Foreclosure in Virginia

Presentation to the Senate Finance Committee

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Foreclosure in Virginia

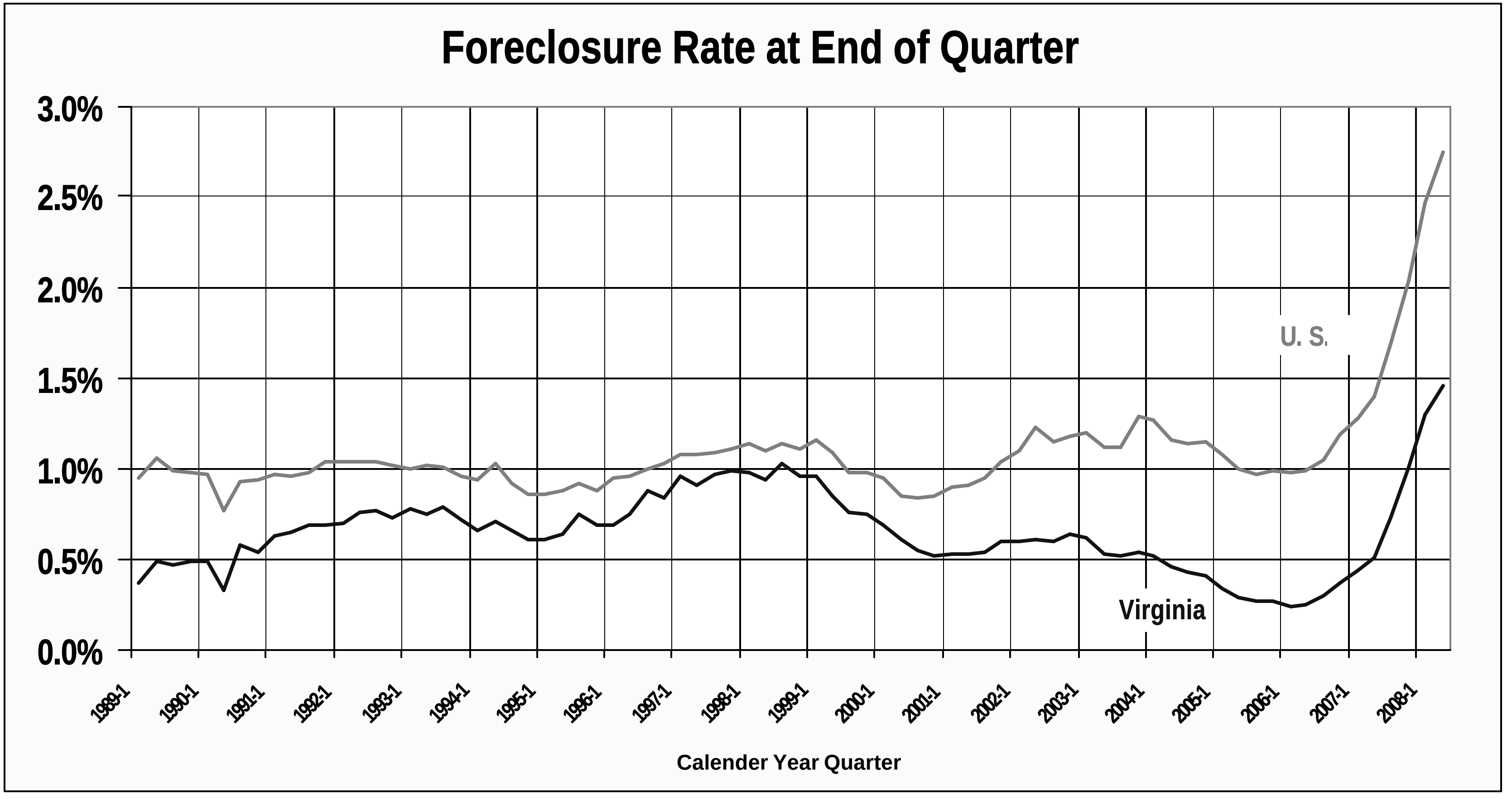
This presentation addresses:

- What data indicates about Virginia’s place in the context of the ongoing foreclosure crisis.
- How the state has responded to the crisis.
- How recent federal legislation may affect both the current crisis and future state responses.

