The public radio show about law and American life

Justice Talking
Radio Transcript

Fixing the Mortgage Mess—Air Date: 11/12/07

Many Americans' dream of homeownership has been lost as the subprime mortgage crisis has forced them to face foreclosure. Others ready to buy or refinance a home are finding fewer financing options as lenders are shutting their doors or laying off thousands of employees. Tune in to this edition of Justice Talking as we look at the current mortgage mess and ask how business and government should respond.

MARGOT ADLER: From NPR, this is Justice Talking. I'm Margot Adler. The housing downturn has brought down a house of cards in the mortgage industry. Millions of homeowners are in crisis, whether they have bad debt or live near neighbors that do. Today on Justice Talking: a look at the mortgage meltdown.

UNIDENTIFIED MALE: What's new about this decade is that a whole new group of predatory lenders got into the game, often doing flimflams with consumers, and the regulators were asleep at the switch.

UNIDENTIFIED MALE: I don't buy into this myth that everybody should own a home, that it's the American dream, that it's the way to build wealth, it's the way, you know, America needs to go.

MARGOT ADLER: The mortgage crisis in America: after the news.

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MARGOT ADLER: This is Justice Talking, from the University of Pennsylvania's Annenberg Public Policy Center. I'm Margot Adler.

The news has been filled with the far-reaching effects of what has been dubbed America's mortgage meltdown. There are charges of fraud, thousands of layoffs, widespread closures in the mortgage industry, and hundreds of billions of dollars in losses among the big financial firms. But if the housing downturn has brought panic-like conditions in the credit market, it is a wrenching disaster for an estimated two million Americans who are expected to lose their homes in the next two years. Today on Justice Talking: the mortgage crisis. How far should the government go to help people who own their homes? Could more regulation backfire? The answers to these questions will ripple broadly through the economy. Millions of Americans took on these risky mortgages when low interest rates and rising housing values led to appeals like these:

UNIDENTIFIED MALE: I'm in debt up to my eyeballs. I can barely pay my finance charges.

UNIDENTIFIED FEMALE: If you want to refinance your mortgage...

UNIDENTIFIED MALE: Consolidate bills...

UNIDENTIFIED FEMALE: ...or make home improvements...

UNIDENTIFIED MALE: ...and you want a great deal...

UNIDENTIFIED MALE: Tired of high interest rate bills? Whether you are refinancing, purchasing your dream home, or consolidating debt...

UNIDENTIFIED FEMALE: If you have credit card and other debt that's piling up and your payments keep changing monthly, you can lower...

UNIDENTIFIED MALE: When banks compete, you win.

UNIDENTIFIED MALE: Somebody help me!

MARGOT ADLER: I'm joined by Scott Reckard, a financial reporter for the Los Angeles Times. Scott, analysts say two million people will lose their homes in the next two years because of defaults on their mortgages. All of these homeowners took out what are called "subprime mortgages," geared toward people with poor credit. These loans start with very low payments, but later the payments shoot up, the so-called "exploding adjustable-rate mortgages" or A.R.M.'s. For example, one of these mortgages can start with a low 2 percent interest rate, or even zero, and then two years later jump to 8 percent. Some go into double digits. Many borrowers were betting on rising housing values so that they could easily refinance later. Is that why people took on these unfavorable loans?

SCOTT RECKARD: I think that's essentially right. I think in the real subprime market people had bad credit scores. They probably wouldn't start at zero percent or two percent. They had loans that would start like that, usually for people with a little bit better credit, a whole other set of problems. But in the subprime market, yes, a lot of people were told that they could refinance after two years. And in fact the loans in many ways were designed to do that. In a perfect world you would pay this loan for two years on time, clean up your credit, and then when it was about to go up a lot, you could then refinance and get a prime loan at a more reasonable interest rate.

MARGOT ADLER: Are all subprime mortgages bad?

SCOTT RECKARD: I don't think so, not at all. A lot of the activist groups, the advocates, will tell you that good subprime lending is a very good thing. It enables some people, particularly a lot of immigrants, minority populations, people who haven't had a chance to maybe buy a first house--there are times when you may want to refinance, you've had some problems, you need to get some money out to get something straight or send a kid to college. So, no, it's not all bad. But most of the bad, predatory lending tends to take place within that subprime category.

MARGOT ADLER: In addition to these jumping interest rates, I gather that there are other things about the loans that make them dangerous? One of the things I've heard about is prepayment penalties.

SCOTT RECKARD: That's right.

MARGOT ADLER: And some other features. Tell me about some of these practices.

SCOTT RECKARD: Well, the prepayment penalties are pretty onerous. And we looked into one company that was giving people loans that would adjust after two years but then they'd give you a prepayment penalty that didn't go away until the third year. So you were really stuck. And what it did was it forced you to go back and if you were going to refinance, probably refinance with them, and try to get them to make that prepayment penalty go away. The biggest problem has been in qualifying people at the start rate but then not making sure that they could pay the fully adjusted rate. And as time went on what they did was they combined these sort of exploding mortgage characteristics with other things like the stated-income loan so you didn't have to prove how much money you made.

