Foreclosure Crisis Demands Congress Take FDR Approach

by Nancy Spannaus

With the U.S. housing foreclosure crisis hitting levels unseen for decades, leaving millions of families vulnerable to losing the roofs over their heads, Congressional leaders pulled together a special hearing on July 25 to discuss the topic. The Joint Economic Committee hearing was called by Sen. Charles E. Schumer (D-N.Y.), with a specific focus on the impact of the subprime mortgage lending crisis on what he called "one of the hardest-hit communities in the nation—Cleveland, Ohio." Testimony was presented by five witnesses from the Cleveland area, including Hon. James Rokakis, treasurer of Cuyahoga County; Hon. Anthony Brancatelli, Cleveland City Council; Mrs. Audrey Sweet, resident of Maple Heights; Ms. Barbara Anderson, resident of Slavic Village; and Kenneth D. Wade, CEO of NeighborWorks America.

The hearing succeeded in providing a sensuous picture of the disaster which predatory lending practices in the housing sector have created for low-income families and local governments in urban centers. If anything, it understated the disaster that looms nationally. An estimated 1.7 million Americans will lose their homes over the next year when adjustable rate mortgages reset, according to an analysis by Moody's Economy.com reported in the Aug. 1 *New York Times.*

An Inadequate Response

But the hearings' failure was in not providing guidelines on how Congress should act to reverse this process, which can only get worse, if its root causes are not addressed.

References were made in the course of the hearing to some of the legislative measures which have been put on the table, in response to the crisis. In nearly all cases, these measures avoid the reality that caused the disaster: the fact that housing has become an object of insane speculation, without regard for the need to provide decent affordable housing for the nation's citizenry. It is this reality, the current *housing system*, which has to be changed.

Specifically, as Lyndon LaRouche has emphasized, Congress has to *throw out* all of the deregulation measures which were adopted for the housing sector, from the 1960s forward. After declaring a national economic emergency, Congress has to reorganize the banking system, including declaring a moratorium on foreclosures, in such a way that the huge speculative bubble based on mortgages is effectively wiped off the books, and such speculation is outlawed in the future. Then, as part of an overall banking reorganization, mortgages on owner-occupied homes should be *written down* to a reasonable level. Congress should then authorize a regulated Fannie Mae to act as President Franklin D. Roosevelt's Home Owners Loan Corporation did, to purchase from the banks and other institutions these rewritten mortgages, while bridge loans, at very low interest rates, are provided to homeowners who need such aid in order to stay in their homes.

More could be said about what specific measures are needed,* but the overall point should be clear: The foreclosure crisis is but a *symptom* of the bankruptcy crisis of the dollar-based world financial system, and cannot be solved independently of dealing with that bankruptcy crisis. Either an FDR-style approach is taken, including wiping out trillions of dollars of unpayable debt, or so-called ameliorative measures will do nothing but pour monies down the drain—into doomed financial institutions.

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* See "Put the Toothpaste Back in the Tube: Rebuilding FDR's Dedicated Lending System for Housing." *EIR*, July 27, 2007.

Documentation

Senate Hearing on Crisis: 'Cleveland Under Siege'

Excerpted here is the opening statement of Sen. Charles Schumer (D-N.Y.) at the Senate Joint Economic Committee Hearing, July 25, 2007, which was titled "A Local Look at the National Foreclosure Crisis," with the subtitle "Cleveland Families, Neighborhoods, Economy Under Siege from the Subprime Mortgage Fallout."

Subheads have been added.

I would like to welcome my fellow Committee Members, Sen. Sherrod Brown, our witnesses and guests here today for this very important hearing on a problem that is plaguing too many families and communities across the nation—the subprime foreclosure crisis.

The numbers are staggering and getting worse.

Consider these statistics:

• The Center for Responsible Lending estimates that as many as 2.4 million families may ultimately lose their homes to the subprime foreclosure crisis, at a cost of $164 billion in home equity.

• In June alone, foreclosure tracker RealtyTrac counted 165,000 new foreclosure filings, more than double the amount recorded in June 2005.

