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MORTGAGE TAKINGS AND MUNICIPAL FINANCE: A SOLUTION FOR PRESERVING HOME OWNERSHIP

*Necessity alone is not the test by which the limits of state authority in this direction are to be defined, but a wise statesmanship must look beyond the expenditures which are absolutely needful to continue the existence of organized government, and embrace others which may tend to make that government subserve the general well-being of society, and advance the present and prospective happiness and prosperity of the people.*¹

INTRODUCTION

Several years into the largest financial crisis since the Great Depression, housing prices and the value of home equity have stabilized.² While the free fall may have been suspended, the stagnant growth of a matured American economy³ and lackluster income growth⁴ have left many homeowners financially overwhelmed by the mortgages they took on when credit was cheap and owning a home appeared to be a sound, if not wildly profitable, investment. That the housing market is still hemorrhaging foreclosures⁵ suggests that the market correction process is nowhere near an end.⁶ It may take years to fully recover.⁷

1. *People ex rel. Detroit & H.R. Co. v. Salem Twp. Bd.*, 20 Mich. 452, 475 (1870) (per Chief Justice Thomas M. Cooley).

2. Press Release, Fiserv, Inc., *Fiserve Case-Shiller Home Price Insights: After Six Years of Decline, U.S. Home Prices Find Their Footing* (Aug. 6, 2012), available at <http://newsroom.fiserv.com/releasedetail.cfm?ReleaseID=698315>; Press Release, Fiserv, Inc., *Fiserv Case-Shiller Home Price Insights: U.S. Housing Markets Stabilizing, Affordability Reaches 40-Year High* (May 8, 2012), available at <http://investors.fiserv.com/releasedetail.cfm?ReleaseID=671290>.

3. OFFICE OF MGMT. & BUDGET, *FISCAL YEAR 2013 ANALYTICAL PERSPECTIVES: BUDGET OF THE U.S. GOVERNMENT 17* (2012), available at <http://www.whitehouse.gov/sites/default/files/omb/budget/fy2013/assets/spec.pdf> (generously predicting three percent GDP growth for FY 2013).

4. Jesse Bricker et al., *Changes in U.S. Family Finances from 2007 to 2010: Evidence from the Survey of Consumer Finances*, FED. RES. BULL., June 2012, at 1, available at <http://www.federalreserve.gov/pubs/bulletin/2012/pdf/scf12.pdf> (From 2007 to 2010, “real (inflation-adjusted) family income before taxes fell 7.7 percent; median income had also fallen slightly in the preceding three-year period.”).

5. Monthly foreclosures are decreasing in number, but the total number of foreclosures is still quite high. Associated Press, *Data Show US Foreclosure Filings Fell to 5-Year Low in September; Homes on Track down 12 Pct.*, FOX NEWS (Oct. 11, 2012), <http://www.foxnews.com/us/2012/10/11/data-show-us-foreclosure-filings-fell-to-5-year-low-in-september-homes-on-track/> (“There were 180,427 foreclosure filings report for September [2012], the fewest since July 2007 in the midst of the housing market bust.”).

6. See BD. OF GOVERNORS OF THE FED. RESERVE SYS., *THE U.S. HOUSING MARKET: CURRENT CONDITIONS AND POLICY CONSIDERATIONS 8* (2012) [hereinafter *BD. OF GOVERNORS, U.S. HOUSING MARKET*], available at <http://www.federalreserve.gov/publications/other-reports/files/housing-white-paper-20120104.pdf> (estimating that in 2011 there were approximately 2 million vacant homes for sale, with one-quarter of that inventory possibly coming from foreclosures—“held by banks, guarantors, and services after the completion of foreclosure proceedings”).

