

## **The Housing and Economic Recovery Act of 2008: Summary of Federal Response to the Foreclosure Crisis**

President Bush signed the Housing and Economic Recovery Act of 2008 (the “Act”) into law on July 31<sup>st</sup> after dropping a veto threat. The Whitehouse steadfastly opposed a provision in the legislation providing local governments with \$3.92 billion to buy, repair and sell foreclosed properties. The compromise version allows states and local governments to use these authorized funds on establishing a range of financing mechanisms to reoccupy or redevelop foreclosed upon homes or residential property without actually having local governments purchase them. This Act has several other components aimed at providing economic stimulus to the housing sector and, thereby, stimulating the broader economy.

The impasse between the president and Congress over how best to deal with the problems in the mortgage credit markets and in residential construction was overcome when the Treasury Department was able to obtain modifications in the bill authorizing Treasury to provide financial liquidity to the nation’s key mortgage credit institutions – Fannie Mae and Freddie Mac – should that become necessary in the coming year. The provision gave Treasury the authority through 2009 to purchase stock in either company or extend either of them additional credit, and also increases the federal debt ceiling to accommodate use of that authority.<sup>1</sup>

Fannie Mae and Freddie Mac own or guarantee approximately half the nation’s mortgage loans and their capacity to buy mortgages from lenders and repackage them for sale to investors as debt-backed securities is essential to maintaining the flow of credit in the mortgage market. In recent months the share of new mortgages either owned or guaranteed increased to 70 percent. If these government-sponsored enterprises are unable to fulfill their core function, mortgage credit comes to a standstill and the collapse of the housing and construction sector would likely follow. Such a collapse would not only have severe consequences for the U.S., but also for the global economy. The risks associated with either or both institutions facing serious financial difficulty led the Treasury and the U.S. Federal Reserve Bank to take measures to restore investor confidence in both institutions.<sup>2</sup>

The major components of the Act directly affecting the residential mortgage foreclosure crisis are Title IV, Division A – Hope for Homeowners – and Title III, Division B – Emergency Assistance for the Redevelopment of Abandoned and Foreclosed Homes. Hope for Homeowners establishes an FHA program to help distressed borrowers avoid foreclosure through federally insured refinanced loans on principal residences and also includes measures that support long-term and sustainable homeownership. Participation in the program is voluntary for borrowers and lenders, and requires: 1) waivers of prepayment penalties or fees on existing loans; 2) elimination of second liens; and 3) that the new loan carry a fixed interest rate for a term not less than 30 years and not exceed 90 percent of current appraised value. Increases in the property’s value must be shared with the federal government as a condition of participation in this program. The number of homeowners who will likely participate in this program, however, is uncertain in light of all the conditions that must be satisfied and the difficulty of negotiating voluntary agreements with all concerned parties.

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<sup>1</sup> The federal government took control of both companies on September 8<sup>th</sup>, placing them under government conservatorship. The conservatorship is similar to a corporate bankruptcy reorganization and the management of both companies have been replaced.

<sup>2</sup> The conservatorship established on September 8<sup>th</sup> will keep both Fannie Mae and Freddie Mac operating normally until the next president and Congress restructure the operations of both companies.

The final legislation included a provision that authorizes funding through the U.S. Department of Housing and Urban Development (USHUD) to assist states and units of local government with the redevelopment of abandoned and foreclosed upon homes and residential properties. Title III requires the Secretary of Housing and Urban Development to allocate \$3.92 billion in funding to states and local units of government according to a formula that considers number and percentage of: 1) home foreclosures in a state or local unit of government; 2) homes financed by a subprime mortgage related loan; and 3) homes in default or delinquency. Miami-Dade County is likely to receive a considerable share of the total funding available given the extent of the foreclosure problem in the County, although a greater emphasis in the final allocation formula on actual numbers of foreclosures and residential mortgages in delinquency or default rather than on the percentages of homes or mortgages in these categories will result in higher funding levels for Miami-Dade. USHUD has indicated that their allocation decisions will be announced on September 26<sup>th</sup> and local governments will then learn if they will receive their funding allocation directly from USHUD or if instead it will come through their respective state governments. Since Title III requires that funding allocations be used within 18 months of the award, large cities and counties have requested that USHUD make allocations directly to eligible cities and counties.

The broad legislative language in Title III describes the eligible uses of these funds as: 1) establish financing mechanisms for purchase and redevelopment of foreclosed upon homes and residential properties, including such mechanisms as soft-second, loan loss reserves, and shared-equity loans; 2) purchase and rehabilitate homes and residential property that have been abandoned or foreclosed in order to sell, rent or redevelop such properties; 3) establish land banks for homes that have been foreclosed; 4) demolition of blighted structures; and 5) redevelop demolished or vacant properties. A coalition of large cities and counties that include Miami-Dade, have asked USHUD to interpret these eligible uses broadly so that local governments may formulate strategies and policies that best address the foreclosure problem according to the specific characteristics of their communities. Local governments are expecting greater specificity regarding eligible uses when USHUD issues its official program notice at the end of September.

Assistance provided through Title III is limited to households whose incomes do not exceed 120 percent of Area Median Family Income (AMI) as calculated by USHUD.<sup>3</sup> Title III also requires that 25 percent of the allocated funds be targeted to benefit low income households with incomes at 50 percent or less of AMI. Reliance on providing rental housing opportunities will almost certainly be necessary to serve low income households with Title III funds.