MARGOT ADLER: So they or the mortgage broker would essentially lie?

SCOTT RECKARD: That's correct. Those are called "liar's loans." They certainly overstate their income.

MARGOT ADLER: Are these practices a recent innovation? And where do they come from? What led to them?

SCOTT RECKARD: Well, it's a development over a period of decades. The sort of the modern subprime industry kind of stepped in between the old banks that would only loan to--typically would loan to people with good credit who were doing okay in fairly nice parts of town, and then the sort of loan shark types who were in the less nice parts of town. And what you had then was the mass marketing of subprime loans to lots and lots of people probably at better rates than they would have got from the loan shark, but with these odd features. And still not at the kind of rates that you could get from a bank for a prime borrower.

MARGOT ADLER: Countrywide is one of the biggest lenders of subprime loans and recently it said that it would refinance tens of thousands of these loans. What's happening there?

SCOTT RECKARD: Well Countrywide, like a lot of lenders, is finding that many, many, many of these loans went bad. You know, home prices have come down. A lot of the excesses of the subprime market and the market in general were covered up by rising home prices. What that meant was that you could refinance maybe at a new start rate again or if it was really bad you could sell the house, pay off the lender, and you'd have something left over to go and start again. Now with home prices going down and especially with the kind of very low down payment loans that you saw at the height of the lending frenzy in 2005/2006, now people just can't refinance and their prices--their payments are going up and they are being forced into foreclosure because they can't pay the higher payment and their house isn't worth what they owe.

MARGOT ADLER: But it seems that what Countrywide says, that it's going to refinance, even if it does 100,000 loans, and they're talking I think of doing less, like 82,000 loans--

SCOTT RECKARD: Right.

MARGOT ADLER: Isn't that a drop in the bucket? I mean, it will only reach about 5 percent of homeowners in trouble.

SCOTT RECKARD: Yeah, if that. I mean the big issue now is despite the rhetoric from all the lenders, including Countrywide, by and large the people working on the street with borrowers say they haven't seen any sort of loan modifications, mass loan modifications, that could keep people in loans.

MARGOT ADLER: And why, um, why so few? I know that financial analysts at Moody's estimate that up till now lenders were only renegotiating about 1 percent of these loans, which, you know, I would imagine that it's better to renegotiate and continue to get some payments even if they're lower than foreclosure than hold a title to a house that's losing its value.

SCOTT RECKARD: I think that's exactly right and, you know, the lenders say they lose $30,000 to $50,000 on every foreclosure. Typically they don't want to be in the rental business, the foreclosed property business; they want to have mortgages. So I think that's true. Keep in mind that these things, mainly at companies like Countrywide, they've been sold off and so you're dealing with investors. And so before you modify that loan, the investors have to say it's okay. And they have to be happy with it. What the advocacy groups would like to see is to do mass loan modifications. And here's the basic plan that would happen there: You would have people who have shown that they can make the payments at that initial start rate. You know, they're paying the loan at six and a half percent or something. They're not going to be able to do it or it's going to be threatened when that loan adjusts upward. And so what you would do in the case of those people rather than let them slide towards foreclosure, or rather than give them entirely a new loan, you'd just reset the payments permanently or for a long period of time at that initial rate that they'd already showed that they could pay. And that would take care of a good chunk of people who, you know, really want to stay in their homes and have struggled to make those initial payments so far.

MARGOT ADLER: I understand that a disproportionate number of subprime mortgage holders are minorities. Is there any reason to believe that brokers are more likely to sell unfavorable mortgages to minorities even if their credit is just as good as white applicants?

SCOTT RECKARD: Some research has shown that there are disparities like that that can't be explained by factors such as income, circumstance, the price of the house, and all. The Center for Responsible Lending, for example, has done very careful studies that show that. And even the Fed, the Federal Reserve, did everything it could in a study to try to find out, including saying well maybe minority borrowers are more likely to walk into a company that just does subprime loans, and we'll rule that out. Even though the company didn't tell them they can get a better loan somewhere else, we'll rule that out. After all the factors had been ruled out it did look as though there was still some discrimination, that minority borrowers were getting a slightly greater percentage of subprime loans than they should have been.

MARGOT ADLER: How would you assess the current situation? Some say that the subprime situation right now is the worst disaster to hit American homeowners since the 1930s and at that time homeownership dropped to about 44 percent. Are there concerns that we're heading that way?

SCOTT RECKARD: Well, I don't know if it will drop to 44 percent. It had gotten up nearly to 70 percent from sort of the mid-60 percent range largely because of subprime lending. It's a huge crisis. It's a real problem. Overappraisals are going to pull property values down as that washes through. That will affect everybody. The prices really weren't as high as people thought. I think the subprime lending will be seen to have contributed to a very great decline in prices in a lot of markets, especially places like California and Florida. So I think it's a very damaging sort of thing, but particularly for that segment that couldn't get any other kind of loan. You know, people were told: Well try taking on this loan and after two years you clean your credit up you'll get a prime loan. But you know what? That isn't necessarily the case if it turned out that your home is now worth a lot less. You're underwater on the loan. You can't get a new loan if you owe more than the house is worth usually. And for reasons like that I think the pain is going to be very, very deep. And really what you're seeing now is the companies trying to find out ways to modify some of these loan terms so that you don't have quite as many people going into foreclosure.