Foreclosure in a Virginia Context

- The seriousness of the foreclosure issue is well-documented, both for today and for the immediate future.
- In early 2007, Virginia appeared relatively well-off, at least compared to such sunbelt markets as Arizona, California, Florida and Nevada and rust belt markets in Ohio and Michigan, which first experienced a wave of foreclosures, declining sales and plummeting home values.
- However, during 2007, many Virginia housing markets began to mirror national trends. While the overall foreclosure rate in Virginia approached 1.5% of all mortgages earlier this year–a little over half the national rate–the trend was definitely upward.
- Whether Virginia ranks among the top ten or top twenty states with the highest foreclosure rates is less significant than the fact that foreclosures have reached levels not seen in decades.

Virginia's foreclosure rate is much lower than the U.S. rate, but has risen rapidly since 2006.



Source: Mortgage Bankers Association (MBA)

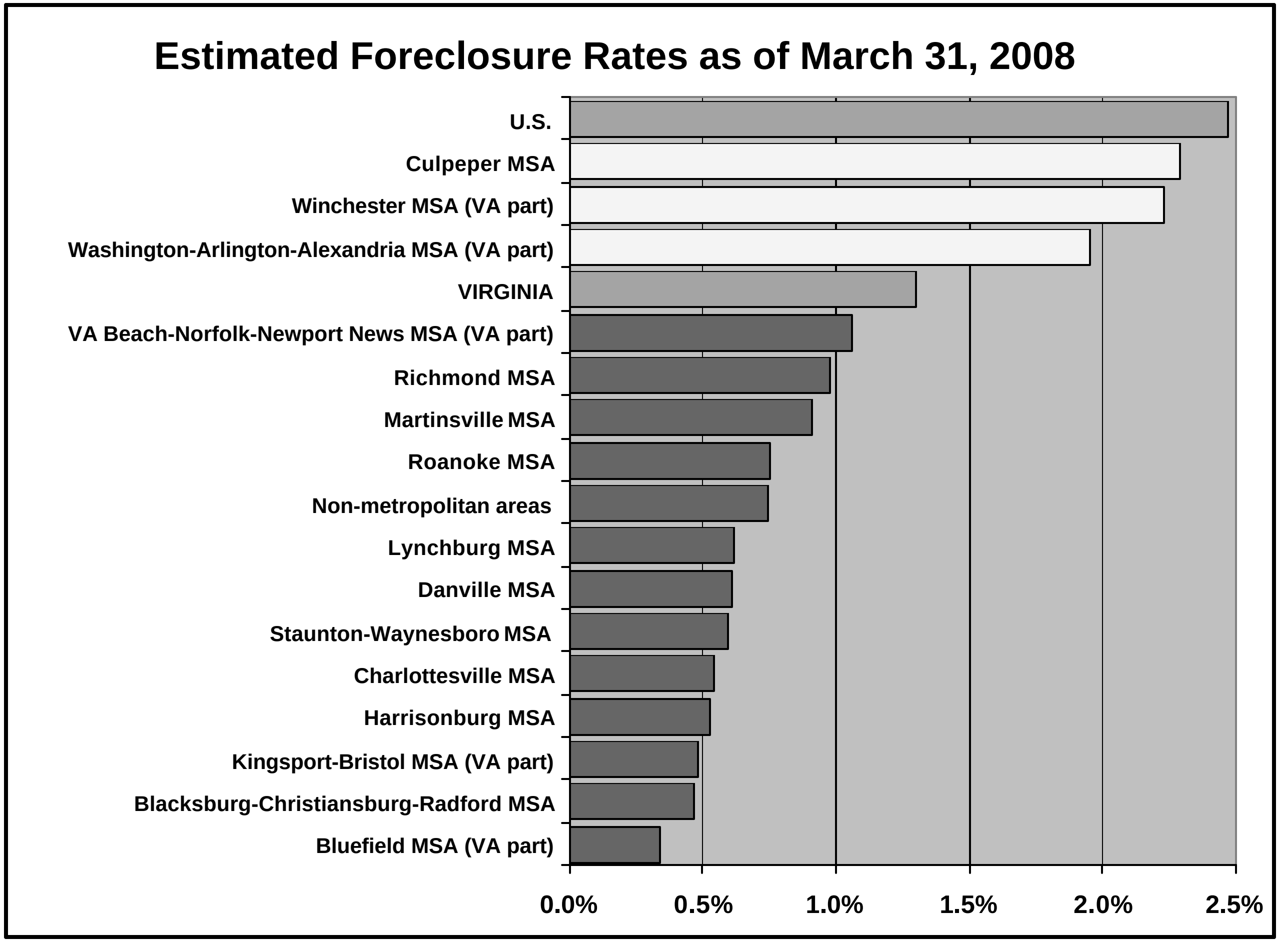
Locus of the Problem

- Foreclosures afflict every region of the Commonwealth, but there are concentrations by location, by type of mortgage, and by population sector.
