not to be bad citizens and brandishing a stick at them... Freddie Mac's Web site, the company's executive vice president, Don Bisenius, acknowledged that walking away "might well be a good decision for certain borrowers" but argues that those who do it are trashing their communities.").

160 Memorable Quotes for the Godfather, http://www.imdb.com/title/tt0068646/quotes (last visited Feb. 10, 2011).

161 ZANDI, *supra* note 7, at 1.

162 SCHECHTER, *supra* note 3, at xxiii (reporting that populist Jim Hightower said: "At its core, this is a classically simple story of banker greed and outright sleaze. And the astonishing part is that nearly all of the rank injustice perpetrated by today's money changers is considered legal and is practiced by supposedly reputable financial firms"); SCHECHTER, *supra* note 3, at 160 (reporting economic advisor Carly Fiorina: "there was a situation where there was greed on Wall Street, there was a lack of transparency around a new set of financial instruments . . . there were a whole new set of financial players who were less regulated then banks, and all that together created a situation, which now is rippling through the economy").

163 *Id.* at 38 (reporting that investor Warren Buffet said: "Wall Street is going to go where the money is and not worry about consequences").

164 *See* SCHECHTER, *supra* note 3, at 4 (reporting the Senate's Joint Economic Committee's findings: "Approximately $71 billion in housing wealth will be directly destroyed through the process of foreclosures. More than $32 billion in housing wealth will be indirectly destroyed by the spillover effect of foreclosures, which reduce the value of neighboring properties. States and local governments will lose more than $917 million in property tax revenue as a result of the destruction of housing wealth caused by subprime foreclosures"); *see also* David Streitfeld, *Housing Fades as a Means to Build Wealth, Analysts Say*, N.Y. TIMES, Aug. 22, 2010, at A1, *available at* http://www.nytimes.com/2010/08/23/business/economy/23decline.html (reporting that "many real estate experts now believe that home ownership will never again yield rewards like those enjoyed in the second half of the 20th century, when

"Wall Street pushed and pulled for more predatory practices. The people who had the most were deeply involved in ripping off the people who had the least."[165]

Wall Street would like Americans to believe that it is helping to fix the crisis it caused by offering various loan modification and short sale programs. But what is Wall Street really doing? Wall Street is operating in the black again,[166] but Main Street is still suffering. So, what is Main Street doing about it? This, too, is business not personal.

III. WHAT'S REALLY HAPPENING?

A. Case Studies

a. Residential Mortgage

1. Case Study: Florida

Below is an actual hardship letter written in April 2009, requesting a loan modification of a residential loan:

> I am requesting a loan modification because I cannot afford my mortgage under the current terms. I have lived in the home since June 2007 after an expected separation from my wife in June 2007. We divorced in August 2007 (which caused my credit score to drop resulting in a higher interest rate than I should have) and have suffered several setbacks since then. However, since that time, I have been able to raise my credit score to a good-excellent range (mid-700s).
>
> To begin, I am a disabled Vietnam Veteran who is on a fixed monthly income. My current loan terms include an ARM at a present interest rate of 8.875%. Presently, my home is worth less than $200,000 and I owe well over that amount (approximately $275,000). In addition, I have only been able to make the minimum payment (Option 1), which is causing my mortgage to increase in negative amortization each month.
>
> [Lender's loan modification company] turned me down for a loan modification in March 2009. I am requesting that [Lender] (not Lender's loan modification company) review my

houses not only provided shelter but also a plump nest egg").

165 SCHECHTER, *supra* note 3, at 36.

166 *See e.g.*, Roben Farzad, *Goldman Sachs: Don't Blame Us*, BUSINESS WEEK, Apr. 12, 2010, at 30, 32 (reporting that Goldman Sachs "posted a $13.4 billion profit in 2009, a Wall Street record").

loan for a modification. Also since then, [A state bar] has assigned to me a volunteer attorney to help me with this loan modification under [its home ownership program. I have copied her on this letter, and she is on file with your company as my lawyer.

My hardship began with my unexpected and devastating divorce from my wife of 9 years, but who I lived with for almost 11 years total. As a result, I had to move and obtain a mortgage for myself only. My wife said that she could not continue to deal with my disability.

Subsequent to the divorce and soon after I refinanced my home in 2007, my sister died in the fall of 2008 from Parkinson's disease, and my brother-in-law died soon after in January 2009 from heart failure. This placed enormous stress on me, including financial stress as I depleted my entire savings to help pay the medical and funeral expenses for them.

In addition to all of the above, as a disabled Vietnam Veteran, I must continue with medical care at the VA medical facility. The nearest medical facility is a two hour drive from my home. This long drive coupled with the increased frequency of visits that I must make as well as the unpredictable and rising cost of fuel and vehicle maintenance, have significantly contributed to my financial drain.

I cannot continue to drive myself into a negative amortization with my home. It is causing me severe stress on top of my other medical conditions, and is providing me with no financial security for the future in investing in a home.