MARGOT ADLER: Scott Reckard is a financial reporter for the Los Angeles Times. Thank you so much for coming on Justice Talking.

SCOTT RECKARD: Thank you very much for having me. I appreciate it.

MARGOT ADLER: Countrywide, mentioned in the earlier interview, is one of the largest lending institutions in the country and has come under criticism for its loan practices. Company officials did not return calls for this program, but the company has announced a multi-billion dollar plan to help thousands of their customers avoid foreclosure.

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MARGOT ADLER: Coming up on Justice Talking, one homeowner's story of another peril in the mortgage market: the false promise of help.

UNIDENTIFIED FEMALE: It sounded too good to be true, but at the same time I had nowhere else to go or nothing else to do.

MARGOT ADLER: And a debate on how the mortgage industry has changed, for good or ill.

UNIDENTIFIED MALE: The mafia really was in charge of this lending. There has been a great amount of progress here that we've gotten this lending out of the hands of the mafia.

MARGOT ADLER: Stay with us.

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MARGOT ADLER: This is Justice Talking, the public radio show about law and American life. I'm Margot Adler. The housing foreclosure crisis is reaching historical proportions. And another phase of this crisis has caught the attention of law enforcement officials: after the foreclosure notice comes the rescue scam. Karen Brown reports.

[DOGS BARKING] KAREN BROWN: Debra Avasey lives with her three large dogs in a modest two-story Cape in Springfield, Massachusetts. Thirty years after she bought the place it's teeming with memories. There's the corner where her pit bull had a 13-pup litter...

DEBRA AVASEY: It was amazing. I didn't know they could have that many dogs.

KAREN BROWN: ...the room where she held her mother's wake...

DEBRA AVASEY: And she passed away and we had probably about 100 people in here just for her, you know, after mass and all that, you know, we had the gathering here.

KAREN BROWN: ...and the bathroom her fiancé renovated after an argument.

DEBRA AVASEY: The whole room was gutted. It was a surprise for me. He had taken out all the tile. He had redone the bathroom while I was gone. I mean there are just way, way too many things to give up.

KAREN BROWN: But she may have to. Avasey lost ownership of her home through a deal she thought would save it. It all started several years ago when she and her fiancé refinanced the house so they could remodel. But her fiancé died of cancer. She fell into a deep depression, lost her job, and couldn't afford the monthly payments. As the bank moved to foreclose she started furiously applying for loans. Finally a man at a lending company called her back. He said her credit wasn't good enough for a loan but he could help her on his own.

DEBRA AVASEY: And then they called and said we can help you by buying your house for one year. It would get me to not worry about the mortgage because the taxes, mortgage, and insurance would be paid.

KAREN BROWN: And Avasey says she was told she'd receive $10,000 to get back on her feet so that after a year living there rent-free she could buy her house back.

DEBRA AVASEY: It sounded too good to be true, but at the same time I had nowhere else to go or nothing else to do. They were Christian people. They said, you know, "I'll pray for you." And they made it sound like there was nothing that could go wrong with it.

KAREN BROWN: But things did go wrong. Without realizing it, Avasey had landed in the middle of what the state attorney general and others call a "rescue scam." First, the man who offered to help Avasey had her transfer the deed of her house to a woman she'd never met. Avasey was handed an equity check for $30,000 and then told she had to sign the check over to the new owner. Instead of the promised $10,000, she got $2,000. She says she couldn't get copies of any documents. Then six months later the other shoe dropped. She was told to either start paying the mortgage, twice what she used to pay, or be evicted.

[SOUND OF PAPERS TURNING] UNIDENTIFIED MALE: Here's the appraisal.

KAREN BROWN: Avasey's pro bono lawyer, Joel Feldman, has been helping her retrace the chain of events. He says she was essentially tricked out of her home.

JOEL FELDMAN: There's just no income there for her to have repurchased her house. There was no possibility that she could have ever repurchased this house under the deal they made. Additionally, they didn't tell her they were going to take $30,000 of equity out of the house.

KAREN BROWN: Feldman got the housing court to stop the eviction. He's filed a lawsuit accusing the rescuers of lying to Avasey and stealing her equity. And as of this fall they have the law on their side. Massachusetts Attorney General Martha Coakley just banned all companies from offering to buy a home temporarily as a way to stave off foreclosure.

MARTHA COAKLEY: It's okay for family members to help each other out. We're not concerned about that, or legitimate nonprofit corporations, but for a fee with the company or the individuals taking the deed to the house, we've declared that to be an unfair and deceptive act or practice.

KAREN BROWN: Massachusetts is one of several states targeting rescue scams in addition to other types of predatory lending. Attorney General Martha Coakley says con artists see a ripe market in the rising number of foreclosures. Many find their targets by combing the newspapers for foreclosure notices. Some put signs on the road that say "we buy houses." Coakley has pledged to go after them. She's filed a lawsuit against three lenders.

