Eminent Domain Mortgages Seizures will Hinder the Housing Market Recovery

MBA RECOMMENDS

State and local governments must not attempt to apply eminent domain laws as a way to refinance underwater mortgages in their communities. MBA agrees wholeheartedly with the Federal Housing Finance Authority (FHFA) that “utilizing eminent domain in this way could undermine and have a chilling effect on the extension of credit” to prospective homeowners. Existing, underutilized housing programs are better tailored toward helping distressed homeowners, and policy-makers should encourage and reinforce them.

BACKGROUND

Municipal governments in various parts of the country are considering the use of eminent domain as an option for assisting underwater borrowers in their communities (the Proposals). Generally, the Proposals contemplate using the eminent domain process to seize the mortgages of underwater homeowners who are current in their payments. Homeowners would be able to remain in their homes, while the mortgage itself would incur a principal “cram-down” to market value before being refinanced and resold to new investors.

This unprecedented use of eminent domain would constrict the availability of mortgage credit, as mortgage investors would likely refuse to purchase mortgages in participating communities due to expected lending losses and collateral risk. As investors withdraw from these markets, fewer creditworthy borrowers would be able to purchase a home, depressing demand below its current levels. The result could be many more homeowners pushed underwater by further declines in home values. Mortgage rates and/or down payment requirements would rise to compensate for the added eminent domain risk and in turn, price many prospective homebuyers out of the market, particularly in distressed communities.

MBA believes the Proposals are not constitutional. Transferring mortgages from their current holders to a privately-owned refinancing entity violates the “public use” requirement for affecting a taking under eminent domain. Moreover, owners of a seized mortgage would not receive the “just compensation” required under eminent domain, since performing mortgages would be revalued at some percentage of the value of the collateral. The Proposals likely also violate the Contracts Clause of the Constitution, in that they would substantially impair existing contractual relationships.

The Proposals take advantage of the federal government’s current refinance programs, and as a result would significantly increase taxpayer exposure. This risk prompted the FHFA to issue a statement on August 9, 2012 expressing “significant concerns” with the Proposals. As currently envisioned, seized mortgages would be refinanced into mortgages eligible for sale to Fannie Mae and Freddie Mac, effectively transferring the risk of default to the American taxpayer.

For more information, visit mba.org or call (202) 557-2700.
**ACTION NEEDED**

Initiatives such as the Home Affordable Refinance Program (HARP) and Home Affordable Modification Program (HAMP), among servicers’ other proprietary loss mitigation programs, can better help the type of homeowners targeted by the Proposals. These programs are currently underutilized and do not pose the same risks as eminent domain. Additionally, these programs expressly target homeowners who are truly at risk of losing their homes.

While growth and recovery in the housing market in some areas are not happening as quickly as would be desired, MBA believes policy-makers must not lose sight of the road to recovery. Eliminating uncertainty, reducing foreclosure backlogs, creating a stable environment for private capital, and ensuring access to credit for qualified homeowners are the principles that will lead us into financial stability and economic growth.