I do not have the ability to earn additional income. I was honorably discharged from the United States military where I was severely wounded and remain disabled. I am alone. I do not have a wife, and my daughter from a prior marriage is 30 and has no ability to help with my expenses. Because of my financial situation, I have not been able to travel to see my daughter in over 26 months. I have also not seen my mother since my sister's death also because of my financial situation. When the loan that I have now adjusts after the ARM ends, I will be completely unable to pay for the home, and I will owe so much more on the home than it is worth.

I cannot continue to do this any longer. Please help me. If I had a fixed loan with a much lower interest rate that is now available because the recession has caused interest rates to

> drop, that would help me. In addition, I am very responsible as during this time, I have been able to get raise my credit score to what it has always been in my life – good to excellent. If nothing more, please allow me to do a short sale and move to a home closer to the VA medical facility.[167]

Two months later, the borrower then wrote his congressional representative and state administrative officer about the hardship. He informed them:

> I am contacting you because I have had no relief from my current mortgage, even after twice submitting information to [the lender] for a loan modification. Initially, [the lender] denied a modification because I received too much income. Most recently, even with little income change, I was denied because [the lender] said I would not be able to afford a loan modification. I have worked with [the state bar's housing program], but still no relief from [the lender], which does not appear to be cooperating with [the state bar] for loan relief as other loan institutions are doing.[168]

The borrower received no assistance from either, and his health was deteriorating due to stress and because he was so far from the hospital that he had to visit several times a week for medical care.

After receiving no help from the lender or others, the borrower "walked away" – he moved into a house closer to the VA hospital, stopped paying the lender, and left the keys of his "underwater" home on the kitchen table. He could have continued paying on this worthless investment because he could afford the monthly payment, but he left because his mortgage was heavily underwater and the loan terms were unconscionable – this is business, not personal. His action's got the lender's attention and it began working with the borrower. Since that time, the borrower has obtained a buyer for the house on a short sale contract in the amount of $160,000 – less than $100,000 of the balance owed on the mortgage. The lender's appraiser was $175,000, so the lender's appraisal performed due diligence to determine whether his appraisal was consistent with other area sale or needed an adjustment. After concluding that the short sale contract was $15,000 less than the market value, the lender sought the shortfall from the buyers, who withdrew from the short sale contract. The house is back on

167 Hardship letter from a homeowner to a lender (slight modifications for anonymity) (Apr. 2009) (on file with author).

168 *Id.*

the market.

While awaiting the short sale approval, the lender filed a foreclosure complaint, attaching the note that reflected a different lender than the lender (plaintiff) who filed the lawsuit. This is not unusual; many lenders do not have the proper documentation showing that they are the proper lender.

> In some cases records have been destroyed and mortgages sliced and diced into so many pieces that it is hard to even know who owns certain properties that have been sold or resold worldwide. They have been packaged, bundled, and turned into structured investment vehicles ("SIV's") or Collateralized Debt Obligations (CDOs). Many homeowners pay bills to mortgage servicers companies, not the real owners of their homes and properties.[169]

The borrower's response to the complaint was a motion to dismiss.[170] As of late summer 2010, the borrower was waiting for a new buyer for the house and perhaps the lender's approval of another short sale.[171] The borrower will seek a deed-in-lieu of foreclosure ("DIL"), which "is a disposition option in which a mortgagor voluntarily deeds collateral property in exchange for a release from all obligations under the mortgage."[172] This will save the lender the money that it would spend to foreclose, and the lender may not accept the DIL if it believes the borrower can afford the mortgage. Industry practice shows that borrowers must offer a DIL because the lenders are not mentioning DILs, but it is better than a foreclosure for all parties involved.

169 SCHECHTER, *supra* note 3, at 179.

170 This reveals another issue not a part of this article, but borrowers who cannot afford lawyers are unaware of their defenses when sued; thus, the foreclosure crisis is disproportionately affecting those with lower incomes because the mortgage companies obtain judgments (mostly be default for failing to appear) easily against those without lawyers than those who can afford lawyers when the defendants had valid defenses. The courts should sanction attorneys who continue to file such complaints without the proper documents showing that the lender who is bringing the lawsuit is the lender who is on record as owning the mortgage. The Florida Bar is disciplining attorneys who are participating in the foreclosure debacle. *See* Gary Blankenship, *Bar Ramps Up Foreclosure-Related Activities*, FLORIDA BAR NEWS, Nov. 15, 2010, *available at* http://www.floridabar.org/DIVCOM/JN/jnnews01.nsf/8c9f13012b96736985256aa900624829/cd7f5e65a787b897852577d20068bcde!OpenDocument.

171 Federal guidelines were established to speed up the approval process for short sales, *see* June Fletcher, *Speeding Up Short Sales*, WALL STREET J., Apr. 9, 2010, *available at* http://online.wsj.com/article/NA_WSJ_PUB:SB10001424052702304198004575171882448724258.html, but this has not made a dent in the short sale approval process. Lenders are sitting on short sale offers for months during which time the housing contract usually expires, buyers get tired of waiting, and the lender files a foreclosure action.

172 U.S. Dep't of Housing & Urban Dev., *Deed-in-Lieu: Frequently Asked Questions*, http://www.hud.gov/offices/hsg/sfh/nsc/faqdil.cfm (May 15, 2009).

