Fixing
The Foreclosure System

A workshop on modernizing the foreclosure process to ensure the best outcomes for consumers and neighborhoods

Workshop Summary

Over the past generation, the mortgage market has changed dramatically, from a system dominated by local thrifts and banks to one in which a host of specialists, often operating on a national or international scale, collaborate to originate, fund and service mortgages. This transformation has benefited consumers in many ways, such as by contributing to broader access to credit, higher rates of homeownership, cheaper and faster loan applications and closings, and a greater ability for many to buy bigger houses at an earlier age.

These dramatic changes have allowed some new problems to arise too, including the current surge in mortgage foreclosures. Rising foreclosures are, in turn, revealing weaknesses in Minnesota's foreclosure system— the public laws, information systems and procedures that deal with foreclosed properties. These institutions have changed little over time and in key ways no longer seem adequate to address the losses that foreclosures inflict on borrowers, lenders and neighborhoods.

These institutions were the focus of a recent workshop, "Fixing the Foreclosure System," held at the Federal Reserve Bank of Minneapolis. An audience of lenders, foreclosure counselors, policymakers and others heard local and national experts discuss foreclosure laws, foreclosure data and early warning systems, and ideas for better management of vacant houses. Participants heard, for example, from Professor Ann Burkhart of the University of Minnesota Law School, who described the existing patchwork of state foreclosure laws as more a centuries-old accumulation of ad hoc "band aids" than a coherent system for balancing debtor, creditor and societal interests.

Burkhart's law-school colleague, Prentiss Cox, raised doubts about whether Minnesota's foreclosure auction system provides efficient protection for debtors. With the intent of protecting homeowners, Minnesota allows borrowers to buy their homes back at the auction price up to six months after a foreclosure sale. Relatively few borrowers— probably about 5 percent— actually use this option, but their right to do so creates a six-month limbo of uncertain ownership that can harm affected neighborhoods. Cox also asked whether it still makes sense to provide housing investors the same protections in foreclosure as owner-occupants.

This second question is particularly important because investor-owned properties are estimated to account for almost half of recent Minneapolis and St. Paul foreclosures. Workshop participants stressed the lack of formal protections for the many families who are renting properties subject to foreclosure. They heard how Minnesota's patchwork system of mostly paper-based county foreclosure records makes it hard for counselors and local governments to even track foreclosures and vacant properties.

But there are models for success. Officials from Chicago, Cleveland, Philadelphia and Memphis demonstrated sophisticated information systems that monitor affected properties and provide key information for those trying to mitigate the negative impacts of foreclosures and vacant homes on neighborhoods. Minneapolis, through cooperation with Hennepin County and the University of Minnesota's Center for Urban and Regional Affairs, has initiated its own tracking system, but it is provisional and may not be replicable, and 86 other counties have the same need. With a bit of planning and cooperation, Minnesota's counties and cities might develop new foreclosure and vacant property recording systems that would provide better information and be cheaper to operate.

However, even as Minnesotans deal with the immediate impacts of foreclosures, it is important to ask hard questions about the adequacy of the state's foreclosure systems. The Minnesota Legislature is indeed studying these issues and asking many of the right questions, and the recent Fed workshop showed that there are model laws and innovative approaches from other states and cities from which to draw.