MARTHA COAKLEY: Hopefully both consumers will be wiser and people will find it less and less lucrative to get involved in these schemes.

KAREN BROWN: In other words, Coakley wants to create a disincentive for people like Francine Times, the woman who bought Debra Avasey's house.

FRANCINE TIMES: This is my first deal; this is my last deal. I'm not doing anything like this anymore.

KAREN BROWN: Times lives on the other side of the state and says she owns a few other investment properties. She maintains that she thought purchasing Avasey's house was a legitimate buy-back program.

FRANCINE TIMES: I thought she understood everything that was going on. I was not really familiar with this type of program. So that's my defense.

KAREN BROWN: Times says she's no longer partners with the man who first made the deal, John Segal, who decline to comment for this story. And Times says despite the money she received in the deal she can no longer carry the mortgage and needs to sell it.

FRANCINE TIMES: The thing is I don't want that lady's house. I only stepped in as an investor to help this lady out.

KAREN BROWN: The question remains: Will the courts see it as help? Lawmakers and advocates say what people on the cusp of foreclosure really need is a frank conversation with their bank, state-funded assistance, or at the very least, the opportunity to sell their home and keep the equity. Meanwhile Debra Avasey is working full time at a Subway sandwich shop trying to repair her credit. And if she prevails on the lawsuit, the damages could be high enough to buy back her house. For Justice Talking, I'm Karen Brown.

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MARGOT ADLER: While a lawsuit may determine if Debra Avasey can stay in her home, Congress is considering sweeping measures to help hundreds of thousands of homeowners facing foreclosure. But some argue the hand of government will only add to the harm if it reaches too far into the market.

Debating this question today is Robert Kuttner, a financial journalist and co-founder of The American Prospect. He has written numerous books on the economy and taught at several major universities. And Joseph Mason, a professor of finance at Drexel University's LeBow College of Business and a former economist for the U.S. Treasury Department. Welcome both of you to Justice Talking.

JOSEPH MASON: Thank you Margot.

ROBERT KUTTNER: Thank you.

MARGOT ADLER: More than 7 million people are estimated to hold so-called subprime mortgages. One-third of these mortgage holders are expected to lose their homes. It's a housing crisis that some say our nation hasn't experience since the great depression. It used to be that you gave a down payment and you got a 15- or a 30-year fixed-rate mortgage. Now as many as 20 percent of homeowners, even people who qualify for more favorable loans, are getting these expensive mortgages. Joe, how is it that people with better credit found themselves with such risky mortgages? Were these just bad business decisions or were they conned?

JOSEPH MASON: In many cases they weren't bad business decisions. They're just different types of mortgages than have previously been sold in the U.S. marketplace. And it's important to remember that many of the borrowers were not subprime. They had adequate income. They could have serviced one of your old, traditional 30-year fixed-rate mortgages with 20 percent down very handsomely, but they chose instead to over-leverage themselves and to borrow as much as they could possibly afford. And they did so on the basis of these teaser rates, which often weren't anywhere near what is called the "go-to rate," the ultimate adjustable rate, with the idea that they would refinance before that point hit. The importance of this becomes that these loans were really very much like credit card loans with zero APR interest rates on them, seeking to refinance into a new zero-percent APR before the teaser rate ended to keep rolling over that debt. And eventually consumers got caught by rising interest rates.

MARGOT ADLER: I'm just trying to understand how so many people ended up taking out these kinds of mortgages, including people with, you know, reasonable credit.

JOSEPH MASON: Well the short answer to that question is the mortgage interest tax deduction, which gave an incentive for borrowers of all types to call as much as they could possibly classify a mortgage. And so there was an incentive to take home equity out of the home in order to buy cars, to pay for vacations, for various other purposes, but not to put this on a credit card or another type of vehicle. At the end of the day the mortgage interest tax deduction is an incentive to maximize mortgage debt, not an incentive to minimize mortgage debt by paying off your mortgage and owning the home.

MARGOT ADLER: Let's get Bob in here.

ROBERT KUTTNER: Yeah, I could not disagree more. I mean the mortgage interest deduction has been around for many, many decades. What's new about this decade is that a whole new group of predatory lenders got into the game with these very exotic products, often doing flimflams with consumers--bait-and-switch kinds of products that people did not understand. And the regulators were asleep at the switch and they allowed mortgage originators to lend money to people who had no prospect of paying off the loan. This is exactly the kind of abusive lending practice that financial services regulation is designed to prevent, and in fact Congress in 1994 in its wisdom passed a law requiring the Federal Reserve to crack down on predatory underwriting. But because the Fed doesn't believe in regulation except when it comes to bailing out people after the fact, the Fed declined to issue regulations. What I find offensive about what Mr. Mason is saying is that he's putting all of this on the borrowers, many of whom were deceived by predatory lenders. I think the real estate industry, the subprime lenders, the Wall Street blue-chip firms who were bankrolling the subprime lenders, and the regulators were much more at fault. And there were some individuals who took out these loans for speculative purposes, but I would put the individual borrower fifth on the list of people to point the finger at.