Overall, the borrower has been relieved of his stress related to his housing debt, his health has improved,[173] he is unconcerned with his current credit bureau score that moved from "excellent" to "good," and he is enjoying his new home.

2. Case Study: Florida

In another instance, a homeowner purchased a single family home in the summer of 2006 for $250,000. The house was recently valued at $114,000. The borrower has a thirty year loan with only interest for the first 10 years at a fixed rate of 6.5 percent for $200,000 and 8 percent for the remaining $50,000. The borrower's desire is to remain in the house and she can afford to do so; however, she has not yet explored any possibilities for loan relief.

3. Case Study: Virginia

In another scenario, the borrower purchased a condominium for $450,000 in 2004 that she financed with a first mortgage of $370,000 and a second mortgage of $80,000. By 2008, the value of the condominium had dropped to $380,000. The borrower tried to refinance the loan, but the bank would only refinance at 80 percent of the condominium's current value ($380,000) and expected the borrower to bring $126,000 to closing. As a result, the borrower obtained a buyer for a short sale of the property. The junior lien holder rejected the short sale, and the condominium was ultimately foreclosed. Although the law provided that junior lien holders had the right to veto the sale or modification,[174] industry practice reveals that often the first lien holder would share the proceeds with the cooperating second (junior) lien holder in a short sale.

For example in another Florida case, a house was purchased for $310,000 in 2004, appraised at $424,000 and refinanced in 2006. The house then sold for $240,000 in a short sale in 2009. The first lien holder

[173] *Debt Stress Causing Health Problems, Poll Finds*, June 9, 2008, http://www.msnbc.msn.com/id/25060719/ ("When people are dealing with mountains of debt, they're much more likely to report health problems, too, according to an Associated Press-AOL Health poll. And not just little stuff; this means ulcers, severe depression, even heart attacks. ... 'Although most people appear to be managing their debts all right, perhaps 10 million to 16 million are "suffering terribly due to their debts, and their health is likely to be negatively impacted,' says Paul J. Lavrakas, a research psychologist and AP consultant who analyzed the results of the survey. 'Those are people who reported high levels of debt stress and suffered from at least three stress-related illnesses, he says.'").

[174] ZANDI, *supra* note 7, at 209 ("The law gave second mortgage holders the right to veto loan modifications; yet in the kinds of loan write-downs being proposed, they stood to lose everything. A foreclosure would be no better – junior liens would likely be wiped out in either case – but many second mortgage holders reasoned they had nothing to lose by vetoing a modification.").

was owed roughly $345,000 and the second lien holder (HELOC) was owed roughly $40,000; the first lien holder agreed to accept approximately $205,000 net proceeds and any junior lien holder could receive no more than $11,500 net proceeds, which the junior lien holder accepted. Over a year after the home's closing, the junior lien holder notified the borrower that it waived its right to the deficiency. This is likely a result of President Obama's administration's and states' attorneys generals pressure for these large lenders to work with the American people, as well as the ongoing investigations that so many of the large lenders are now facing and the repeated findings of wrongdoing by these large lenders.

4. Case Study: California

In this scenario, a family bought a home in 1990 for $200,000. The home's value increased to over $800,000, during which time the homeowners took money out for college expenses and other things. The home is now valued at $200,000, and the family owes well over the current value of the house.

b. Commercial Mortgage

The commercial mortgage lending business went south too. Indeed, commercial property lending is said to be in a much worse condition than subprime home property lending.[175] Wall Street is similarly unhelpful to its commercial clients as well.

In another scenario, a borrower bought commercial investment, income-producing property in 2005 valued at roughly $825,000 and paid 20 percent down. The borrower refinanced with a major lender (which later went into bankruptcy) in 2007 to an ARM at 7 percent for 5 years and after the loan could increase to 12 percent for the next 35 years (40 year loan), depending upon the current interest rate. At this time, the property was valued by the lender's appraiser near $1.2 million.[176] Then in 2009, the borrower, trying to survive the impact of the recession, sought a loan modification from the current mortgage holder, which was not the lender who refinanced the property in 2007. At all times, the borrower's credit was "very good" and would have been considered a creditworthy (or prime) borrower. Nevertheless, the borrower was only offered yet another subprime loan – an ARM that changes every 6 months with a balloon payment in three

175 Krugman, *supra* note 78.

176 Ridge & Rushak, *supra* note 146, at 13 (noting that Washington Mutual used appraisers who would inflate the home values).

years. Thus, in three years (now two), the borrower must either refinance or sell the property that is heavily "underwater." This time, the lender's appraiser valued the property at approximately $450,000 and the lender did not willingly disclose the appraisal value to the borrower. Because the current interest rate is at an historic 50 year low,[177] the mortgage payments (ARMs initial payments) have been unusually low – perhaps to the dismay of the lender, another Wall Street giant – but with the variable interest rate, every six months is a "wait-and-see": will the mortgage go up, stay the same, or go down? Thus far, the mortgage payment has gone down every six months since the loan's inception because mortgage rates hit historic lows.

