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SENATE REPUBLICAN POLICY COMMITTEE

Legislative Notice

No. 51 April 3, 2008

H.R. 3221 – New Direction for Energy Independence (a Shell for a Dodd/Shelby Substitute Amendment Concerning Foreclosure Prevention)

Calendar No. 340

H.R. 3221 was read twice and placed on the calendar on September 5, 2007.

Noteworthy

- On April 1, 2008, the Senate invoked cloture on the motion to proceed to H.R. 3221 by a vote of 94-1.[1] At 9:30 a.m. today, the Senate began consideration of the bill and the text of a Dodd/Shelby agreement regarding foreclosure prevention was offered as a complete substitute.
- In December 2007, housing starts fell to their weakest level since May 1991. As a whole, housing starts were down 24.8 percent in 2007, representing the second largest decline on record, exceeded only by a greater decline in 1980. Home prices saw a decline of 8.9 percent in the final quarter of 2007, representing the largest year-to-year drop in the 20-year history of the index.
- Despite the fact that foreclosures have been primarily limited to subprime ARMs, this issue is affecting the economy. In response, Congress, the President, the Federal Reserve and private industry have all taken action.
- The Dodd/Shelby substitute includes:
  - $10 billion in tax-exempt private activity bond authority to refinance subprime loans and to provide mortgages to first time homebuyers;
  - $100 million in pre-foreclosure counseling;
  - $4 billion for the Community Development Block Grant (CDBG) program to purchase and rehabilitate foreclosed properties;
  - $1.63 billion for a $7,000 tax credit (paid over 2 years) to purchasers of foreclosed properties (a scaled back version of Senator Isakson's bill, S. 2566);
  - $6.054 billion to extend the carryback period for net operating losses (NOLs) from two years to four years for NOLs arising in tax years 2008 and 2009;
  - Federal Housing Administration (FHA) modernization, including a $550k conforming loan limit and a 3.5 percent down payment requirement; and
  - Enhanced Truth in Lending provisions.

[1] The first cloture vote on the motion to proceed to the measure took place February 28, 2008; cloture was not invoked by a yea-nay vote of 48-46. Record Vote Number 35.

Background/Overview

While the U.S. economy continues to grow, the economy is no longer enjoying the robust growth it enjoyed over the past several years. The economy grew at an anemic 0.64 percent in the fourth quarter of 2007. Despite a relatively low unemployment rate (4.9 percent), economists are predicting a further slowdown in the short term.

The view of the economy is shared by consumers. Brought on by less favorable business conditions and job prospects, consumer confidence has been slowly declining since July 2007 and declined sharply in February, to its lowest reading since February 2003.[2] Another measure of consumers' view of the economy, the expectations index, has fared even worse, declining to a 17-year low earlier this month.[3]

The economic outlook has no doubt been affected by the increase in consumer prices. In 2007, led primarily by the increase in the cost of gasoline and food, consumer prices increased by 4.1 percent, their fastest rate in 17 years, on top of a 2.5 percent increase in 2006. At the same time however, weekly wages failed to keep up with inflation.[4] Over the past 12 months, wholesale prices have risen by 7.5 percent, which is the fastest increase since the fall of 1981 when the country was in recession.[5]

The housing market has also suffered. December 2007 housing starts declined by 14.2 percent, falling to their weakest level since May 1991.[6] As a whole, housing starts were down 24.8 percent in 2007, representing the second-largest decline on record, exceeded only by a greater decline in 1980. After 14 years of rising home prices, the housing market saw a decline, according to Standard & Poor's/Case-Shiller home price index. Home prices saw a decline of 8.9 percent in the final quarter of 2007, representing the largest year-to-year drop in the 20-year history of the index.[7]

Despite these short term declines, not all housing data is negative. According to the Census Bureau, homeownership rates were still near an all-time high at the end of 2007. Nearly 75.2 million homeowners, or 67.8 percent of households, are living in homes they own.[8] Of the families living in owner-occupied homes, nearly one-third (or 24 million) own their homes free and clear of any mortgage indebtedness while two-thirds (51 million) of homeowners have a mortgage.[9]

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[2] http://www.conference-board.org/economics/consumerConfidence.cfm See also, *Associated Press*, "Job Worries Sink Consumer Confidence," February 26, 2008. The Consumer Confidence Index fell to 75 in February 2008 from a revised 87.3 in January. This was the lowest reading the index has had since it was 64.8 in February 2003.

[3] *Associated Press*. The expectations index measures consumers' outlook over the next six months. The index dropped to 57.9 from 69.3 in January. The index has not registered this low since 55.3 in January 1991.

[4] *Associated Press*, "Gas, Food Spur Inflation Jump in 2007," January 16, 2008.

[5] *Associated Press*, "Wholesale Prices Jump in January," February 26, 2008.

[6] Breitbart.com, "US Housing Starts Plunge 14.2 Percent," January 17, 2008. Housing starts fell to an annualized level of 1.006 million properties, down from the forecast of 1.150 million units.