• From June to October of this year, $100 billion of risky subprime adjustable rate mortgages are scheduled to reset in a weak housing market, many of which are likely to default and lead to further foreclosure increases.

• One in five subprime loans originated in 2005 and 2006 will end in a lost home.

These numbers are not the manifestation of a housing market "correction," as the administration's economists have argued. These facts are not merely the byproduct of a period of bad decision making among a select few over-eager borrowers. These shocking figures are a result of widespread, systemic, irresponsible underwriting practices by too many unscrupulous brokers and lenders that now are threatening the social fabric and economic well-being of our nation's neighborhoods and towns.

And worst of all, this subprime foreclosure crisis is just beginning. I know it is hard to imagine that it could get worse from here, but it will. The wave of foreclosures that we have seen to date does not include the vast number of risky "exploding" adjustable rate mortgages that were originated in 2006. Once these loans start resetting this Fall and into next year, we can expect to see hundreds of thousands more families lose their homes.

And when this foreclosure storm subsides, it will have left a net loss of homeownership in its wake.

I called this hearing today for two main reasons:

First, I fear that the cries for help from the millions of real people trapped in bad subprime loans today are getting drowned out by the headlines of investor woes, collapsing hedge funds, and lower-than-expected earnings from lendees.

And while every city in America is in this together, I chose to focus on the families and neighborhoods of Cleveland, like Slavic Village, that are being decimated by subprime foreclosures. Slavic Village is a harbinger of the crisis that is unfolding in cities across the nation; and I hope that by investigating the human toll of unscrupulous lending up close, we can better prepare to prevent more Slavic Villages from emerging in the near future.

Learning the Lessons of the Present

Second, I am afraid that we are not learning the lessons of the present. I fear that this problem is beginning all over again right under our noses, with predatory lenders preying on those very families already in danger of losing their homses—this time, with the promise that they are rescuing them from foreclosures.

We're reading in the headlines that lenders are tightening underwriting guidelines, and that some have even banned certain types of risky loans. Yet the data examined by the Center for Responsible Lending show otherwise. At the June hearing I held on the Housing Subcommittee that I chair, CRL testified that many of the most recent offerings of mortgage-backed securities still included harmful prepayment penalties and stated income or low documentation loans, and nearly 80% of the mortgages were still risky adjustable rate loans!

The witnesses that we have here testifying for us today are at the epicenter of the subprime lending storm. The testimonies that you will hear tell a story of fraud, corruption, greed, negligence, and heartbreak.

Our witnesses will also inform us about an important side of this issue that is rarely discussed—the ways foreclosure impacts not only the families that own the homes, but their neighbors, their communities, and their local governments.

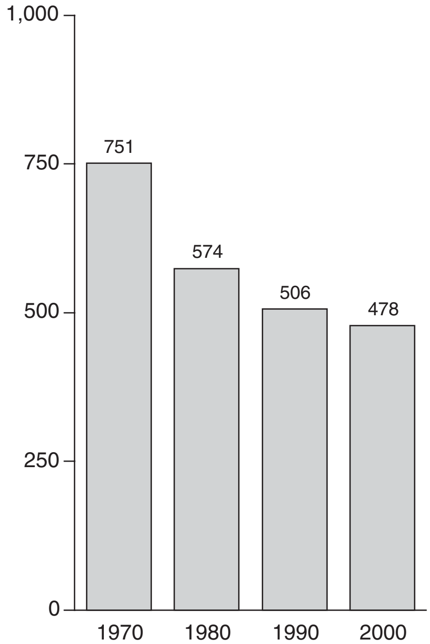
We never hear, for example, that one foreclosure on your city block can bring down your home's value by 1.5%, even if you have never missed a payment on your own mortgage. In neighborhoods like Slavic Vallage outside of Cleveland, where over 1,000 homes are currently foreclosed and vacant, community leaders like Councilman Tony Brancatelli and residents like Barbara Anderson—both of whom are here today—are grappling with lost property values in the area of $60 million. Just think about that. $60 million of financial security that the families in this one community were relying on has disappeared.