B. Strategic Defaults

As reflected above, the current housing crisis began with defaults from the low- to moderate-income borrowers, who had little money elsewhere to draw from in this recession. The crisis now is stuck in the middle class, many of whom have lost their employment, and is also among the upper middle class and the wealthy. "The surprisingly high number of subprime loans among more credit-worthy borrowers shows how far such mortgages have spread into the economy—including middle-class and wealthy communities where they once were scarce."[178] Those borrowers who really could not afford their homes – generally lower income with subprime loans in which the ARM ended—have already defaulted.[179] The borrowers left are those whose homes are deeply underwater but who can afford their loan, even if the payment they can afford continues to put them into negative amortization (option ARM), as they sink money into a valueless asset.[180] "Proposed solutions that would keep more people who aren't behind on their mortgage payments in their homes and stabilize the market have largely been ignored."[181] Additionally, lenders have not been amenable to modifying underwater mortgages even if it would be socially

177 Ann Brenoff, *Mortgage Rates Hit 50 Year Low*, HUFFINGTON POST, June 28, 2010, http://www.huffingtonpost.com/2010/06/28/mortgage-rates-hit-50-yea_n_627529.html (discussing the positive and negative news associated with experiencing the lowest mortgage rate in more than 50 years).

178 Brooks, *supra* note 75.

179 *Double-Dip Drama*, *supra* note 139, at 35.

180 *Id.* ("And a growing number of underwater borrowers are opting simply to walk away from mortgages that they can in fact afford.").

181 Beth Kassab, *Where's the Relief for Homeowners Who Played by the Rules?*, ORLANDO SENTINEL, May 20, 2010, *available at* http://articles.orlandosentinel.com/2010-05-20/business/os-kassab-foreclosure-solution-05212020100520_1_underwater-homeowners-mortgage-payments-default.

and morally responsible for them to modify them to do so.[182] Many lenders are prolonging the inevitable rather than fixing the problem by modifying loans with more subprime terms and conditions; thus, in the next 3-5 years, there will likely be another wave of defaults for residential and commercial property. This wave of defaults will likely also evince the discriminatory manner in which lenders are modifying loans – less educated borrowers are receiving considerably worse terms and conditions.[183] Educated borrowers often have the aid of legal counsel and knowledge of other resources than less educated borrowers.

These case studies reflect what is really happening on Main Street with residential and commercial properties – Wall Street is not helping as much as they would like Americans to believe.[184] They have not discontinued subprime loans to prime customers and others, and they refuse to allow borrowers out of "bad loans," especially if the borrower can afford the bad loan.

Thus, many Americans are "strategically defaulting." They are walking away, even when they can afford the loan, because it is no longer a good investment.[185] In addition, so often the borrower is in a bad loan – a subprime loan. Some borrowers are afraid to just walk away, but higher income borrowers are "less susceptible to the shame and fear-mongering used by the government and the mortgage banking industry to keep underwater homeowners from acting in their financial best interest."[186]

Strategic defaults are increasing and are being heavily criticized.[187] "Fannie Mae and Freddie Mac, the two quasi-governmental mortgage finance companies that own most of the mortgages in America with a value of less than $500,000, are alternately pleading with distressed homeowners

182 White, *supra* note 7, at 2 (distinguishing the influences that affect lenders versus individual homeowners when dealing with mortgages).

183 In one case, the borrower (lower income) was in default and the lender gave the borrower a reduced payment for four months, then the lender tacked the amount in arrears to the end of the loan.

184 *See e.g.*, Beatrice Garcia, *Florida's Broward County Officials Take a Stand Against BofA*, March 15, 2010, http://www.housingwatch.com/2010/03/15/broward-county-officials-take-a-stand-against-bofa/ (reporting that Broward County Board of Commissioners penalized Bank of America because the Commission believes that Bank of America is wrongly seizing people's homes and not properly processing and approving loan modifications).

185 *Double-Dip Drama*, *supra* note 139, at 35 (discussing how homeowners are walking away from their mortgages to avoid suffering a huge loss upon sale); Streitfeld, *supra* note 133, at A1 (noting the recent trend in Silicon Valley of upper class homeowners with lavish properties defaulting on their mortgages).

186 Streitfeld, *supra* note 133, at A1 (quoting Professor Brent White, a University of Arizona law professor who has studied strategic defaults).