- Markets that experienced the greatest price appreciation in recent years were among the first to be affected.

Where are Foreclosures Happening?

- Foreclosures are concentrated in three metro regions: Northern Virginia, Hampton Roads and Richmond. There are significant variations within these regions and within individual localities.
- In NoVA, the increase has been higher in outer ring suburbs such as Prince William, Manassas, Manassas Park or Loudoun and more exurban submarkets such as Culpeper and Winchester. By contrast, rates in inner ring areas such as Arlington, Alexandria and Falls Church have been more muted.
- In Hampton Roads, the problem has been most prevalent in the Cities of Norfolk and Virginia Beach.
- In Richmond, with the exception of a sharp increase in foreclosures in rural Caroline, the problem has largely been confined to the City and the adjacent counties of Chesterfield and Henrico.

Northern Virginia – Toughest Hit



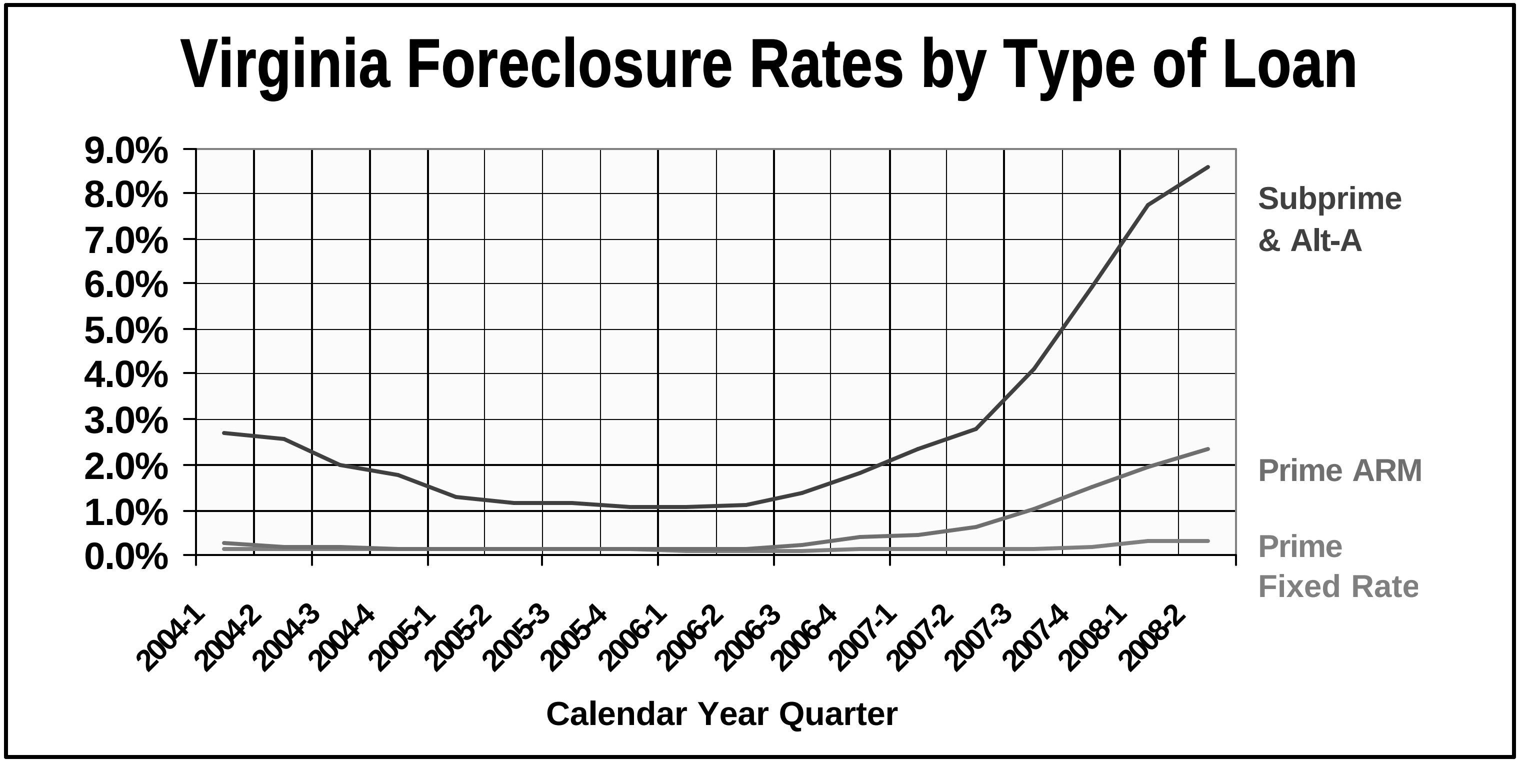
Area estimates are based on data from the MBA and First American LoanPerformance.