And lower property values means lower tax revenues for

FIGURE 1

Cleveland: Population Falls by 36%

(Thousands)

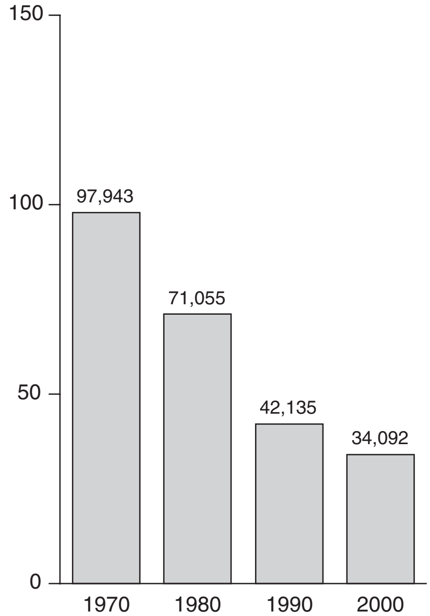


Source: Dept. of Housing and Urban Development; *EIR*.

FIGURE 2

Cleveland: Manufacturing Workforce Falls by 65%

(Thousands)

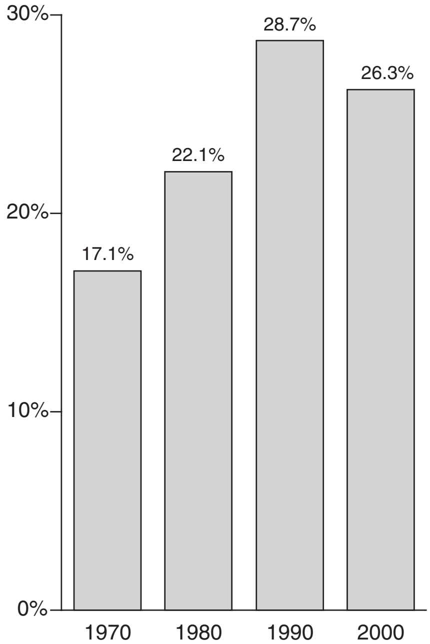


Source: Dept. of Housing and Urban Development; *EIR*.

FIGURE 3

Cleveland: Poverty Rate

(Percent)



Source: Dept. of Housing and Urban Development, *EIR*.

The collapse of the city of Cleveland as a major industrial urban center, shown here, has helped create the conditions for the current housing disaster, in which an impoverished population cannot afford to maintain their mortgages, and fall victim to predatory lenders.

local governments at a time when the demands on them are already too high. County treasurers like Jim Rokakis here with us today now have fewer resources for their schools, their local law enforcement, and for important public services such as those that can help these imperiled homeowners.

This is not a problem that is going to go away when the market corrects itself—the subprime mess is leaving deep scars that threaten economic security nationwide, whether in urban neighborhoods like those in St. Louis and Baltimore, suburbs like Massapequa on Long Island, or entire regions like Greater Cleveland.

'We Cannot Afford Inaction'

We cannot afford inaction. To do nothing means that hundreds of thousands more families will lose their homes and their primary source of economic security. To do nothing means that millions of other homeowners will see the value of their homes plunge through no fault of their own. And to do nothing means that we will be permanently handicapping communities for years to come, which will have widespread repercussions for our economy.

We don't have time for endless debate about the causes of this crisis. We need to help families everywhere, including those sitting in this room, who are struggling with foreclosures today. And we need stronger, common-sense regulations, to prevent a flood of risky or abusive subprime loans rushing into the vacuum that the current crisis has created.

To help stem the surge of foreclosures expected in the months ahead, Senator Brown, Senator Casey, and I are fighting for increased resources for nonprofit groups in the trenches of the foreclosure prevention fight. We have succeeded in getting $100 million of funding for HUD-approved foreclosure prevention programs in the Senate Transportation-HUD Appropriations bill, and we will fight to make sure that this important resource is made available to the many organizations, like NeighborWorks and ESOP here with us today, that are providing an invaluable service to help struggling borrowers keep their homes.

Another goal that Senators Brown, Casey, and I share is to create a national regulatory structure for mortgage brokers and other originators that fall through the cracks of the complex federal and state regulatory agencies.