187 White, *supra* note 7, at 25 ("The clear message to American homeowners from nearly all fronts is that one has a moral responsibility to pay one's mortgage. The message is conveyed not only by political, social, and economic institutions, but by the majority of Americans who believe that voluntarily defaulting on a mortgage is immoral.")

not to be bad citizens and brandishing a stick at them."[188] Indeed, Fannie Mae recently increased the penalty for those who it believes have strategically defaulted.[189] An ethics professor opined that borrowers who can pay their mortgage and were not deceived by the lender (that is, does not have a subprime loan) have a "moral responsibility" to continue to pay the mortgage; otherwise, it would destroy the American economy if borrowers walked away from their commitments.[190] Wall Street and others are calling for Main Street to be honorable in the repayment of their mortgage debts, so as not to "trash their communities."[191] This too was the case with Tulipmania in which there was a "fear, the fear of disorder, was justified, because when the question was one of honor – of the repayment of debts, of the breaking of obligations – the consequences for the community could be dire."[192]

But it was the banks who trashed the nation's communities; the subprime crisis was a "heist by banks," targeting the American people, enriching a few and destroying whole neighborhoods.[193] The subprime crisis has been called a "white-collar crime wave."[194] Crimes committed by mortgage brokers who originated loans to borrowers who did not comprehend the terms, could not afford to pay the loan, and should not have qualified; appraisers who overvalued property to obtain additional business from dishonest brokers; and banks and brokerage firms that originated or bought, packaged, and resold the mortgages for stiff fees.[195] The crimes committed were 'substantial' and in every state in the country.[196]

188 Streitfeld, *supra* note 133, at A1.

189 News Release, *supra* note 138 ("Defaulting borrowers who walk-away and had the capacity to pay or did not complete a workout alternative in good faith will be ineligible for a new Fannie Mae-backed mortgage loan for a period of seven years from the date of foreclosure.... Fannie Mae will also take legal action to recoup the outstanding mortgage debt from borrowers who strategically default on their loans in jurisdictions that allow for deficiency judgments.").

190 James R. Hagerty & Nick Timiraos, *Debtor's Dilemma: Pay the Mortgage or Walk Away*, WALL STREET J., Dec. 17, 2009, *available at* http://online.wsj.com/article/NA_WSJ_PUB:SB126100260600594531.html.

191 Gold, *supra* note 157, at 205 (foreclosures negatively impact neighborhoods).

192 GOLDGAR, *supra* note 17, at 251.

193 SCHECHTER, *supra* note 3, at 13.

194 *Id.* 23, 124 (reporting that the Attorney General indicated that a special task force will be created to investigate whether there was wrongdoing in the mortgage lending agency); *see* Becky Quick, *Why No Jail Time for Wall Street*, CNN Money, June 23, 1010, http://money.cnn.com/2010/06/23/news/companies/prosecutors_ignoring_wall_street.fortune/index.htm (asking where the jail time is for those who oversaw the subprime mortgage crisis); *but see* Kermit J. Lind, *The Perfect Storm: An Eyewitness Report from Ground Zero in Cleveland's Neighborhood's*, 17 J. AFF. HOUS. & COM. DEV. L. 237, 253 (2008) (noting that the defendants in recent civil cases are lenders and investment banks, and that brokers, appraisers, and borrowers are being indicted in criminal cases).

195 SCHECHTER *supra* note 3, at 24 (quoting Basil Williams, CEO of a hedge fund).

196 *Id.* at 31(quoting FBI director Robert Mueller).

It is estimated that roughly 14 million homeowners are currently underwater, and this is expected to increase to 20 million by the end of 2011.[197] "Lenders are fearful that many of the 11 million or so homeowners who owe more than their house is worth will walk away from them, especially if the real estate market begins to weaken again. The so-called strategic defaults have become a matter of intense debate in recent months."[198] After the Tulipmania crash, "some honorable people" attempted to pay something on their debts, but most of the debtors did not.[199] And so it may be with American borrowers because they are opting for strategic defaults.

Because of the current economic climate, many homeowners are seriously considering a strategic default. In fact, strategic defaults are expected to increase.[200] Some homeowners consider strategic defaults to be immoral:

> When I sign a contract, it is not just ink. I have given my word. Events can happen that make carrying out a contract and making good on your word impossible. Events that make it hard, uncomfortable, inconvenient and unprofitable are not reason enough to break your word. Just walking away from a binding contract should have a lasting effect on a person's ability to borrow again.[201]

In a recent study, roughly 80% replied that it was morally wrong to walk away from a house when they could afford to pay the monthly note.[202] And others do not:

> As a homeowner that is currently employing a strategic default, I take exception to your description of my decision as immoral. I chose to walk away in order to save myself financially from a bottomless pit. Should I risk my entire

197 Lita Epstein, *20 Million Homeowners Projected to Be Underwater by End of 2011*, HOUSING WATCH, Aug. 5, 2010, *available at* http://www.housingwatch.com/2010/08/05/20-million-homeowners-projected-to-be-underwater-by-end-of-2011/.

198 Streitfeld, *supra* note 133, at A1.

199 GOLDGAR, *supra* note 17, at 251.

200 Jody Shenn, *"Strategic" Mortgage Defaults Jump to 12 Percent of Total*, BUSINESS WEEK, Apr. 29, 2010, *available at* http://www.businessweek.com/news/2010-04-29/-strategic-mortgage-defaults-jump-to-12-of-total-update3-.html.

201 Beth Kassab, *Readers Write on Mortgage Morality*, ORLANDO SENTINEL, May 25, 2010, *available at* http://www.orlandosentinel.com/business/os-kassab-letters05262010020100525,0,1895697.column.