Title III also authorizes \$180 million to the Neighborhood Reinvestment Corporation to fund counseling organizations that provide foreclosure loss mitigation counseling services (Section 2305). This authorization includes \$80 million that was made available in prior legislation. The additional \$100 million in funding will be available through December 31, 2008. Under Title IV of Act, these funds are intended, in part, to: 1) support referral

**Table 1. 2008 USHUD Income Limits\* for Miami-Dade County**

Family Size	<= 50% AMI	<= 120% AMI
1	\$21,110	\$50,640
2	\$24,100	\$57,840
3	\$27,150	\$65,160
4	\$30,150	\$72,360
5	\$32,550	\$78,120
6	\$34,950	\$83,880
7	\$37,400	\$89,760
8	\$39,800	\$95,520

\* Income limits as of February 25, 2008 and subject to change by USHUD

<sup>3</sup> Area median family income in Miami-Dade County for FY 2008 is \$49,200 according to HUD. The 120 % income threshold for a family of four is \$72,360. See Table 1 for USHUD AMI threshold limits for Miami-Dade in FY 2008. The FY 2009 income thresholds will likely be higher than those in 2008.

and information services to at-risk borrowers; 2) connect distressed borrowers with approved counseling agencies that will assist them in working out a positive resolution to their mortgage delinquency or foreclosure; and 3) facilitate or offer free assistance to homeowners to understand their options, negotiate solutions, and find the best resolution to their particular situation. Thirty million dollars of the increase in grant funding is directed to USHUD approved counseling intermediaries for the hiring of attorneys to assist homeowners with legal issues directly related to the homeowner's foreclosure, delinquency or short sale.<sup>4</sup>

There are two other important provisions of the Act. The first may help alleviate the foreclosure crisis in the near term, while the second supports expansion of low income housing over the longer term. The first of these provisions is Section 3021 of the Act – *Temporary Liberalization of Tax Exempt Housing Bond Rules*. Section 3021 grant state and local housing financing agencies authority to issue an additional \$11 billion in tax-exempt mortgage revenue bonds before the end of 2010. Capital raised from those bonds may be used to refinance *qualified* subprime mortgages, and, thereby, allow borrowers who are under the financial strain of adjustable rate mortgages to refinance to fixed rate loans with more affordable terms. These refinancing mortgages are limited to single family homes.<sup>5</sup> The increase in the tax exempt mortgage revenue bond caps had been sought by local housing finance authorities to provide them with a tool to address the foreclosure crisis in their communities, but the legislation also allows these housing finance agencies to use this additional capital for their traditional mortgage programs (e.g., first time homebuyers). The additional \$11 billion bonding authority will be distributed to each state in proportion to its 2008 allocation prior to this supplemental authority.

Section 1338 of the Act supports the expansion of low income housing by establishing the Affordable Housing Trust Fund that will be financed through a 0.042 percent fee levied against the outstanding principal balance of new loans in the portfolios of Fannie Mae and Freddie Mac.<sup>6</sup> The Trust will be funded beginning in 2010 with projected contributions of initially \$322 million annually rising to \$650 million annually by the third year. Sixty-five (65) percent of the funds will be allocated by USHUD directly to state governments, who in turn must award part of those funds to local governments through a competitive application process. Addressing the housing shortage for low income households is the primary purpose of these funds.<sup>7</sup> The remaining 35 percent will be directed to a Capital Magnet Fund (Section 1339) and allocated to Community Development Financial Institutions. The Capital Magnet Fund establishes a competitive grant program under the U.S. Treasury Department to attract private capital for affordable housing, economic development activities, and community service facilities (e.g., childcare centers, workforce development and healthcare clinics). This program encourages private sector investments through loan loss reserves, revolving loan funds, and risk-sharing loans.

We should also note that Title IX of The Housing and Economic Recovery Act increases the appropriation under the McKinney-Vento Homeless Assistance Act from \$70 million annually to \$100 million annually and requires emergency assistance to children and their families who become

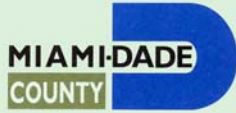
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<sup>4</sup> A "short sale" refers to the sale of a property for a price less than the outstanding balance(s) of the mortgage(s) held on that property. A short sale requires the approval of the lenders that hold the mortgage(s).

<sup>5</sup> A qualified mortgage is defined as an adjustable rate single-family residential mortgage loan made after December 31, 2001, and before January 1, 2008, that the housing finance agency determines would be reasonably likely to cause financial hardship to the borrower if not refinanced.

<sup>6</sup> Fannie Mae and Freddie Mac are both private corporations that are chartered (and regulated) by the federal government.

<sup>7</sup> More information on the Affordable Housing Trust Fund is available from the National Low Income Housing Coalition at <http://www.nlihc.org/template/page.cfm?id=40> (accessed Sept. 01, 2008)



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homeless as a result of foreclosure. This assistance is also available to renters who become homeless due to a landlord's foreclosure. The additional \$30 million in FY2009 will go to state educational agencies based on need, and the state agencies are required to make subgrants available to local educational agencies.

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