In April, we introduced a strong bill, The Borrowers Protection Act, to make it harder for irresponsible brokers and non-bank lenders to sell mortgages that are designed to fail the homeowner and result in foreclosure.

Our ultimate aim is to strengthen standards for subprime mortgages by regulating mortgage brokers and all originators under the Truth in Lending Act (TILA) by establishing on behalf of consumers a fiduciary duty and other standards of care. In addition, the bill outlines standards for brokers and originators to assess a borrower's ability to repay a mortgage, requires taxes and insurance to be escrowed on all subprime loans, and holds lenders accountable for brokers and appraisers.

We look forward to hearing from all of our witnesses today. . . .

Cleveland Activist: 'A Devastating Decade'

These are excerpts from testimony by Barbara Anderson, a Cleveland resident, and the treasurer of the Predatory Lending Action Committee of Empowering and Strengthening Ohio's People (ESOP), which was formerly known as the East Side Organizing Project, a community organization that originated in the southeast side of Cleveland.

. . . ESOP's model is different from most, if not all, other foreclosure prevention counseling agencies. Chief among those differences is that we combine direct action organizing in order to secure an agreement with our loan counseling efforts. Indeed, the secret to our success is direct action organizing to secure written agreements that, most importantly, designate one specific person empowered to negotiate and change the loan terms to keep a family in their home.

Since 2001 when we began keeping track, ESOP's agreements have kept more than 2,500 people in their homes. For 2007, to date, we have assisted more than 400 families and are bracing for the "October Surprise" that will actually hit in January 2008.

I want to spend a few minutes and give you a sense of just how devastating the last decade has been due to the regulators abdicating their responsibility and abusive lenders entering the market place. The following statistics were put together by Paul Bellamy, a fair housing expert in Cleveland. They paint a very grim picture. Consider:

• Ohio's foreclosure rate is three times the national average and the highest of all states.

• Data from 12 of the 13 largest Ohio counties indicate that 2006 foreclosure filings increased by an estimated 25% over 2005, with an estimated 80,000 foreclosure filings.

• The volume of foreclosures is expected to grow much faster in 2007 and 2008 because of the number of subprime ARM [Adjustable Rate Mortgage] loans that will be reset at much higher rates. In 2005, subprime loans accounted for about 13% of the mortgages issued nationally, compared to almost 28% (more than double) of the mortgages issued in Ohio. Subprime loans account for 18% of all outstanding Ohio mortgages currently held by the secondary market and other loan servicers. Despite representing less than one of five outstanding mortgages, subprime loans account for 70% of all foreclosures.

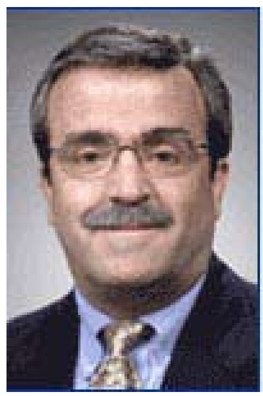
• The most common type of Ohio subprime mortgage is a "2/28" loan. These loans are sold with low initial "teaser rates" that are fixed for the first two years. Beginning in year three, the interest rate increases as often as every six months, so the monthly payment grows dramatically. Often, these loans are not underwritten to anticipate the inevitable rate escalation. In 2007 and 2008, roughly $14 *billion* of these 2/28 subprime loans are going to reset in Ohio, impacting some 150,000 to 200,000 mortgages.

• Many borrowers with 2/28s and other ARMs can't refinance or sell to avoid default because their property is not worth what is owed. All too often, their original mortgage was based on an inflated appraisal. In 2006, six of Ohio's eight major metropolitan areas experienced depreciating real estate values between 3.5 and 7.7%—well above the U.S. average of 2.7%. . . .

Interview: Jim Rokakis

Home Foreclosures Slam Formerly Industrial Cleveland

Mr. Rokakis is treasurer of Cuyahoga County, Ohio. Marcia Merry Baker interviewed him on July 26.