202 Luigi Guiso et al., *Moral and Social Constraints to Strategic Default on Mortgages* 10, 19 (Fin. Trust Index, Working Paper, July 2009), *available at* http://www.financialtrustindex.org/images/Guiso_Sapienza_Zingales_StrategicDefault.pdf.

> financial life, my family's financial life and my retirement on a single house? I don't believe that I did anything IMMORAL. I tried for a year to work things out with the bank, but THEY refused. They left me in a position to make a serious decision about my financial future. One that I didn't take lightly. One that will ruin my credit. One that I will be paying for years to come. I don't just get a free ride by walking away![203]
>
> "I'm mad as hell and I'm not going to take it anymore." I guess that is where I and many other hard-working Americans are just now. That is why they are walking away in droves from their mortgages and are voting out the establishment.[204]

One legal scholar stated: "It's simply wrong, in my opinion, to ask underwater homeowners to accept their own financial ruin for the common good, especially when the housing collapse was caused primarily by the mortgage industry and the government's failed policies,. . . [a mortgage] is purely a legal document, not a sacred promise."[205] He argues that a strategic default is similar to terminating a mobile phone contract if you find a better deal with a different carrier.[206] In addition, attorneys and others advisors are recommending to homeowners that strategic defaults may be the best solution in the homeowners' situation.[207]

Some economists assert that strategic defaults may not be an ideal solution in some situations because of economic reasons, such as: 1) the interest on the mortgage may be less than renting another house; 2) moving incurs relocation costs; 3) the defaulter's credit bureau score will decline;[208] and 4) the defaulter may face a deficiency judgment if the

203 Kassab, *supra* note 201.

204 *Id.*

205 Beth Kassab, *Is It Wrong To Walk Away From Your Mortgage When You Can Still Pay?*, ORLANDO SENTINEL, May 19, 2010, *available at* http://articles.orlandosentinel.com/2010-05-19/business/os-kassab-mortgage-morality-05192010-20100519_1_underwater-homeowners-luigi-zingales-mortgage-industry (quoting Professor Brent White).

206 *Id.*

207 *See e.g.*, Kaufman, Englett & Lynd, PLLC, *Strategic Default*, www.dominionrealtynation.com/strategic-default.htm (last visited Feb. 10, 2011) ("This is the situation where a strategic default makes sense. A strategic default involves deliberately failing to pay a mortgage despite being able to do so. Obviously, a strategic default must be very carefully considered in order to be effective. Unless you are confident that a strategic default is the best move for you, you should seek other options."); *see also*, Carman Law Firm, P.A., *Considering Walking Away from Your Home?: Strategic Default*, www.floridaforeclosuredefenders.com/Foreclosure-Defense/Strategic-Default.aspx (last visited Feb. 10, 2011); YouWalkAway, www.youwalkaway.com (last visited Feb. 10, 2011) (providing foreclosure information from real estate professionals to assist owners of underwater homes to strategically walk away from their properties).

208 While the FICO score may decline roughly 130-140 points, it often springs back in a few months to where its pre-default level assuming the consumer has good credit otherwise. However, the foreclosure or short sale indication will remain on the defaulter's credit record for seven years.

mortgage is a recourse-loan, which allows creditors to pursue the deficiency of the mortgage balance after the resale value of the house.[209] But these concerns pale in comparison to overwhelming debt coupled with a loan with risky terms and conditions. Furthermore, the homeowners who have been so bold as to "walk away" from their bad loans, experience little of what these experts are cautioning. Professor White said it best:

> [T]here is in fact a huge financial upside to strategic default for seriously underwater homeowners – an upside that is routinely ignored by the media, credit counseling agencies, and other political and economic institutions in "informing" homeowners about the consequences of default. Moreover, the costs of default are not nearly as extreme as these same institutions typically misrepresent them to be. In reality: homeowners face no risk of a deficiency judgment in many states or, regardless of the state, for FHA loans or loans held by Fannie Mae or Freddie Mac; even in recourse states, lenders are unlikely to pursue a deficiency judgment because it is economically inefficient to do so; there is no tax liability on "forgiven portions" of home mortgages under current federal tax law in effect until 2012; defaulting on one's mortgage does not mean that one's other credit lines will be revoked; and most people can expect to recover from the negative impact of foreclosure on their credit score within two year years (and, meanwhile, two years of poor credit need not seriously impact one's life.[210]

The reality is that a strategic default may be the best course of option when you are locked in a bad loan. Even corporate housing lending executives believe that walking away may be the best option for some homeowners.[211] This applies to residential and commercial properties. Recommended courses of action are not a one size fits all, but rather a property owners' individual situation must be considered on a case by case basis. Companies understanding the current economic national and global crisis are developing programs and guidelines for people who may have a mortgage default on their credit.[212] Strategic defaults – properly named –

209 Guiso, *supra* note 202, at 3 (explaining that a defaulter may face a deficiency judgment for the amount of his home).

210 White, *supra* note 7, at 32-33.

211 Streitfeld, *supra* note 133 (providing an example where a corporate executive suggested that walking away from an underwater home may be a good option).

