

# ***THE WEEKLY WHIP***

TUESDAY, JANUARY 29, 2008

## **MORTGAGES & FORECLOSURES**

As a slowing real estate market creates a drag on the national economy, foreclosures are emerging as a threat to stability in every county in the state. At the end of the second quarter of 2006, the state experienced 921 foreclosures. At the same point in 2007, the state experienced 4,092 – an increase of 3,171 or 344% in twelve months.

Maryland is 15<sup>th</sup> worst nationally based on the number of foreclosure filings per household, and the trend towards higher foreclosure rates suggests the problem has not reached its peak. Many adjustable rate mortgages taken out between 2004 and 2006 are scheduled to reset to higher rates in the coming months. The new rates will put homeowners struggling to make payments at risk of losing their homes to foreclosure.

This is a statewide problem – no jurisdiction is immune. Prince George's County had the most foreclosures, with 1,192 reported in the second quarter of 2007. Neighboring Montgomery County saw a 1679% spike in foreclosures between the second quarter of 2006 and 2007. And rural counties, like Caroline and Kent, saw triple-digit percentage increases in their year-over-year statistics.

The problem disproportionately involves sub-prime loans. Sub-prime loans are marketed towards borrowers with bad credit and others who might not otherwise qualify for a loan. They carry higher interest rates and "exotic" options, including adjustable rates, prepayment penalties or no requirement for proof of income. Between 2000 and 2007, sub-prime loans grew from 1.6% of the market in Maryland to 11.7%, and sub-prime loans accounted for nearly 60% of all state foreclosures as of the second quarter of 2007.

Increased foreclosures have led to rescue scams, wherein a con artist approaches a homeowner facing foreclosure, offers help, only to steal their equity by tricking the desperate homeowner into signing over the deed to the home. As foreclosure rates have spiked this year, so have the incidence of rescue scams.

## **THE COST OF FORECLOSURES**

The cost of foreclosures goes beyond individuals losing their homes and any equity they have built up in their property. In Maryland, the average home sold in a foreclosure sale sells for 18.8% below market value. Each foreclosure on a single-family home reduces property values within 1/8 of a mile by nearly 1%. A study of foreclosures in Chicago in 2005 estimated a single foreclosure costs city government \$5,000.

Foreclosures bring about the potential for increased violent crime. Published research shows that for every percentage point the foreclosure rate climbs in a neighborhood, violent crime in that neighborhood increases by about two percent. Moreover, vacant and neglected properties can become a target for vandalism and other criminal activities.

Finally, the lending industry has taken a hit from rising foreclosures. Lenders typically lose \$50,000 or more on a single foreclosure – the banking industry cites a figure well over \$60,000.

## **PROPOSED SOLUTIONS**

The Governor's legislative agenda includes four bills to confront the foreclosure problem head-on. Taken together, the bills will: (1) improve regulation of the mortgage industry and reform lending practices by banning pre-payment penalties for sub prime loans, assuring a borrower's ability to repay a loan and verify sources of income, and increasing the mortgage licensing requirements, (2) create a mortgage fraud statute that covers all potential actors engaged in mortgage fraud, (3) modify the Protection for Homeowners in Foreclosure Act (PHIFA), which was passed in 2005, by banning the conveyance of real property in the foreclosure rescue context, (4) reform the foreclosure process by requiring a lender to wait 90 days after default before filing the foreclosure action, and (5) reform lending practices in Maryland by tracking rates of default and foreclosure of mortgage industry professionals; and strengthening the experience requirement to obtain a license.