EIR: What you testified to the Joint Economic Committee of the Senate yesterday, was about the situation in Cuyahoga County, in Cleveland, which is in the forefront of the national home foreclosure crisis. Would you summarize some of the dimensions which you have been pointing out?

Rokakis: Let me give you some benchmarks. In 1995, there were 3,300-plus private mortgage foreclosures filed in Cuyahoga County. By 2000, the number had doubled to over 7,000 private mortgage foreclosures. Last year, in 2006, there were over 13,600. This year we're on pace to do 17,000.

EIR: Mr. Brancatelli, the Cleveland city councilman who testified yesterday, said that in his particular neighborhood, it is running something like two per day.
Rokakis: Look, there are 300 to 350 auctions every Monday here in the Sheriff's office. I don't know what his particular statistics are, but it's not surprising, since his is one of the hardest-hit districts in town.

EIR: What happens? What are you seeing in terms of evictions, people out on the street, vacant lots? You're seeing scrambling for housing. Some of the properties were bought for rental, some are where people were still trying to live?
Rokakis: I would say that half of them—and it's anecdotal, we're not really sure, it could be a little more—but, roughly half of these are purchased by people who thought they could get rich in real estate. They saw giant loopholes in the system that allowed them to buy property without downpayment; that allowed them to buy property in spite of the fact that they had no credit; that allowed them to buy property without documenting their income.

It not only did all of that, but it even gave them cash back at the close. So it was like manna from heaven!

"I'm poor. I have nothing. You'll let me buy a house? With no credit check, with no proof of income? And you'll give me money back at the sale? At the closing?"

Big surprise that people did it by the thousands. You could blame them. We could blame the poor. We could talk about the fact that they need to make better economic decisions. But we've got to stop blaming the poor, and we've got to look at the system that enabled Wall Street to pour hundreds of billions of dollars into this market. Money that didn't belong to them. Hedge fund money. Money that came from pensions, or whatever the source. And look at the damage it caused.

EIR: In your written testimony yesterday, you advised the Senators, "Don't buy the argument of the Federal Reserve Bank that the market will correct itself. . . ." This goes along with what you are saying now.
Rokakis: That's been the thing all along. Look, they had the authority of the Ohio Homeowner Protection Act of 1984. They had authority under the Truth in Lending Act, Regulation Z. The Fed has had authority for a long time to do something about this, and they've looked the other way.

What they did do, is keep interest rates low for a long, long time. They created all this liquidity, and then stood by and watched these banks make these incredibly bad decisions. And Wall Street, you know, was part of the game: "How do we securitize this, and spread the risk out?" With these investment trusts and residential mortgage back securities—they thought they'd created the perfect model. They could democratize credit, give everybody a loan, and nobody would lose.

A huge mistake.

EIR: And now the bubble is popping.
Rokakis: That market's down today, what—300 points or more?

I hope Bernanke is right and that it's *only* $100 billion. I think it's wishful thinking. I think the losses will be a multiple of that number.

It's not just subprime lending. It's also the fact that we have, in this country, encouraged people to strip equity from their homes. You might argue that in the last four or five years, we have been living on borrowed money. It's been equity that people have taken out of their properties, always believing that the property and the real estate value would appreciate, and if worse came to worst, they could always sell the property and get out.

Well, now that the market is falling, and now that values are dropping—in some cases, into the basement—the combination of their first mortgage debt, and their home equity loans, well exceeds the value of their property.

EIR: You have quantified that some for Cuyahoga County, right? It's multi-millions.
Rokakis: We know that just in terms of the amount of money they loaned Argent Mortgage—we estimated that it's roughly $30 million of negative equity—this is money loaned in excess of the value of the property.

What kind of company would make loans that go bad at the rate of one in four, in the first three years? Who would do that kind of business?

EIR: That characterizes the whole country in the bubble.