What Mortgages are Involved?

- Much of the current problem is associated with higher cost “exotic” or non-traditional loans. These include subprime, Alt-A (no or low-documentation) and adjustable rate (ARM) loans–or loans combining these features.
- Earlier this year, data from the Mortgage Bankers Association indicated that 58% of foreclosures represented two types of non-traditional loans–subprime and Alt-A. Another 27% were on prime and government-backed ARM loans.
- By early 2008, the foreclosure rate for Subprime and Alt-A loans in Virginia was four times the rate for prime ARMs and almost twenty times greater than the rate for prime fixed rate mortgages.
- These loans were often associated with high loan-to-value ratios fueled by the expectations of both lenders and borrowers that an early refinance would be possible thanks to continued rapid appreciation in home values in hot markets.

The Problem is Primarily with Higher Cost, Non-traditional Types of Loans

Virginia's foreclosure rate has increased sharply since mid-2005. The rise is attributable to poorly performing subprime, Alt-A, and adjustable rate loans.

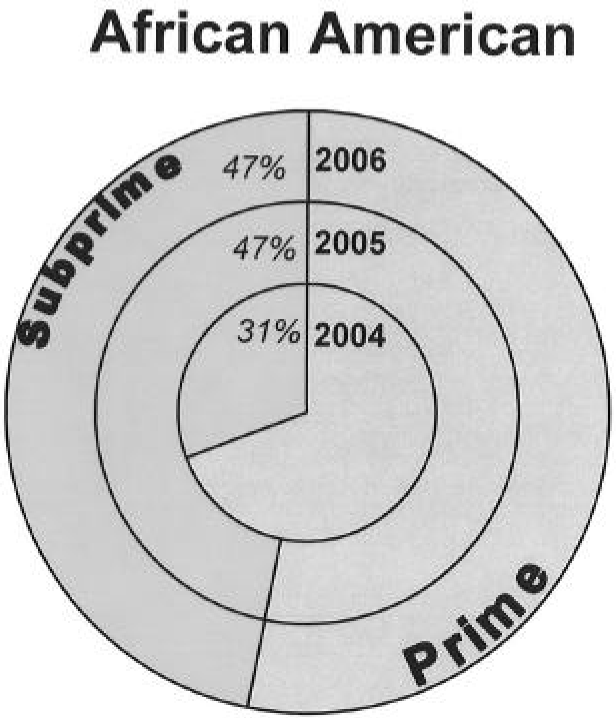


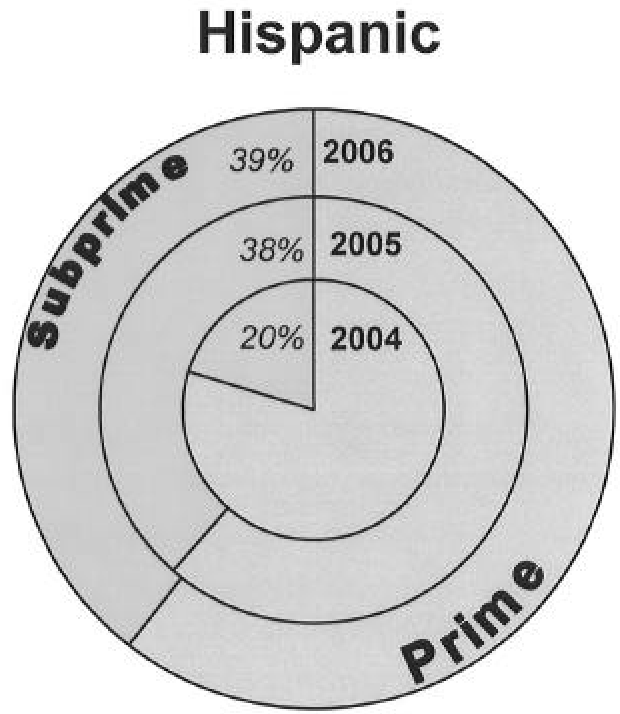
Source: Mortgage Bankers Association (MBA)

Which Borrowers are Affected?

- Minority home purchasers–primarily, but not exclusively, African American and Hispanic–were increasingly dependent on more costly and riskier mortgage products beginning in 2005.
- Areas of concentrated foreclosures in Northern Virginia such as Loudoun, Prince William and Stafford Counties and the Cities of Manassas and Manassas Park were not only a focal point for foreclosures but also among the localities with the fastest growing minority populations in the U.S.
- The geographic distribution of foreclosures in other markets also suggests that minority borrowers were heavily affected.

Which Borrowers are Affected?





Prospects for Recovery

- The current crisis grew out of the combined effects of a worldwide glut in credit availability, lax lending standards, some outright fraud and mendacity, and the unrealistic expectations of homeowners respecting the future financial performance of housing.