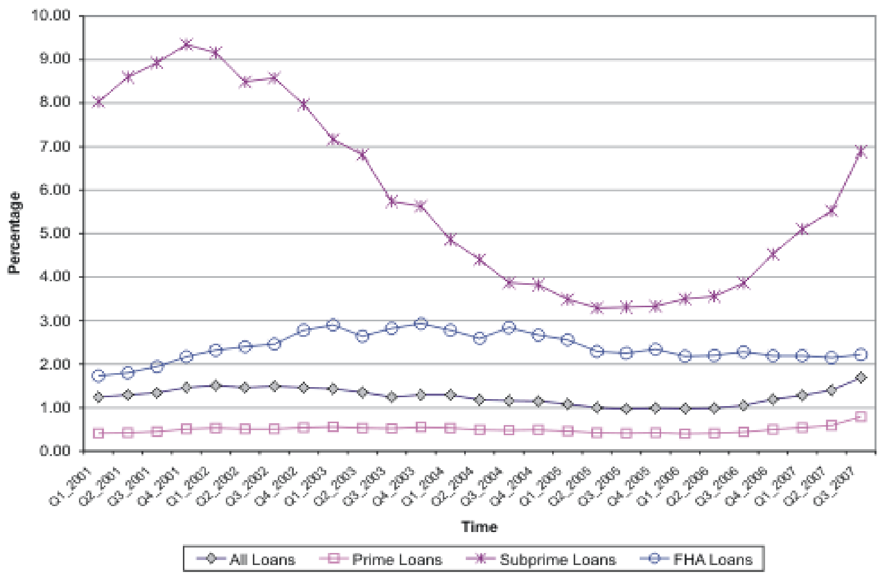
[7] *Los Angeles Times*, "U.S. Home Prices End 2007 With Record Drop," February 27, 2008.

[8] Census Bureau's Housing Vacancy Survey, January 29, 2008. http://www.census.gov/hhes/www/housing/hvs/qtr407/q407press.pdf

[9] Census Bureau's 2006 American Community Survey.

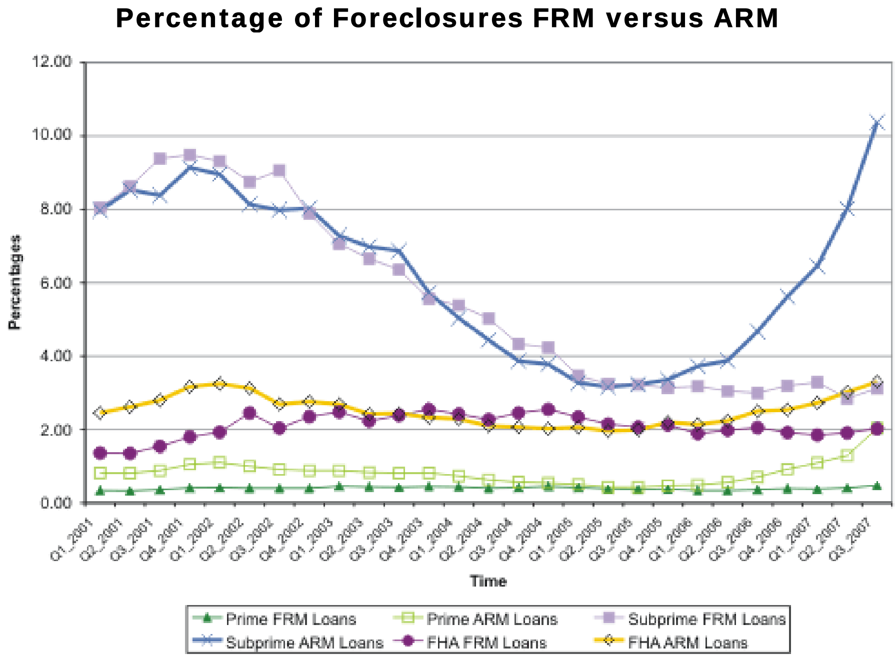
The Mortgage Bankers Association's tracking of 41 million mortgages shows that foreclosures among prime loans and Federal Housing Authority (FHA) loans has stayed relatively constant from the beginning of 2001 through the Third Quarter of 2007. Data shows that the slight increase in foreclosure rates is due in large part to the rise in foreclosure rates with subprime loans (a rate which is still lower in Q3, 2007 than it was at any point from Q1, 2001 through Q1, 2003).[10]

Percentage of Foreclosures by Aggregate Category



Additional data shows that among subprime mortgages that are in default, the increase in foreclosures is a result of subprime adjustable rate mortgages (ARMs). The foreclosure rate among subprime fixed rate mortgages (FRMs) has actually been in decline since 2002.

[10] Congressional Research Service (CRS), "Understanding Mortgage Foreclosure: Recent Events, the Process and Costs," CRS Report for Congress RL34232, January 14, 2008.



