Testimony of John Dodds,
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On Subprime Mortgage Foreclosure Prevention

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My name is John Dodds, Director of the Philadelphia Unemployment Project, a non profit membership organization that has been involved in efforts to prevent mortgage foreclosures since the early 1980s. In 2008 we are seeing a different kind of foreclosure not caused by the economic disruptions that have historically caused families to lose their homes.

Now the nation and the city of Philadelphia are in the midst of a foreclosure crisis caused by the growth and abuses of subprime mortgage lending. Nationally Wall Street analysts estimate that there will be 3.5 million foreclosures in the next three years in the United States. Many of them will be for families with Adjustable Rate Mortgages or ARMs and others high cost loans that were never affordable from the beginning.

What happened is that mortgage brokers and lenders created loan products that were unaffordable for millions of homeowners, but were sold to them in order to make quick money for those originating these loans. A major way of doing this was with Adjustable Rate Mortgages or ARMS that tend to start with an affordable monthly payment and after two or three years begin to increase by 1.5% every six months until they peak at between 10% and 13%. Payments often more than double and many homeowners had no idea that their loans who go up like that. Many of these subprime loans were sold to people that could qualify for prime loans. A recent study by the Wall St. Journal of subprime loans originated in 2006 found that 61% went to people with credit scores high enough to qualify for a conventional mortgage. Even families who didn't qualify for prime credit and were placed in "exploding" ARMS could have qualified for 30 year fixed rate mortgages for only .5 to .8 percent higher than the teaser rate they were given. Subprime lenders and brokers searched out homeowners and buyers and pressed high cost loans on them, often with terms that were hidden or that the homeowners did not understand.

Now we are starting to see the loans go bad all over the country and in Philadelphia. These loans have been concentrated in minority neighborhoods throughout the city. You can see that in many neighborhoods over half the loans made in 2005 were high cost subprime loans. These neighborhoods include East Germantown, West Oak Lane, Ogontz/Logan, SW Philadelphia, and West Philadelphia/Parkside. Large numbers of these loans have adjustable rates that will reset in 2008, very often at levels that homeowners were not expecting and will not be able to afford. We are very concerned that these subprime loans are going to result in a growing number of mortgage foreclosures all over Philadelphia with concentrations in the neighborhoods I just mentioned, but impacting all parts of the city.

This crisis is acknowledged all over the world, as it is affecting banks, investors and global stock markets. Even President Bush has made some feeble attempts to do something to stem the tide of subprime foreclosures. However, his plans will only help a fraction of the homeowners facing foreclosure and much of the announcements seem to be more public relations than an attempt at an actual solution to the massive number of mortgages that are expected to default.

The HOPE hotline the administration created took 176,000 calls in the past two months according to the Wall Street Journal. Of that number 9,975 were recommended for a work out and 4,400 were told to sell their home. 12,113 were referred to in person counseling or job placement services. That means that only15% of the calls got action. The director of the Hope Now Alliance told the Journal that she expected the numbers helped to "inch up." She said the numbers reflect "a natural progression."

The recently announced 30 day moratorium is called an incremental step by the Treasury Department and only applies to six mortgage companies and homeowners behind by at least 90 days who contact their lenders. Mark Zandi chief economist of Moody's Economy.com says that the administration plans are "likely to be overwhelmed by the eroding housing and job markets."

So we sit on a time bomb here in Philadelphia waiting for these ARMS to reset and become unaffordable while efforts to solve the problem are inching up and incremental. I was recently in Cleveland, Ohio, which is acknowledged to be a center of subprime lending and foreclosures. Cleveland is a horrible sight. Abandoned, stripped and gutted homes are all over. Property values have gone through the floor. Homes in these neighborhoods are going for $14,000 if anyone would buy them. We are not anywhere near where Cleveland is and we need to take action now if we hope to not go to where they are.

Over the past several years Philadelphia has reduced the number of abandoned properties and has cleaned up the blight in many of our neighborhoods. But what happens if foreclosures soar? One result of the subprime crisis is that mortgage money for those with less than prime credit is almost non-existent at this point. Who will be able to buy the homes sold at Sheriff Sale in West Oak Lane, Germantown, Olney, Southwest and West Philadelphia? If they aren't quickly sold we will find boarded up homes all over these and other neighborhoods and the resulting blight will destroy property values of those still able to make their payments.

We need to act before Philadelphia starts looking like Cleveland. Once these properties are foreclosed and abandoned it will be too late. If the houses are stripped, how long will they be vacant? This is why we are happy that City Council and Councilman Jones and Blackwell are pursuing this issue.

The answer to this crisis that most experts look to is for mortgage lenders and servicers to modify these unaffordable loans and make them affordable. This means to change the terms of the loans, reducing interest rates, cancelling adjustments and even reducing principal when loans are for more than the value of the property. This takes a costly foreclosure and turns it into a performing 30 year fixed rate mortgage that the homeowner can afford to make payments on. Lenders can lose up to 50% of the loan amount when they are forced to foreclosure according to a recent Wall St. Journal article. Thus, a loan modification is in the interest of the lender, the homeowner and the city of Philadelphia. In the February 12 New York Times the head of Bank of America's consumer real estate services said his bank would "certainly be willing" to consider writing off substantial portions of some mortgages. Loan mods are happening. At PUP we have been negotiating these loan modifications for some time.

The issue is how to do this at a scale to meet the tremendous numbers of loans that need to be modified in Philadelphia and all over the nation. We believe that advocates and the City and City Council need to get agreements from lenders holding subprime loans to do loan modifications at a scale sufficient to head off large scale foreclosures for Philadelphia homeowners and neighborhoods. We need a public private partnership to protect our homeowners and our property values.

<u>We need to demand that mortgage servicers agree to use the city of Philadelphia's extensive network of OHCD funded housing counseling agencies to do work outs for Philadelphia homeowners.</u> Servicers are being flooded with requests and will not be able to handle the volume needed. Only 3.5% of mortgages that have reset were modified in the 3rd quarter of 2007 according to Moody's Economy.com. Foreclosures outnumber loan modifications by 13 to one for subprime loans according to the Mortgage Bankers Association.

These non profit agencies could gather sufficient information from the homeowner to determine what a workable modification or other work out would be to resolve a delinquent mortgage without loss of the home. This would allow servicers to handle the volume of resets and defaults coming out of the subprime mortgage crisis in Philadelphia.

We would agree on a standard format to forward information to mortgage servicers from homeowners and servicers would agree to offer affordable workouts as computed by the counseling agencies. Counseling agency staffs would be trained to implement the system. We would have to work out agreeable criteria for affordable workouts and servicers could spot check forms submitted to check for improper submissions from the counseling agencies. Foreclosure actions would stop while work outs are in process.

This could be a model for the nation, a public private partnership to allow lenders to avoid the losses of subprime loans going bad and homeowners and the city avoiding the tragic consequences of large scale foreclosures. We need our elected officials to take leadership in calling for the major subprime lenders to join us in this partnership for the good of everyone. We also believe that there should be a moratorium on Sheriff's Sales in Philadelphia until such a system is in place. We look forward to working with council on this important endeavor