- The prolonged downturn in housing now turns many of these mutually reinforcing conditions on their head. Contractions in global credit, more stringent lending standards, efforts to regulate previously non- or lightly-regulated aspects of the mortgage industry, and the sober realization by homeowners that values can fall–especially where there is a glut of foreclosed property–all contribute to the downturn that is still playing out.

Remain Uncertain

- The sub-prime ARM portion of the crisis will likely have run its course by mid-2009, but initial interest rate resets for Option Adjustable Rate and Alt-A products will not peak until 2010 or 2011.
- Recovery will not be secure until prices have fallen sufficiently to boost home sales. Upticks in home sales, which have already appeared in some local markets in NoVA, will be an important indicator of change.
- The possible effects of a recession or near recession on jobs and employment, continued turmoil in financial markets, and the sheer volume of foreclosed properties in some local markets will continue to threaten a broad housing recovery and increase the possibility that some prime borrowers will default.

Steps to Recovery

- The down spiral is not likely to end before equilibrium returns to housing markets.
- The President and Congress, the Federal Reserve, the Treasury Department and, in Virginia, the Governor and General Assembly, have all acted to address different aspects of the crisis–with an eye toward restoring equilibrium.

Steps to Recovery

The Foreclosure Prevention Task Force

- Governor Kaine created the Task Force by Executive Order in November 2007.
- Secretary of Commerce and Trade, Patrick O. Gottschalk, chairs this 21-member body representing a wide array of affected parties with a stake in the future of Virginia's housing, including:
  - consumers
  - mortgage bankers
  - homebuilders
  - realtors
  - local governments and non-profits
- The Task Force called on the resources not only of the state's housing agencies, but also the Federal Reserve Bank of Richmond, HUD, and experts in housing finance, real estate, and other relevant disciplines from across the state, the southeast and the nation.

