Keep hammer in anti-foreclosure plan

by The St. Louis Post-Dispatch

President Barack Obama's plan for preventing foreclosures and helping to stabilize the housing market is serious in scope and imaginative in approach â€” as far as it goes.

The plan, announced Feb. 18 in Mesa, Ariz., needs a hammer to force an unrepentant banking industry to make deals that protect communities and keep deserving families in their homes.

Millions of homeowners have seen their monthly mortgage payments rise to between 40 percent and 50 percent of their income, often because they signed adjustable-rate loans they could not afford. The president's plan seeks to reduce their payments to not more than 38 percent â€” and perhaps as little as 31 percent â€” of gross monthly income. He's doing this by appealing to mortgage holders' self interest:

If they give a little, they will get a lot.

Some mortgage lenders, for example, would reduce their risk of loss on loans if they refinance loans at lower rates. Other lenders would become eligible for government payments and other cash incentives if they make significant concessions in interest rates.

The idea is to reduce monthly payments enough to make them affordable, thus keeping families in their homes and keeping a glut of foreclosed homes from destroying communities and wrecking home values. And, by the way, lenders could avoid the cost of foreclosure, which generally costs more than working out a loan.

Among those who work with distressed homeowners to prevent foreclosures, there's consensus that the president's program represents a drastic improvement in the government's response to what's become a genuine crisis.

But the plan suffers from obvious limitations. It does not directly force the mortgage industry's bottom feeders off the sidelines, pushing them to make concessions on loans with predatory terms rather than pursue foreclosures.

Rather, the incentives focus more on mainstream loans and don't touch billions of dollars in "toxic" subprime mortgages bundled and sold by Wall Street as mortgage-backed securities.

This represents a huge hole in the president's plan, one that he proposes to fill by offering consumers relief under federal bankruptcy law. Lenders who won't work out loans could find a federal bankruptcy judge doing it for them.

Dan Claggett, managing attorney of Legal Services of Eastern Missouri's consumer unit, sees foreclosure cases involving sharp practices on the part of lenders â€” unsophisticated borrowers "promised one thing and receiving something else altogether."

Mortgage holders on such loans typically are defiant in foreclosure proceedings, and existing law provides little leverage to force them to make a raw deal reasonable.

Nationally, legal advocates for homeowners have been turning to bankruptcy courts to get relief for mortgage-strapped clients. But they have to work around the edges, with credit card and other consumer debt, because under current law, judges don't have the power to directly modify mortgages on primary residences.

Under Obama's plan, bankruptcy judges would get such power â€” erasing an exemption the home mortgage industry won with its enormous lobbying influence over Congress. The plan is unpopular with home mortgage holders because it would treat them like other secured creditors â€” no better, no worse.

The home lending industry is happier with the financial part of the presidents' program â€” $75 billion in direct incentives to lenders and another estimated $200 billion for purchasing or guaranteeing mortgages (mainly through Fannie Mae and Freddie Mac) â€” because it would impose only modest burdens.

The real fight is yet to come. Lenders will fight a change in the bankruptcy law tooth and nail. If Congress kowtows, it would doom thousands of deserving homeowners to foreclosures that could have been prevented.