MARGOT ADLER: Let me ask Joe this: Do you think that only people that are financially sophisticated enough to recognize a bad deal should own a home? For example, I can't make heads or tails out of a lot of this stuff, and so isn't it in my interest to have this market regulated?

JOSEPH MASON: Well, it's in your interest to have the market regulated. It's a matter of how to regulate. I want to take a little bit of issue with Bob, but I also want to agree with him. There was a lot of this bait-and-switch-type behavior going on, but there was also a lot of this speculative behavior going on. The important thing going forward in regulation is how to separate the two. One very simple remedy, which is in the hands of Congress, not in the hands of the Federal Reserve, is to change the Real Estate Settlement Procedures Act to allow you, Margot, or me, to have those closing documents, a substantially complete set of those closing documents, in our hands, say 10 business days before closing. Once we sit down at the closing table, a) if I tried to read those documents at the closing table from start to finish I'd have a lot of very upset people there at the closing table with me, and closing would last about 18 to 20 hours. Furthermore, if I have an issue with any one of those terms, it's not going to be resolved at the closing table because there is no competition there. There's one loan officer and I don't have a chance to go out and get another offer.

MARGOT ADLER: Bob, you say that loans provided to low-income people used to be a good deal. They made ownership dreams come true. And you blame deregulation and speculators in the housing market for the problems of today. Why?

ROBERT KUTTNER: The federal government has largely gotten out of the business of subsidizing low-income homeownership or moderate-income homeownership, and so the only place for them to go a lot of the time if they can't really afford to become a homeowner is down the block to your local mafia lender. Although these lenders used low-income homebuyers as kind of poster children for their get-rich-quick schemes, what you're having now in low-income neighborhoods is an epidemic of foreclosures, which is hurting not only the people who tried to become homeowners but the people who are existing homeowners, because it's creating a glut on the market in a very concentrated way. I think moving up the date at which people get documents for a real-estate closing is woefully inadequate. I think these kinds of lenders ought to be put out of business. This was a scam pure and simple. If we want moderate-income people to become homebuyers -- because that's a goal of national policy -- we need below-market-rate interest loans, not above-market-rate loans. And that's a decision that Congress needs to make. But I think this whole thing was perverse.

MARGOT ADLER: So, Joe, should they be in business?

JOSEPH MASON: I think, Bob, you need to go back further in history when the mafia really was in charge of this lending. There has been a great amount of progress here that we've gotten this lending out of the hands of the mafia. Now, I think that your policy proposals are ignoring a dynamic marketplace with many more minds than we have in this room who can come up with financial products you never dreamed of before and have armies of attorneys and financial engineers that can develop those products and market them long before you catch up with them.

MARGOT ADLER: There are a lot of proposals out there for making changes to fix the situation. They range from changing the bankruptcy laws to allowing homeowners to sue Wall Street firms for backing predatory loans. I'd like each of you to sort of tell me what you want to see in various proposals, what you think would be a good idea. What's your bottom line, Bob?

ROBERT KUTTNER: Either under existing law or under new legislation to be written by Congress, we need to restore normal underwriting standards to the business of mortgage lending, whether it is a mortgage company that is currently unregulated or a mortgage broker or a bank. Secondly, we need an explicit program to subsidize the interest rate on mortgages for moderate-income, first-time homebuyers. We do a little tiny bit of that through neighborhood housing services. We do a little bit more of it through banks that agree to give below-market-rate loans in order to comply with the Community Reinvestment Act. And then, thirdly, we need a process for refinancing mortgages for people who got suckered who were not speculators, but who were trying to become homeowners in good faith. I think if we did those three things we could bring sanity and discipline back to the mortgage markets.

MARGOT ADLER: Joe, your bottom line for what we should do.

JOSEPH MASON: Well, I agree with Bob that we need an assistance program for those who have been suckered. The trouble in implementing that program is to determine who's been suckered and who was otherwise trying to use the system for their own gain. But nonetheless that system needs to be in place. Other than that I think it's important for regulatory reforms to first of all not abrogate contracts, not force lenders to write down principal values or force lenders into modifying loans that are not economical. But most of all I think that there need to be movements across the financial industry for transparency for these new products. The worst kind of financial crisis that you can get, Great Depression included, and today included, is when investors don't have information and they overreact.

MARGOT ADLER: That was Joseph Mason, a professor of finance at Drexel University and a former financial economist with the U.S. Treasury Department, and Robert Kuttner, a financial journalist with The American Prospect. His new book is "The Squandering of America: How the Failure of Our Politics Undermines Our Prosperity." What do you think? Should the government require lenders to renegotiate loans? Join the conversation on our blog at justicetalking.org.

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MARGOT ADLER: Coming up on Justice Talking, we hear from an Ohio official who tells us how foreclosures are wiping out whole neighborhoods.

UNIDENTIFIED MALE: This was the wild west of lending and quite frankly there was no sheriff in town. There was no action at the state level to slow down these lenders and these lending practices. There's really been nothing done in Congress since the mid-1990s. The Fed did nothing to prevent this.