Steps to Recovery

The Foreclosure Prevention Task Force

- The Task Force had four major functions:
  - Locate and analyze data to determine the needs of homeowners and affected communities.
  - Identify resources that could minimize the number of foreclosures occurring in Virginia.
  - Provide a source of outreach, counseling and education that support foreclosure prevention.
  - Review existing laws and regulations related to foreclosure.

Steps to Recovery

The Foreclosure Prevention Task Force

- To accomplish its purposes, the Task Force established three workgroups to focus on specific issue areas:
  - Foreclosure Impact - monitor economic, social and fiscal impacts and assess their effects on families, neighborhoods and communities and identify emerging issues.
  - Education and Outreach - reduce the number of homeowners affected by foreclosure by increasing their knowledge of available options and overall financial literacy, enhancing housing counseling efforts, and promoting loss mitigation best practices.
  - Regulatory Reform - forestall future foreclosure problems by reviewing relevant existing laws and regulations to identify areas where adjustments may be needed.

Steps to Recovery

The Foreclosure Prevention Task Force

- Recent Accomplishments:
  - Training for 239 new Foreclosure Mitigation Counselors statewide.
  - Extensive education/outreach efforts including PSAs in English and Spanish via television, cable, radio and print media.
  - Hosting education and outreach mortgage clinics for distressed borrowers, which attracted 848 attendees and led to 668 individual counseling sessions.
  - With the cooperation of the Richmond Fed, creating a comprehensive assessment of the incidence and locale of foreclosures in Virginia.
  - Identifying the concerns of local governments and communities through focus groups and by sponsoring a Foreclosure Impact Summit.
  - Assisting in the allocation of funding provided in the budget for foreclosure counseling services.

Steps to Recovery

The Foreclosure Prevention Task Force

- Legislative Efforts
  - Facilitated the passage of SB 797, which provided eligible homeowners facing foreclosure with breathing room to explore workout options with lenders.
  - Supported other consumer protection legislation that addressed foreclosure rescue scams (HB 408) and began the process of closing gaps in the regulation of mortgage brokers (HB 1487).

Steps to Recovery

The Foreclosure Prevention Task Force

- Looking Forward
  - Continue to monitor the impact of foreclosures on neighborhoods and communities.
  - Continue to foster opportunities for counseling and outreach to homeowners facing foreclosure.
  - Follow the effects of recent federal housing legislation as it addresses regulatory reform, housing finance, foreclosures, and the mitigation of the impact of concentrated foreclosures on neighborhoods and communities.

Steps to Recovery

HR3221: The Housing and Economic Recovery Act of 2008

- The new law addresses three major issue areas:
  - housing finance reform
  - foreclosure prevention
  - tax related provisions
- Each area contains one or more provisions that could influence state decision–making over the next year that directly affects the environment for housing in Virginia. It creates potential new opportunities *and* responsibilities for state agencies such as DHCD, VHDA and the SCC.

Steps to Recovery

HR3221: The Housing and Economic Recovery Act of 2008

Housing Trust Fund Features:

- Contingent on their capitalization, the GSEs (Fannie Mae and Freddie Mac) must set aside 4.2¢ of every $100 in total new business starting in 2009.
- From 2009-2011, 25% of the funds are to be deposited in the Treasury Department’s HOPE for Homeowners Program (the FHA refinance program for qualifying borrowers).
- Of the remainder,
  - 65% is to be transferred to the new HUD Housing Trust Fund
  - 35% is to be transferred to a new Treasury Department Capital Magnet Fund
- However, in 2009, all of the remaining assessments are to go to the Hope Program; in 2010, 50% will go to that purpose; and in 2011, 25%.