In your multi-county area, is there discussion among lawmakers, county treasurers, and others, of emergency policy? The Federal response so far—and it's often bipartisan, like Senators Stabenow and Voinovich—has been to ask for tax relief, and this and that. But we have a systemic crisis here.
Rokakis: Actually, this is only helping us to resolve one of the problems. The reality is that you have to rein in this industry. They've proven they can't be trusted. They've proven they're not going to play by the rules. They can talk around this, and over this, and through this, but at the end of the day, you are going to have to codify some of these reforms, because otherwise, they'll continue to make no-document loans; they'll continue to make loans that look the other way on issues involving value; they are going to continue to make loans to people with poor credit. I just think they'll continue to make loans with no regard to whether the person they're making the

loan to has the ability to make good on the loan—not just at the initial teaser rate, but at the fully indexed rate. We could talk about this until we're blue in the face, but they'll continue to make loans where the broker claims to be the borrower's friend and trusted ally, where in reality, the broker is trying to make the very best deal he can to hurt the borrower, by putting him into a loan that is more than he can pay. Because there's a reward for them at the other end.

EIR: If you reined these practices in, what about dealing with the situation of housing and the need for Federal emergency action to help? There is the precedent from the 1930s. Frankin Roosevelt had the Home Owners Loan Corporation?
Rokakis: There's a role for government to play in this, and they're not playing it. I think that what we have to recognize is that the democratization of credit—by making money available to everybody—has been a failure. It hasn't worked.

So, let's be honest. Not everybody can be a homeowner. We sure think it's a great idea. Everybody should own a home some day; but not everybody is ready. To continue to perpetuate this myth is going to be cruel and costly and devastating to our country.

So let's clean this mess up, and then focus in on things like quality rental housing and creating programs that give people a fighting chance at making that monthly mortgage payment. And not putting them into a payment they can't afford, into a loan that they're likely to fail on.

EIR: You've been treasuer in Cuyahoga County for ten years, what about the context—
Rokakis: The context is that nobody was home in Ohio on the regulation side. Because nobody was home, they did what they could get away with.

EIR: Your area has had such an outflow of people, such a loss of steel and other industry—on a belt running from Buffalo to St. Louis, with Cleveland and your county right in the middle, so that you have been hit hard. Your city functions, your tax base has taken a tremendous hit.
Rokakis: Yes it does impact the tax base. At one time, for example, Cleveland was a big, booming city. Half of the property taxes collected in this county in 1965 came from the City of Cleveland. The city has declined so drastically, that last year, the city's share of my total tax collections for the county dropped to 17%.

EIR: So here is the reflection of the dramatic de-industrialization of the economic base.
Rokakis: It's the decline of the cities. The decline of cities is not an Ohio-only phenomenon.

EIR: No. You're representative. Cleveland probably had the most generalized high living standard, 40 years ago, of all the industrial belt.

Fifty-Year Program Inspires Denmark

by Our Copenhagen Bureau

This Fall, an infrastructure commission appointed by the Danish government has to present a list of major infrastructure projects that should be considered for the coming 30 years. Meanwhile, the Danish Schiller Institute—which during the past year has distibuted three programmatic newspapers in runs of 50,000 copies each (in a population of 5.5 million), with the demand that the pessimistic/hedonistic "68er" culture be replaced with big infrastructure projects and a Danish maglev network—is gathering support for transforming the infrastructure discussion from "what are the next repair projects to be undertaken" to a comprehensive 50-year development perspective, based on building three major bridge projects, along with the first parts of a Danish maglev network, over the next decade. That would mean tripling the annual Danish infrastructure budget.

In the aftermath of the recent agreement to build the Fehmarn Bridge (*EIR*, July 20, 2007), an intense public debate has taken place regarding the need to investigate a 46-km Kattegat bridge project linking Zealand directly with Jutland via the island Samsø. All the major newspapers have been discussing the possibility of combining this with the first Danish high-speed train route to connect the two biggest cities, Copenhagen and Århus. This discussion is now broadened to include the general lack of investment in rail and road infrastructure in recent decades.

Present Plans Are From 1936

On July 15, the biggest Danish newspaper, *Jyllands-Posten* (*JP*), had a feature on how Danish road traffic is jammed up due to lack of long-term planning and investment. The paper outlined how the evolution of the Danish highway system has followed a script from 1936, when the so-called H-plan was proposed. It involved highways going north-south in Jutland and Zealand, with a connecting highway over Fyn completing the H. The plan included the Great Belt Bridge, the Fehmarn Bridge, and a bridge to Sweden. The time has now come, the article argued, for putting a new vision on the table for development of the highway system.