Despite the fact that the increase in foreclosures is predominately limited to subprime ARMs, foreclosures are impacting the economy as a whole. In response to the slowdown in the economy, Congress, the President, industry, and the Federal Reserve have all taken action. The collective response from the federal government includes:

- Multiple reductions in interest rates by the Federal Reserve;
- Enactment of H.R. 5140, the original stimulus bill, which raised the conforming loan limits for FHA, Fannie Mae, and Freddie Mac;
- Enactment of H.R. 3648, which became law on December 20, 2007, and extends mortgage insurance premium deductibility for three years and makes mortgage loan forgiveness non-taxable for a three year period;
- Proposal of Home Ownership and Equity Protection Act (HOPEA) regulations by the Federal Reserve, consisting of strong new regulations under HOPEA to greatly improve underwriting standards and protections for mortgage borrowers, regulations which will be finalized this spring; and
- Agreement by the private lending industry to participate in the HOPE NOW program (an effort to reach out to borrowers and offer assistance), and to participate in Project Lifeline (a targeted industry effort to reach out to seriously delinquent homeowners to offer a pause in the foreclosure process). Six major lenders, representing 50 percent of the mortgage market, are working with borrowers to help them stay in their homes under these programs.

State and local governments have also taken steps to assist borrowers who are in default. Many of these efforts, however, have been met with some resistance from citizens who view this assistance as a "taxpayer bailout." For example, in Seattle, a city with a relatively modest foreclosure problem, the city's plan of a $5,000 loan for people in danger of losing their home was met with opposition.[11] A loan program in Massachusetts, which allowed for loan

[11] *New York Times*, "Foreclosure Aid Rising Locally, as Is Dissent," February 26, 2008.

refinancing with bond revenue, was also met with public resistance. MassHousing, the quasi-state agency that was running the program, had to engage in a public-relations effort to assure citizens the effort was "not taxpayer funded." Commentators have stated that programs which involve "government intervention could reward irresponsibility and make markets unpredictable."[12]

Bill Provisions

This notice summarizes major provisions of the Dodd/Shelby complete substitute, an amendment dealing with foreclosure prevention.

Housing Provisions

Housing Counseling Resources. The substitute increases pre-foreclosure counseling funds by $100 million. These funds will be distributed by the Neighborhood Reinvestment Corporation by the end of 2008. In the FY 2008 omnibus appropriations bill, $180 million was appropriated for pre-foreclosure counseling and that money has not yet been spent. Approved housing counseling agencies include, but are not limited to, Urban Leagues, ACORN, and Catholic Charities.

FHA Modernization. Under the substitute, the FHA loan limit is increased from 95 percent to 110 percent of area median home price with a cap at 132 percent of the GSE limit (currently, $550,000). Downpayments of 3.5 percent will be required for any FHA loan. The substitute also contains enhanced counseling requirements.

Emergency Assistance for the Redevelopment of Abandoned and Foreclosed Homes. The substitute adds an additional $4 billion to Community Development Block Grants (CDBG) to purchase and rehabilitate foreclosed properties.

Enhanced Mortgage Disclosure. The substitute expands the types of home loans subject to early disclosures (within three days of application) under the Truth In Lending Act (TILA), including refinancings. The substitute requires that disclosures be provided no later than seven days prior to closing. The substitute requires a new disclosure that informs borrowers of the maximum monthly payments possible under their loan, and also increases the range of statutory damages for TILA violations from the current $200 to $2000 to $400 to $4000.

Additional Foreclosure Forgiveness for Veterans. The substitute lengthens the time a lender must wait before starting foreclosure from three months to nine months after a soldier returns from service and also provides returning soldiers with one year of relief from increases in mortgage interest rates. In addition, the Department of Defense is required to establish a counseling program to ensure veterans and active service members can access assistance if facing financial difficulties. Also included is a provision that increases the VA loan guarantee amount, so that veterans have additional homeownership opportunities.

[12] *New York Times.*

Tax Provisions

Expansion of Mortgage Revenue Bonds. The substitute provides an additional $10 billion of tax-exempt private activity bond authority to be used to refinance subprime loans, and provide mortgages for first-time homebuyers and multifamily rental housing. The proposal also exempts interest earned on the bonds from the alternative minimum tax.

Homeownership Tax Credit. The substitute allows taxpayers who purchase, as their principal residence, homes upon which foreclosure has been filed pursuant to the laws of the state a $7,000 non-refundable tax credit claimed ratably over two tax years. The credit is available for purchases made within one year of the date of enactment.

Non-Itemizer Tax Deduction. The substitute allows property owners that do not itemize to claim an additional standard deduction for the amount of local property taxes paid subject to a $500 and $1,000 cap. Under present law, itemizing taxpayers may deduct the full amount of local property taxes paid from their federal tax return. The relief would not be available if the local jurisdiction increases taxes after April 2, 2008 and before December 31, 2008.

Net Operating Loss (NOLs) Carryback. The substitute extends a law allowing corporations to apply excess net operating losses to tax returns from prior profitable years and receive any applicable refunds. For 2008 and 2009 losses, the provision extends the "net operating loss (NOL) carryback" to four years (back to 2004 and 2005, respectively) from the two years currently in law. Measures to prevent companies from abusing the intent of the provision are also included.

Administration Position

The Statement of Administration Policy (SAP) for the Dodd/Shelby substitute was not available at press time.

Cost

At press time, there was a cost estimate for the tax title of the substitute - $10.848 billion over 10 years. No other costs estimates were available.