212 *See, e.g.*, The Golden 1 Credit Union, www.golden1.com/loans/mortgageassistance (last visited Feb. 12, 2011) (advertising many individualized options to its constituents who have been adversely affected by the mortgage crisis).

may in some cases be the best option for the property owner.

Most homeowners who are underwater in their homes continue to pay despite knowing that they will likely never recoup their losses.[213] And one scholar advises that: "Homeowners should be walking away in droves. But they aren't."[214] Fear, shame, guilt, and possible retribution have stifled homeowners from considering all of their housing options.[215] Not only fear and guilt, but there is also envy among homeowners who have not been so bold as to walk away – they argue that indeed they are now paying for the costs of the walkway's defaulted loan. The non-walkaways want to join the ranks of the walkaways, but they are embarrassed and terrified.

Wall Street was savvy enough to get America in this subprime mess, but has come up short with remedies to help the real victims – Main Street. Lenders do not want borrowers to walk away, but rather stay in underwater homes with subprime terms and conditions. But, instead of foreclosing on homeowners, destroying their credit (thus preventing them from obtaining employment),[216] and evicting them from their homes, or modifying subprime loans with more subprime terms and conditions which will cause another wave of defaults, lenders should consider some viable options or a combination thereof.

One idea is for the lender to take back the mortgage and allow the borrower to remain in the home and rent it back at the fair market value ("FMV"). The borrower would not be able to move unless he found another borrower to rent the house, but the banks would be the ones to wait out this crisis while holding the note. Any equity that accrues would go to the lender; the borrower then is not accruing equity nor liability and still has a place to live, and the lender is not holding empty homes and destroying neighborhoods. If the original borrower continues to live on the property (instead of moving and finding another person to rent the home), then the lender and borrower may agree to share any equity that accrues while the original borrower is still there.

Another consideration is that the lenders could readjust or modify the

213 White, *supra* note 7, at 971-72 (analyzing why homeowners would rather pay off their mortgage though their houses are worth far less than the mortgage).

214 *Id.* at 983.

215 *Id.* at 935-95 (discussing the sociological reasons as to why underwater homeowners are reluctant to default on their mortgage).

216 Liz Pulliam Weston, *How Bad Credit Can Cost You a Job*, MSN Money, http://articles.moneycentral.msn.com/Banking/YourCreditRating/how-bad-credit-can-cost-you-a-job.aspx (Aug. 17, 2009) ("A fair chunk of employers want to examine your credit history before offering you a position or a promotion. Blotches there -- repossessions, collections, high credit card balances -- could cost you the job you want. For example, applicants for Transportation Security Administration airport screener jobs are rejected if they have more than $5,000 in overdue debt.").

note by 1) reducing the interest rate to 1 or 2 percent of the current underwater mortgage balance of $250,000 (residential case study 2 above); or 2) reducing the loan to the current FMV of $114,000 (residential case study 2 above) and the interest rate to the current interest rate of 4.44 percent, which rate is being wasted because borrowers are unable to qualify under the stricter refinance lending guidelines, requiring a FICO score of 620 or above, a higher down payment, and lower monthly debt service ratios.[217] However, loan modifications do not need to qualify as it is not a refinance. These options may allow the owner to remain in the home and if there is a sale and any equity at the time of the sale, then the lender and homeowner can share the equity.

Another solution that may help some homeowners maintain their homes is for lenders to modify the existing loans (including those underwater) to the current, historic interest rate of 4.44 percent. The lender will still have the same collateral – the house – that it currently has, but the borrower will have lower monthly payments, and therefore, is more likely to avoid foreclosure. What good is a high interest rate to the lender if the borrower cannot afford it? Thus, the lender will cut its losses and the buyer will keep the home, avoiding issues with squatters taking over vacant properties.[218] The only risk to the lender is if a foreclosure occurs, then the house will sell for less than the value of the mortgage. This is exactly the same risk the lenders currently face. This proposal would mitigate some of the risk because lenders would be able to avoid some foreclosures while receiving additional payments from some borrowers, who ultimately default, even with the reduced payments. The lenders keep asking Main Street, the victims, to wait this crisis out, but they should be the ones to wait it out.

Additionally, this subprime crisis will be further impacted by collection companies buying deficiency judgments from foreclosures, deed-in-lieu of foreclosures, or short sales. Absent regulatory or legislative intervention, more collection companies will buy the deficiency judgments for pennies on the dollar and try to collect 100% from the debtor/borrower.[219] If that

217 Nin-Hai Tseng, *The Wasted 4.44% Mortgage Rate*, CNN Money, Aug. 16, 2010, http://money.cnn.com/2010/08/13/real_estate/mortgage_rates_refinancing.fortune/index.htm (discussing the all-time low mortgage rates that are inaccessible to those who need to refinance most).

218 John Leland, *With Advocates' Help, Squatters Call Foreclosures Home*, N.Y. TIMES, April 10, 2009, at A1, *available at* http://www.nytimes.com/2009/04/10/us/10squatter.html ("Michael Stoops, executive director of the National Coalition for the Homeless, said about a dozen advocacy groups around the country were actively moving homeless people into vacant homes — some working in secret, others, like Take Back the Land, operating openly. In addition to squatting, some advocacy groups have organized civil disobedience actions in which borrowers or renters refuse to leave homes after foreclosure.").

