

FORECLOSURE CRISIS MAY WELL BE CATASTROPHIC IN ANY CASE

John Cole asks a bunch of questions about what a foreclosure moratorium would accomplish.

I just don't understand what good would come from a national moratorium. Forty state AG's are on the ball, what exactly could a national moratorium do? **The idea is to stop the bad foreclosures, not grind every single transaction in this sector to a damned halt.** You aren't hurting the banksters when you do something like that. You're hurting every single buyer and seller in the market. **It would be catastrophic.** On top of that, under what legal authority does the White House declare a moratorium on a specific type of business transaction? How would that happen? Who would be in charge of it? Geithner? Warren? Under what legislative or Constitutional authority? [my emphasis]

At the start, let me say two things. First, I am a buyer and seller at the moment—a pretty cranky one about being in this limbo as this shit hits the fan, to say nothing about already losing 1/3 of the value on the house I'm selling (though I have the luxury of being in a month-to-month apartment, which means I would be less screwed by a moratorium on the purchase side). Second, I don't think I—or anyone else—knows what the least bad solution to this problem is going to be.

But I do suspect it's probably going to be catastrophic in any case.

John frames this as an issue of stopping bad foreclosures. But that's not the problem, not by

half. The problem is that the problems exposed by foreclosures in judicial states are problems that exist throughout mortgages that were securitized in the last 6-10 years. The reason the servicers are going to such lengths to make up for deficient paperwork—including robo-signing affidavits or counterfeiting notes—is presumably because for at least a significant portion of mortgages that were securitized, the paperwork is not in order. What we're seeing through the foreclosure process is just what is getting exposed through the random sampling of foreclosure, and any other random sampling of securitized mortgages would presumably have the same level of deficient paperwork.

Perhaps the best description of the stakes comes from that hippie publication, CNBC. It suggests the problems being exposed by the foreclosure process are probably systemic, affecting a good portion of mortgages securitized in the last six to ten years (or more). Which means it's not entirely clear who owns a good percentage of the housing stock in the United States, which could set off a free-for-all among those trying to resolve that question.

So with the chain of documentation now in question, and trustee ownership in question, here is one legal scenario, according to Prof. Levitin:

The mortgage is still owed, but there's going to be a problem figuring out who actually holds the mortgage, and they would be the ones bringing the foreclosure. You have a trust that has been getting payments from borrowers for years that it has no right to receive. So you might see borrowers suing the trusts saying give me my money back, you're stealing my money. You're going to then have trusts that don't have any assets that have been issuing securities

that say they're backed by a whole bunch of assets, and you're going to have investors suing the trustees for failing to inspect the collateral files, which the trustees say they're going to do, and you're going to have trustees suing the securitization sponsors for violating their representations and warrantees about what they were transferring.

Keep reading, if you have the stomach, for the suggestion that this could be worse than the Lehman bankruptcy if—as some think—every single loan written during this period was written without the proper endorsements.

This may well be catastrophic whether or not there's a moratorium on foreclosures until such time as people start admitting what's going on.

If that's true (and as I said, I don't really know, but that seems to be the obvious implication of all the fraud that was going on), then the question is, **which catastrophe is going to be least bad for the American people? And which catastrophe best preserves the rule of law and property—the bedrocks of our country? Do we enter this catastrophe on the banksters' terms, or on more equalized terms?**

As I said, I can't say I know the answer to that; I doubt anyone does.

But I believe one reason to halt foreclosures is because the current default state in foreclosures gives banks an advantage over homeowners. What banks claim in non-judicial states is assumed to be accurate, which puts homeowners who would want to challenge their foreclosures at a big disadvantage. That's a problem in any case, but particularly given the mounting evidence that the paperwork underlying these mortgages may be questionable. The best

way to fix that power imbalance is to halt foreclosures until it's clear foreclosures have some kind of paperwork to justify a foreclosure.

It's also a matter of admitting precisely what the problem is. When David Axelrod first announced the Administration position—admitting the seriousness of this but not supporting a moratorium—he said, “‘there are in fact valid foreclosures that probably should go forward’ because their documents are accurate.” But that endorses the claim that the banks just got sloppy with some foreclosure paperwork not with **mortgage** paperwork through the process of securitization more generally. The truth is, David Axelrod doesn't actually know whether those foreclosure or mortgage documents are accurate, because no one yet knows the extent of the underlying problems with the documents.

And the ability to frame the issue, at this point, is the ability to control the timing of how this unravels. If it's true the issue is the underlying mortgage paperwork and not just the foreclosure paperwork, then the framing that happens now will affect whether we deal with this catastrophe based on a one-page proposal over a panicked weekend (as we did in fall 2008), or whether we start planning for the best way to unwind a gigantic rupture to our system of private property. It will affect whether we, as a country, get input into the way to deal with the catastrophe created by the banksters, or whether the banksters and a few Administration officials do so in private. It will affect whether we get to impose some conditions on the banksters before we bail them out this time, or whether the real people continue to bear the burden of the banksters gambling.

And then there's the question of what happens to these foreclosures in the market (and as I said before, I'm in the market). Granted, I'm a pretty news-savvy buyer. But whereas, as recently a month ago, I considered short sales and even foreclosures, at this point I'm looking

skeptically at anything that might have been sold in the height of securitization. Either foreclosures should be regarded skeptically at this point, or peoples' realtors aren't informing their clients of the risks they should be. But if you're putting foreclosures on the market that buyers **should** regard skeptically, you're not helping anyone; because they're just going to lower property values for all properties, whether or not they're on the market.

And then there's the issue of the President's authority to do something about this. As DDay suggested, there's the possibility that the regulators (Office of Thrift Supervision or Office of the Comptroller of the Currency, for example) would impose a moratorium. Or, as Alan Grayson has requested, the government could (and probably should) declare this a systemic risk, which gives them the authority under Dodd-Frank to do what they need to do to protect our system. That doesn't make it legally or (especially) politically easy to declare a moratorium (as the deepwater drilling Obama imposed makes clear). But once you regard this as an issue that may affect securitized mortgages more generally (and not just some foreclosures), then the claim that this may be systemic seems fair.

Now, as I said, I can't say I know more than anyone but the banksters.