Chapter M: Federal Mortgage Title Resolution

Create a special prepackaged, streamlined mortgage bankruptcy chapter that does not affect non-mortgage debt. All foreclosure actions are automatically removed from state court to federal bankruptcy court. The foreclosure is adjudicated in federal bankruptcy court under standardized, streamlined procedures. Homeowner and lender both required to make evidentiary showings: homeowner must document ability to pay; lender must document title to note and mortgage, but with validity of securitization transfers conclusively presumed. Limited rights of appeal.

If homeowner is willing and able to pay, then homeowner keeps the house. Fresh appraisal done by court-appointed appraiser. Lender chooses between an FHA short-refi with principal reduced to [90]% of LTV or a standardized loan modification with principal reduced to 100% LTV and loan restructured to 30-year fixed-rate, full amortization, market interest rate adjusted to ensure maximum [31]% DTI ratio), with 50% risk-weighting for modified loans. Court validates lenders' title to mortgage. Junior liens exceeding LTV cut-offs are eliminated If the homeowner redefaults, an expedited, standardized federal foreclosure procedure is used ([45] days to sale), with limited defenses and clear title imparted by sale by bankruptcy trustee.

If homeowner does not qualify, lender gets same fast-tracked federal foreclosure and quiet title coming out of the foreclosure sale. If lender cannot show title, homeowner gets quiet title to property. In all situations, the homeowner's non-mortgage debts "ride-thru" the Chapter M bankruptcy, unaffected, but the homeowner could also file for a traditional Chapter 7 or 13 bankruptcy to address those debts.

Advantages:

- Provides quiet title to the whole system.
- Eliminates robosignor problem by reducing evidentiary burden on lenders.
- Addresses negative equity (principal reduction) as well as affordability (DTI cap).
- Removes mortgage servicers from process, ending servicer capacity and incentive issues.
- More attractive to mortgage lenders than traditional Chapter 13 cramdown option:
  - Fast-tracked, standardized foreclosure process;
  - Quick foreclosure upon redefault;
  - Protection of property against homeowner destruction during foreclosure;
  - Foreclosure sale by federal fiduciary; and
  - Ability to impart clear title.
- Addresses second lien problem via principal reduction.
- Does not affect non-mortgage lenders (actually helps them via consumer deleveraging).
- No cost to federal government except via GSEs/FHA.
- Immediately available, using existing courts and Chapter 7 panel trustees for sales.
- Federalizing foreclosures gives federal government control and information about process.
- No adverse selection issue—all homeowners in foreclosure get the choice of paying per standardized terms or losing the house quickly.
- Quick sorting of homeowners and reset for housing market.

Disadvantages:

- Could initially result in a glut of properties on market, depressing housing prices further.
- Lenders will not want to take write-downs, and would prefer to forbear on principal.
- Lenders will be concerned about loss of future appreciation with cramdown.
- Underwater second lien holders will object to getting nothing.
- Does not address total consumer debt burden.
- Non-mortgage creditors benefit at expense of mortgage creditors.
- Does not deal with unaffordability due to unemployment.

Possible corrections to the disadvantages:

- Clawback mechanisms can address potential future appreciation.
- Consumers could still file for Chapter 7 or 13 bankruptcy to address other debts.
- Eligibility could be narrowed, including exclusion of loans in Ginnie Mae pools.