On July 17, *JP* had a second feature, accompanied by an editorial, on the sad state of affairs for the Danish railroads. The feature reported that while other European countries are building high-speed rail, sections of the Danish railroads are slower today than they were 40 years ago—simply due to lack of investment. The next day, *JP* reported figures from the Union of Construction Engineers that Denmark would have

to invest 100 billion crowns (about $17 billion) over the next 30 years—simply to keep the rail system functioning. A more ambitious policy, improving the railroad, would require 200 billion crowns.

The traffic policy spokesmen for the various political parties were then interviewed. Magnus Heunicke from the opposition Social Democratic Party thought that those 200 billion crowns had to be spent, while the Social Liberal Party thought 100 billion for 20 years would be more reasonable. The government parties, on the other hand, wouldn't even consider that amount of money for rail infrastructure. The traffic spokesman for the Liberal government party added, that he thought high-speed trains would be irrelevant for a little country like Denmark. The worry in the government is whether the present limited infrastructure budget should be spent on improving the railways or the highways. The solution to that paradox is, of course, to change the underlying flawed axioms and massively expand the Danish infrastructure budget—a change that, with the present budget surplus, seems like an obvious thing to do.

Op-Ed by Schiller Institute's Gillesberg

That point was brought home in an op-ed entitled "Bridges Are the Foundation for the Next 50 Years Infrastructure," by Tom Gillesberg, the chairman of the Schiller Institute in Denmark, in *Jyllands-Posten* on July 30. The Schiller Institute, which operates internationally, was founded by Helga Zepp-LaRouche. The prominently placed op-ed calls for a visionary 50-year perspective, and *JP* highlighted a quote: "The task which the Infrastructure Commission and the Danish politicians are faced with is to decide the overall visionary plan which can lay the basis for the development in the next 50 years. A foundation which can be completed piece after piece, and further built upon." This is the second recent op-ed *JP* has printed by Gillesberg. The first one was on the need for a Danish maglev network, which was prominently published on June 21.

After referring to *JP*'s series on the lack of long-term planning, Gillesberg continues, under the subhead "Maglev": "Therefore, it is important to choose the right foundation. In a little more than ten years, the Great Belt Bridge and the Øresund Bridge [both now in use] ought to have been supplemented by a series of new bridges: the Kattegat connection, the Fehmarn Bridge, and a bridge between Helsingør and Helsingborg. These three projects, which have to be built anyway, should be completed as fast as possible, so the coming infrastructure projects can be planned accordingly.

"At the same time, we have to build a brand new rail connection between Århus and Copenhagen via the future Kattegat link, which gives us a unique chance of establishing the first part of a new Danish high-speed rail network. This should be a maglev train connection between Copenhagen and Århus, which with a speed of 500-600 km/h would make it possible to traverse the distance between the two cities in 25 minutes, and thereby replace the car as the Danes' preferred means of transportation. The maglev net will then, of course, be expanded nationally and internationally, and over time will also come to play a major role in freight transport. We will be first with the new, instead of being the last with the old!"

The op-ed also argues, that even though Denmark, with the building of a maglev network, will avoid having to spend fortunes on trying to transform an outdated railroad to a high-speed rail network that would have to be replaced by maglev in the coming decades anyway, we still will have to spend significant amounts on improving existing, neglected rail infrastructure. All in all, we will have to triple the combined annual budget for infrastructure spending, compared with what has been the rule the last two decades. That, however, is not a frightening proposition. Such an investment will, as the result of increased productivity and creation of wealth, return with compound interest. With the building of the maglev and those three new bridges, there is a vision for Danish infrastructure development to further build on.

Gillesberg ends by stating that "other infrastructure projects should fit into this larger plan, with the Kattegat/maglev project as the rotation point for the next 50 years, and therefore the starting point for the work the Infrastructure Commission and Danish Parliament will take up after the Summer break."