MARGOT ADLER: And we learn how people with good credit are fairing in the mortgage market today--coming up on Justice Talking.

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MARGOT ADLER: This is Justice Talking, where we make the connection between law and American life. I'm Margot Adler. Jim Rokakis has an up-close view of how damaging the mortgage crisis can be for a community at large. Rokakis is treasurer of Cuyahoga County in Ohio, where whole neighborhoods have been decimated by foreclosures. Cuyahoga County is considered one of the epicenters of the mortgage crisis. Jim, welcome to Justice Talking.

JIM ROKAKIS: Thanks for having me.

MARGOT ADLER: Jim, just so people have a sense of where we're talking about today: Cuyahoga County includes Cleveland and surrounding areas. Last year more than 13,000 homeowners faced foreclosure in your county alone. That's the highest rate in the nation. What's happening in your community?

JIM ROKAKIS: Well what's happening here is that years of an unregulated mortgage lending industry have resulted in the inevitable. We're talking about people who had loans made to them that were not only not capable of sustaining these loans, they weren't even able to sustain them for one or two payments. The fraud that has gone on in Ohio really since the latter part of the 1990s is really unparalleled. I suppose the only good news is we're not first anymore because the most recent figures show that we've been outstripped by a number of cities in California, Las Vegas, and other parts of the country. We're not going to be experiencing what we've been experiencing all along.

MARGOT ADLER: And why do you think Ohio, and particularly your county, was so hard-hit compared to other places?

JIM ROKAKIS: Without question the economic conditions here have been tough. It's well known that a quarter of all the manufacturing jobs lost in the last five, six years in this country have been lost in the state of Ohio. But the reality is this was an unregulated industry. This was the wild west of lending, and quite frankly there was no sheriff in town. There was no action at the state level to slow down these lenders and these lending practices. There's really been nothing done in Congress since the mid-1990s. The Fed did nothing to prevent this. In fact they helped to feed the fire by keeping interest rates low. There were a lot of people that could have done something and they did not. And it doesn't mean there weren't attempts at the local level to deal with this problem. But we were really powerless in the scheme of things. The city of Cleveland can pass whatever they want, but at the end of the day they are going to be pre-empted by both state and federal law.

MARGOT ADLER: In a recent Washington Post article you singled out a particularly hard-hit area of Cleveland called Slavic Village. What was Slavic Village like before all the mortgage defaults and foreclosures?

JIM ROKAKIS: Well, I have to say upfront that it's still a good neighborhood, but clearly it's been dealt a real blow. Slavic Village is a tightly knit, ethnic community in the 44105 zip code. And I mention that zip code because there have been more foreclosures in 44105 than any other zip code in the country. Back in the 1990s these unregulated, unsupervised mortgage lenders came to Slavic Village and began making loans to buyers who weren't qualified. This phenomenon known as "flipping" began to occur. You saw properties changing hands two, three times. You saw mortgages begin to go bad at an unprecedented rate. So what you have today in Slavic Village is a good core, a lot of decent people struggling to keep the neighborhood alive, but one out of every seven, one out of every six houses, is vacant. And given the nature of this housing stock here, there are smaller, older, probably functionally obsolescent houses. There's very little chance they are going to be restored as housing. So now we are faced with a massive demolition problem.

MARGOT ADLER: So is the neighborhood, if it has so many foreclosed houses, is it more dangerous now? Is it a hard place to be in?

JIM ROKAKIS: As I spoke in The Washington Post, in the piece that I wrote, about an individual, 78 years old, who heard some noise outside his house--and the house next to him had been abandoned. It had been stripped of its aluminum siding, of all its copper. He stepped out. I guess kids were taking aluminum siding off of his house. He was 78 years old and they beat him to death in the driveway, on his birthday I might add. So clearly it is less safe because of situations like that. You've got these houses being stripped. You've got them being vandalized. And I've always said vacant houses provide a convenient opportunity for people to hide who have a reason to hide.

MARGOT ADLER: So the mortgage crisis is not only hurting the people who took out bad loans and have lost their homes. Their neighbors are in bad shape, too.

JIM ROKAKIS: Look, the real victims here-- You'll hear about Merrill Lynch. You'll hear about O'Neill. You'll hear about Bear Stearns. You'll hear about people losing their jobs. And clearly you'll hear about billions of dollars in hedge-fund losses. So they'll be a lot of losers out there, pension funds and others. But the real losers here are the innocent folks who have not been part of any of this, these shenanigans. They just, they have a house. They take care of it. They pay their taxes. The majority of their net worth is tied up in that structure. And here they go. They sit there and they see a house going vacant next door to them, one across the street, one down the block. And before you know it, their equity and their only real value, their net worth, is disappearing virtually overnight. And for a lot of folks who want to sell today, they couldn't sell even if they wanted to.

MARGOT ADLER: And when you look at people like you're talking about, let's say the people of Slavic Village, what choices do they now have?

