



## What to do about Housing?\*

Jim Sivon

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It has been almost five years since the housing market collapsed. Yet, the market is still troubled. Unfortunately, the problem is multi-faceted. For consumers, the promise of home ownership as an investment has been seriously undermined as millions of existing homeowners continue to pay on mortgage loans backed by properties that are worth significantly less than the loan amount. The collapse of the housing market also has affected potential homeowners, who remain reluctant to buy on the belief that prices may continue to fall, even though it is now cheaper to purchase than rent in many markets.

Lenders, in turn, are facing significant compliance and legal costs. The large lenders that also act as servicers are facing an apparently open-ended review of foreclosure practices by the federal banking agencies, a multi-billion dollar settlement with state attorneys general over the same practices, the on-going return of mortgages by the GSEs for non-compliance with underwriting standards, scrutiny by a new fraud task force, and an ever-growing number of lawsuits from individuals and institutions that purchased mortgage-backed securities.

Added to this is the uncertainty of regulation. The federal financial regulators are grappling with the Dodd-Frank mandate to define underwriting standards for lenders (the “qualified mortgage” rule) and to set “risk retention” rules for mortgages (the “QRM” rule). These rules may not be final for months. Congress may give FHA a put-back authority comparable to the authority currently being exercised by the GSEs. And, no one expects any serious action on GSE reform until after the election.

What can be done to right the housing market? The following are some near term reforms to housing finance that would help:

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- Put the past behind us by implementing the AG settlement and putting a clear end date on the on-going foreclosure review being conducted by the federal banking agencies; this would help to establish boundaries on future litigation;
- Establish uniform mortgage servicing standards based upon the standards in the AG settlement; conflicting or competing standards adopted by different regulators serve no stakeholder;
- Expand, in an appropriate fashion, the REO to rental pilot to put those properties into use; this will not be easy, but it would help to clear the market;
- Expand, as the President has proposed, the existing mortgage refinancing program to cover all mortgages and in doing so allow borrowers to meet a wider debt-to-income ratio; also find a way to spread the cost of this program to all stakeholders and beneficiaries, otherwise it may be a non-starter in Congress;
- Set a foundation for GSE reform through a series of transitional actions that would revive private securitization (e.g., sharing the risk of GSE securities with the private sector, gradually increasing the guarantee fees charged by the GSEs, lowering loan limits for GSEs and FHA);
- Standardize the trust indentures used in private securitization;
- Include a materiality standard in the reps and warranties used by the GSEs to stop put-backs based upon immaterial changes in a borrower's status; and
- Finalize the QM and the QRM regulations.

The collapse of the housing market was a once-in-a-century event. It will take some time for individual homeowners and the economy as a whole to recover. However, the actions listed above would set a good foundation for that recovery.

*Jim Sivon is a partner with the law firm of Barnett Sivon & Natter, P.C.*