Steps to Recovery

HR3221: The Housing and Economic Recovery Act of 2008

Housing Trust Fund Features

- Highly targeted funding to low-income households (<50% of area median)
  - Up to 10% for ownership activities for very low-income first-time homebuyers
  - At least 75% of rental spending must benefit very low-income or poverty level families
- Distribution to the states based on a multifactor formula to be established next year that addresses the shortage of affordable housing for extremely low-income and very low-income households as well as housing quality and cost burden factors.
- The formula will be adjusted to reflect the ratio of each state's construction/ rehabilitation costs to the national average.
- Each state and D.C. to receive at least a $3 million allocation annually.
- Each state may designate an entity/instrumentality to receive and administer the grant in accordance with an allocation plan it prepares, after public notice, hearing and comments.

Steps to Recovery

HR3221: The Housing and Economic Recovery Act of 2008

Housing Trust Fund Features

- At least 80% of grant must be used for rental housing production, preservation, rehabilitation and operating costs.
- Up to 10% can be used to produce, preserve and rehab housing for sale to first-time homebuyers.
- The initial price cannot exceed HOME purchase limits (95% of median purchase price as adjusted by HUD) and units are subject to HOME resale restrictions.
- Buyers must complete an approved homebuyer education course.
- States may use up to 10% of the allocation for administration costs.
- States may allocate grant funds to qualified sub-recipients.

Steps to Recovery

HR3221: The Housing and Economic Recovery Act of 2008

- ***Reform of the Mortgage Origination System***
  - In addition to initiatives focused on the GSEs, the bill also seeks to bring greater uniformity and accountability to the mortgage origination business.
  - States will have one year to bring their regulation of the origination business and of individual originators into line with new federal standards.
  - States that fail to act or at least show adequate progress toward the creation of adequate state regulation could then be preempted by HUD.

Steps to Recovery

HR3221: The Housing and Economic Recovery Act of 2008

- **Foreclosure Prevention**
  - **The *Neighborhood Stabilization Fund*** authorizes a HUD program of grants to states and units of general local government for the purchase, management, and resale of foreclosed and abandoned properties.

Steps to Recovery

HR3221: The Housing and Economic Recovery Act of 2008

Neighborhood Stabilization Program

- HUD will allocate $3.92 billion in FY2008 allocated as grants to states and units of general local government according to a formula to be established by late September of this year based on:
  - home foreclosures
  - homes financed with a “subprime mortgage related loan”
  - homes in default or delinquency

Steps to Recovery

HR3221: The Housing and Economic Recovery Act of 2008

Neighborhood Stabilization Program Features

- State and local grantees must give “priority emphasis and consideration” to metro areas, metro cities, urban areas, low- and moderate-income areas, rural areas and other areas with greatest needs in distributing their portion of the funding.

Steps to Recovery

HR3221: The Housing and Economic Recovery Act of 2008

Neighborhood Stabilization Eligible Activities

- Provide financing mechanisms for the purchase and redevelopment of foreclosed residential properties (e.g., soft-seconds, loan loss reserves, shared-equity loans for LMI homebuyers).
- Purchase and rehabilitate abandoned or foreclosed homes, residential properties for sale, rent or redevelopment.
- Establish land banks for foreclosed homes and demolish blighted properties.
- Redevelop demolished or vacant properties.

Steps to Recovery

HR3221: The Housing and Economic Recovery Act of 2008

Tax Related Provisions

Because federal tax policy plays such a large role in shaping U.S. housing markets, the housing bill also made significant changes in a number of areas with the intent of facilitating home sales and the production or preservation of affordable rental housing.

- ***Low-Income Housing Tax Credits:*** The bill revised provisions of the existing tax credit program and the tax-exempt bond program with the intent of more easily meshing the use of LIHTC and other federal housing activities.
- ***Temporary Tax Credit for First-time Homebuyers:*** The bill created a refundable tax credit of up to $7,500 (subject to a fifteen year repayment schedule) for first-time homebuyers who purchase between April 9, 2008, and July 1, 2009. It also allows non-itemizers to claim at least a portion of their real property taxes via a standard deduction.

Steps to Recovery

HR3221: The Housing and Economic Recovery Act of 2008

Tax Related Provisions

- ***Tax-Exempt Bonds (MRB) :*** Temporarily (for 2008 only) increase the national cap on Private Activity Bond Authority by $11 billion and allocate the new capacity increase to the states based on population.