
Eminent Domain to Fix Troubled Mortgages Makes a California Comeback.

A controversial proposal to get local government officials to condemn distressed mortgages – in the same way they might condemn a dangerous property – is slowly gaining traction in some California communities, several months after it appeared the idea had been killed.

After months of contentious debate, officials in San Bernardino County, in January killed the idea of seizing troubled home loans in a process known as eminent domain. They rejected the idea after fierce opposition from Wall Street trade associations and investors in mortgage-backed securities.

But since then, San Francisco-based Mortgage Resolution Partners (MRP) has signed advisory agreements with five California towns that permit the financier-backed group to begin negotiating a sharp reduction in the dollar value of distressed loans that are held in securities administered by banks and mortgage servicing firms.

MRP's strategy is to either achieve a voluntary agreement with servicers and banks to reduce the principal owed on loans that are valued at prices higher than the homes are worth, or use the club of eminent domain to forcibly seize the loans and restructure them at a lower price.

MRP, which earns a $4,500 fee for every loan that is restructured, argues the threat of eminent domain gives municipalities, hard-hit by the housing crisis, an opportunity to help cash-strapped homeowners struggling to pay their mortgages.

But Wall Street trade groups like the Securities Industry and Financial Markets Association and the Association of Mortgage Investors argue that forcibly condemning home loans and rewriting them is a violation of contractual agreements between a bank and a borrower.

"This type of government intervention is only going to harm the housing market," said Chris Katopis, executive director of the Association of Mortgage Investors, which represents a group of about two dozen, private bond investors. "This is not a fair and equitable solution."

Chris Killian, a SIFMA managing director, said the MRP plan forces "investors to lock in a loss on a loan" by reducing the mortgage value, even if the borrower is still making payments.

MRP's most recent advisory agreement was signed on April 2 with the city of Richmond, Calif., according to public records and MRPs marketing materials reviewed by Reuters. Other California communities that have signed similar agreements with Mortgage Resolution Partners are El Monte, La Puente, San Joaquin and Orange Cove.

The group is also negotiating with officials in North Las Vegas, Nevada a community of 227,000 people that was particularly hard hit by the housing bust. In North Las Vegas, MRP has identified at least 4,700 underwater home loans, mortgages that are for more than the homes are currently worth, that could qualify under its plan.

The revival of eminent domain as a strategy for restructuring distressed mortgages comes as the U.S. housing market is showing signs of revival. But according to CoreLogic there are still an estimated 10.4 million U.S. homeowners who are underwater on their mortgages.

“It’s not a panacea to deal with the broad issue of foreclosure, but it is another tool that could be potentially effective,” said Bill Lindsay, the manager for Richmond, California, a city of 105,000 people.

The loans MRP seeks to restructure are those packaged into securities sold by Wall Street banks before the financial crisis. These private label mortgage securities do not carry a government guarantee of principal repayment, which distinguishes them from mortgage debt issued by government-sponsored mortgage firms Fannie Mae or Freddie Mac.

Loans in private label bonds are not eligible for most federal government mortgage modification programs.

Last year, private label mortgage bonds returned 21 percent, making it one of the top performing assets for bond investors, according to Amherst Securities Group. The bonds rose in value in response to the Federal Reserve’s decision to buy $40 billion in government-guaranteed mortgage debt each month and an improvement in the performance of some of loans.

Traditionally, local governments have used eminent domain to condemn blighted properties or seize land for public works projects. Wall Street trade groups have warned communities that using eminent domain to seize mortgages could spark litigation and cause lenders to be wary about writing mortgages in certain towns.

MRP, in its marketing documents, has said it has investors willing to finance the cost of condemnation so the municipalities do not have to spend any money seizing mortgages. The group has not publicly identified its financial backers.

By Matthew Goldstein

Copyright © 2024 Bond Case Briefs | bondcasebriefs.com