JIM ROKAKIS: Well clearly their choices are limited. Part of what we're doing here in this town now is we're working hard to create a land authority that will step in, take a lot of these properties back, and take them down. Their best hope is demolition. For us, getting these properties down and out of the housing stock, the housing market, is a good thing, because there is very little chance they're going to be restored. Unlike Washington, D.C., Boston, California, Seattle, Portland, other parts of the country that are high-growth areas, this is a shrinking area. This is an area where population is declining. So the reality is we have an oversupply of housing stock and in cases like this we're best off taking most of those properties down--not all of them, but most of them.

MARGOT ADLER: The picture that you're painting sounds extremely frustrating.

JIM ROKAKIS: Well, it is. And it's part of the--you know, the part that I just struggle with is how many of these lessons do we have to learn? How many times do we have to through this? In the 1980s it was the "SNL" crisis, which cost the taxpayers of this country -- and I've seen different numbers -- $150, $200 billion. In the late 1980s I saw junk bonds through Drexel Burnham Lambert used to purchase perfectly good companies in northeast Ohio, stripping them of their assets and putting them out of business within five, six, seven, eight months. And then take your pick: GlobalCom, World Crossing, Enron. I mean this is just something. And we just keep putting up with it. And this will make all of those pale by comparison. And it's all greed. There's no other way to describe this. There were so many players in this game: brokers, appraisers, sellers, buyers, banks, mortgage banks, the issuing agencies, the rating agencies on Wall Street who made this possible by telling investors these were all good bets.

The problem with a crisis like this, Margot, is there's so many people to blame it's a case of where you almost feel there will be nobody to blame and there will be nobody held accountable at the end of the day except for those poor innocent folks in places like Slavic Village. They'll pay the price.

MARGOT ADLER: What do you think can be done now?

JIM ROKAKIS: Well unfortunately we're in a mop-up mode in many of these neighborhoods. I mean, I think that it is critical that we get as many of these properties down as we possibly can. They're not going to be restored and they continue to pose real threats to neighbors who live around them. I'd rather have a vacant lot next to me than a house that could be used for a crime or a house that might be set afire and threaten mine. And then going forward we have to make sure that we can create responsible opportunities for homeownership. And I don't buy into this myth that everybody should own a home, that it's the American dream, that it's the way to build wealth, that it's the way, you know, America needs to go. If there's anything this crisis has taught me -- and we have a foreclosure prevention program where we've met with thousands of borrowers -- a lot of these folks were simply not prepared to become homeowners. Not just because the loans weren't sustainable but because their financial literacy was weak. They just didn't understand what it meant to own a home and for a lot of them who wanted to stay in that home it's very tragic. That dream has been lost for a very long time.

MARGOT ADLER: That was Jim Rokakis, the treasurer of Cuyahoga County in Ohio.

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MARGOT ADLER: The dream of homeownership has become more complicated for people with good credit, too. Reporter Curt Nickisch visited a would-be borrower looking for a conventional loan. Lucia Sullivan wants to move her family from their small condominium in Cambridge, Massachusetts, where one recent afternoon her son was waking up from a nap.

LUCIA SULLIVAN: What's wrong? Is your house too small?

MARGOT ADLER: Sullivan says at first lenders assured her troubles in the mortgage market wouldn't affect her.

LUCIA SULLIVAN: And it's funny because I had called the mortgage banker and we had said, you know, we've read all these articles in the, you know, in The New York Times and everything, about what's going on. And she said very adamantly, you know, I'm not a subprime lender and you're not a subprime borrower and this doesn't affect you. And it doesn't, you know, this won't have any effect on us. And then every time we spoke to her it was like a little bit, you know, it was sort of like, okay, there's a little bit different information.

[PAPERS SHUFFLING] These are these letters we keep getting that come automatically. I guess they are computer-generated. So every time the banker enters a scenario we get this big packet which sort of explains the whole loan. But the funny thing is there seems to be a little disconnect, because then when I call the banker and say what is this, this is a different interest rate than we were talking about or this is a different loan than we were talking about, she says I was just trying to find you a better option, you know, so I tried something different, you know, a slightly different rate or a slightly different configuration. But then every time she does it I guess the computer sends a new one of these packs. And so it has, you know, every single detail, you know, truth-in-lending statement and all that. But it's just frustrating because, you know, you think, you know, everyone says your credit is excellent. We have the cash. We have done everything that we were told that we had to do. And then as it comes down to the wire you find out that everything keeps changing and the, you know, parameters change, the criteria changes. What the bank is willing to do changes.

But I think it's that, like even now, I mean, we're supposed to close a week from Friday and I still really don't have like a firm grasp on what our--I don't know what the closing costs are going to be. I don't know how much cash I need to come up with for, you know, in 10 days. And I don't really know what the monthly payment's going to be. I mean it's all sort of--every day it's a little different.

I remember years ago, like everyone was talking about their interest rate. It was like cocktail party conversation. You know, it was like oh, who was under 6 percent and who had this and who had that. And it was great. It was so interesting. But I feel like now, I mean, I just feel, I feel the same way I did when I first bought this little condo by myself. I'll just feel grateful to buy the house.