219 Kimberly Miller, *Borrowers Beware: Firms Profit Off Defaults*, PALM BEACH POST, June 12,

happens, "[i]t's going to be a blood bath."[220] This "deficiency" is due to the fraudulent and deceptive business practices used by mortgage brokers, appraisers, and lenders – that is, the loan was fraudulent at its inception, so collection companies should not be able to benefit from the deceptive activity of the team of persons who originated the loan, appraised the property, and funded the subprime loan. The state and federal governments need to enact protections – legislative protections – now, so that the economic recovery of America is not further stymied by collection companies chasing borrowers years after they have separated from their property where so often the borrower was deceived at the inception of the mortgage loan.

There will also likely be another wave of defaults within the next few years because loan modification ARMs will end on residential and commercial properties. Furthermore, prime borrowers with non-traditional mortgages will see their mortgages reset, and many will be unable to afford the increase.[221] Sadly, true loan modifications are just not happening.[222] As a result, many borrowers with loan modifications have re-defaulted[223] because the lenders are not providing significant relief to home owners. Perhaps this is in part because lenders are trying to overcompensate for the losses due to the long overdue reforms with the credit card industry which was needlessly profiting off of consumers in unconscionable ways.[224] Without true loan modifications the defaults and foreclosures will continue.

2010, *available at* http://www.palmbeachpost.com/money/real-estate/borrowers-beware-firms-profit-off-defaults-744186.html (reporting that a cottage industry of entrepreneurs will begin buying deficiency judgments from foreclosures or short sales and making borrowers pay up); Michael McCauley & Megan Ryan, *Debt Collection Abuses on the Rise During Tough Economic Times: Advocates Call for Stronger Protections for Consumers*, ConsumersUnion.org (Feb. 2, 2011), http://www.consumersunion.org/pub/core_financial_services/017368.html ("Buying and selling debt is essentially an unregulated industry.").

220 Miller, *supra* note 219 (quoting an owner of a short sale operation).

221 SCHECHTER, *supra* note 3, at xxiii (stating that Sheila C. Blair, chairperson of the FDIC, warned a Senate Banking Committee panel that "in 2009, $600 billion worth of prime borrowers will see their "non-traditional" mortgages reset, and many won't be able to find the cash").

222 Miller, *supra* note 219 (noting that Joshua Rand, a principal in the New York-based Deficiency Judgment Recovery Network, expressed that "[p]eople are under the assumption that the banks are so busy modifying home loans that they don't have the bandwidth or stomach to go after those who are walking away. That's a bad assumption").

223 Lita Epstein, *Mortgage Mods: Most Borrowers Are Likely to Redefault Within a Year*, June 18, 2010, http://realestate.aol.com/blog/2010/06/18/mortgage-mods-most-borrowers-are-likely-to-redefault-within-a-y/; Tami Luhby, *Borrowers Flunking Out of Trial Mortgage Modifications*, CNN Money, May 17, 2010, http://money.cnn.com/2010/05/17/news/economy/HAMP_modifications/index.htm.

224 *See e.g.*, Lita Epstein, *JPMorgan Chase Is No Fan of Latest Obama Plan to Stem Foreclosures*, Apr. 13, 2010, http://realestate.aol.com/blog/2010/04/13/jpmorgan-chase-is-no-fan-of-latest-obama-plan-to-stem-foreclosur/ (reporting that Chase is opposed to principal reductions of mortgages and Chase CEO "complained that the credit card reforms alone will cost Chase between $500 million and $750 million in after-tax income").

"If [defaults and foreclosures continue], losses will deepen for investors and lenders, home values will plummet for surrounding communities, and the entire economy will suffer."[225]

And if all else fails for these borrowers, then a strategic default, in the words of Freddie Mac's executive, "might well be a good decision for certain borrowers."[226]

CONCLUSION

The economy is showing small signs of recovery. Unemployment appears to be going down. Bankruptcy filings and foreclosures, however, continue to increase largely because housing prices continue to decrease. The media tends to focus on the problems of Wall Street, yet there are far greater challenges facing the millions of Americans who have lost or are facing loss of their jobs and their homes. Wall Street appears to have gone back to business as usual, and the help that Wall Street is providing Main Street is dismal. Wall Street may be recovering from a cold, but Main Street has pneumonia.[227]

225 Krimminger, *supra* note 49, at 265.

226 Streitfeld, *supra* note 133.

227 *See* TheBigApple.com, *When Wall Street Sneezes, The Rest of the World Catches Pneumonia*, http://www.barrypopik.com/index.php/new_york_city/entry/when_wall_street_sneezes_the_rest_of_the_world_catches_pneumonia_when_ameri/ (last visited Feb. 12, 2011) ("Wall Street influences Main Street and even the rest of the world. 'When Wall Street sneezes,' the saying goes, 'the rest of the world catches pneumonia.' The phrase has several variations, with 'America' or 'United States' replacing Wall Street and with 'cold' replacing 'pneumonia.'").