MARGOT ADLER: Sullivan was finally able to get her mortgage. To close the deal she says she had to increase her down payment by $7,000 and to pay a heftier monthly fee than originally quoted, $200 more a month.

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MARGOT ADLER: Elizabeth Razzi is an expert on the perils and opportunities of the housing market. She's the author of "The Fearless Home Buyer" and "The Fearless Home Seller." She's also a real estate columnist for The Washington Post. Welcome to Justice Talking.

ELIZABETH RAZZI: Oh, I'm glad to be here. Thank you.

MARGOT ADLER: Earlier in the show we talked about the impact of the mortgage crisis on homeowners. Everybody's watching the slumping housing market. How do you look at it as someone who counsels buyers and sellers?

ELIZABETH RAZZI: Well, there's a lot of fear going on out there right now. And it's different from the early '90s when the last big housing recession hit because that happened mainly on the coasts. The East Coast and the West Coast had big downfalls in prices, whereas the middle of the country did pretty well. This time it's spread more evenly. There still are some communities though, the Charlotte, North Carolina area for example, that are doing pretty well. So consumers really need to pay attention to their own local market rather than nationwide trends.

MARGOT ADLER: And is it really possible to be a fearless home buyer or a fearless home seller now at this time?

ELIZABETH RAZZI: You know, it never really is. Even, in fact, for me, I thought the scariest time to buy a home was at the peak of the market, 2004, 2005. It was ridiculously difficult to buy a home in most of the markets that were doing really well, the places where the bubble built up. People were getting outbid on homes when they were offering full price or even more. That was a truly scary time.

MARGOT ADLER: Is now a good time to buy?

ELIZABETH RAZZI: If you have the courage and if you have the time to sit it out a while. That's the question I get more than anything else. Everybody's saying what's going to happen next year? No one knows what's going to happen to prices between now and next year, or even now and two years from now. But very likely if you buy a home where you're planning to settle down for a while -- and that's a good five years, maybe longer -- you should be able to ride this out.

MARGOT ADLER: What advice do you give first time home buyers, or people with more modest incomes, or shaky credit history? Do they have any good options now that lenders are more cautious?

ELIZABETH RAZZI: Well the shaky credit history is the weak one there. You really can't do a lot with a shaky credit history now. The best thing to do now if you do have a shaky credit history is to rent for a little while and build that credit back up, build up your savings, pay off the credit card debt. Make your payments on time. And really get yourself in better shape. You'll have a lot more options in a year or so if you do that now.

MARGOT ADLER: I'm wondering how vulnerable would-be homeowners are? For example, can you trust your mortgage broker to tell you the truth about the terms of a loan? And how can an applicant protect him or herself?

ELIZABETH RAZZI: Some mortgage lenders now, loan officers, are calling themselves mortgages counselors. That's not the way you should look at it. These people are selling loans. And when you're sitting there applying for a mortgage, you should keep in mind that they're trying to sell you a mortgage. Mortgage brokers do not have an obligation to give the borrower the best mortgage. They don't have an obligation to find even the most suitable mortgage. And so you have to really sit down before you get any lenders involved whatsoever, sit down with your own budget and consider just what you can afford, what you are comfortable paying.

MARGOT ADLER: So what you said before that, um, these lenders are trying to sell you a loan. So that would mean that unless an applicant knows enough to ask certain questions a lender doesn't really have to disclose the real terms of the loan?

ELIZABETH RAZZI: Well, they're supposed to disclose the terms of, you know, the interest rate and things like that. But we found that over the boom years when so many really shaky mortgages were being made, there was an awful lot of "trust me" happening between the mortgage lender and the borrower. Oh, don't worry about this, you know, your income will get you through on this. And people trusted them. And you really cannot trust anyone to make that big a financial decision for you. I've spoken to a lot of people who truly didn't understand the terms of the loan that they were committed to.

MARGOT ADLER: And is that because there's just generally a lot of financial illiteracy in the country? Or, I mean, I admit that I look at some of these things and I don't understand them.

ELIZABETH RAZZI: Well, there is a lot of financial illiteracy, but you shouldn't feel like you're a dummy, because these things are very, very complicated. There's nothing wrong with talking to someone and you can get housing counseling before you take out a mortgage. That doesn't mean that you're in credit trouble. It doesn't mean you're financially illiterate. It just means that you're really empowering yourself to take advantage of everything that's available to you. The HUD website, www.hud.gov, has a link to a lot of accredited housing counselors who can advise you on this before you're committing.

MARGOT ADLER: Elizabeth Razzi wrote the books "The Fearless Home Buyer" and "The Fearless Home Seller." She's also a columnist for The Washington Post. Thank you so much for joining us on Justice Talking.

ELIZABETH RAZZI: Oh, I'm glad to be here. Thank you.

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MARGOT ADLER: Tell us what you think about the mortgage crisis and how government should respond. Join many of the nation's leading commentators on law and American life on our blog at justicetalking.org. Thanks for listening. I hope you'll tune in next week. I'm Margot Adler.

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