If the raw foreclosure data were not bad enough, the mortgages that have not yet defaulted or been foreclosed upon present dismal prospects for the macroeconomy and a possible “housing recovery.” Many homeowners are behind on their mortgages⁸ or nearing default.⁹ Even homeowners who are current on their mortgages¹⁰ often have little hope or economic incentive¹¹ to pay down the balance of their mortgage. This disincentive is the result of negative equity, which means the amount still owed on the mortgage exceeds the value of the underlying home.¹² Throughout the country, homeowners who are trying to stay in their homes, and trying to protect what might be their most valuable asset and investment, face the prospect¹³ of continuing to make huge mortgage payments relative to their homes’ actual value.¹⁴

The *longer* homeowners must contribute large portions of their income just to keep their existing homes, the *worse* their situation will become; and the longer the cumulative housing-foreclosure strain will weigh on the larger economy, which in turn weighs on homeowners who have no home

7. The home mortgage market is still smaller than it was six years ago, down to \$10.0 trillion from \$10.4 trillion in 2006. BD. OF GOVERNORS OF THE FED. RESERVE SYS., FLOW OF FUNDS ACCOUNTS FOR THE UNITED STATES: FLOWS AND OUTSTANDINGS: SECOND QUARTER 2012, at 104 tbl. L.217 (2012), available at <http://www.federalreserve.gov/releases/z1/20120920/z1.pdf>.

8. BD. OF GOVERNORS, U.S. HOUSING MARKET, *supra* note 6, at 21 n.39 (“About 660,000 mortgages are 30 days past due, 310,000 are 60 days past due, 1 million are 90 days or more past due . . .”).

9. The Federal Reserve estimates that 12 million mortgages are underwater, “representing roughly \$425 billion in negative equity.” *Id.* at 21. For bleaker numbers, see John Gittelsohn, *U.S. Homeowners with Negative Equity Drop as Prices Rise*, BLOOMBERG (Aug. 23, 2012, 4:27 PM), <http://www.bloomberg.com/news/2012-08-23/u-s-homeowners-with-negative-equity-drop-as-prices-rise.html> (“About 15.3 million homeowners, or almost 31 percent of those with a mortgage, had negative equity as of June 30 [2012] . . .”).

10. BD. OF GOVERNORS, U.S. HOUSING MARKET, *supra* note 6, at 21 (estimating 8.6 million negative equity mortgages are current on their payments).

11. See Robert C. Hockett, *It Takes a Village: Municipal Condemnation Proceedings and Public/Private Partnerships for Mortgage Loan Modification, Value Preservation, and Local Economic Recovery*, 18 STAN. J.L. BUS. & FIN. 121, 174–75 (2012) [hereinafter Hockett, *It Takes a Village*].

12. A negative equity mortgage is one where the homeowner owes more money on the mortgage than their home is actually worth. This is also referred to as having an “underwater” mortgage. Christopher L. Foote et al., *Negative Equity and Foreclosure: Theory and Evidence 1*, (Fed. Reserve Bank of Bos., Discussion Paper No. 08-3, 2008), available at <http://www.bos.frb.org/economic/ppdp/2008/ppdp0803.pdf>. These two terms of art are used interchangeably throughout the Note.

13. For examples, see Peter S. Goodman, *Eminent Domain as Underwater Mortgages Fix: Why Some Cities Are Considering Unorthodox Measure*, HUFFINGTON POST (October 1, 2012, 11:22 AM), http://www.huffingtonpost.com/2012/10/01/eminent-domain-mortgages_n_1917391.html.

14. The mortgage industry and economists generally refer to the “loan-to-value” ratio as a simple and crude measure to analyze the default risk of a mortgage. *Fannie Mae Multifamily Securities Locator Service Glossary*, FANNIE MAE, 6, http://www.fanniemae.com/resources/file/mbs/pdf/Disclosure_Glossary.pdf (last updated Aug. 2013).

equity.¹⁵ Moreover, the incentive structure for the various constituents affected by the mortgage and housing market is one that makes it unlikely that any one party—the homeowner, the mortgagee, or the servicer—will take any action that preserves the economic fundamentals beyond those that directly impact its individual interests.¹⁶ Homeowners want to keep their homes and maintain home-equity value; mortgagees (investors)¹⁷ want to get the most money out of their mortgage investment;¹⁸ and servicers want to generate fees.¹⁹ One scholar has articulated these divergent interests, and the “self-worsening” cycle that they create, as part of a larger collective action problem that plagues the housing market and stifles economic recovery.²⁰

An appropriate solution to the collective action problem must tolerate millions of homeowners²¹ with diverse financial circumstances and varying abilities to pay their mortgages as they come due, matched against a smaller and more uniform demographic of mortgage investors, who having cast their bread on the water are tasked with deciding how best to get it back.²² Consequently, the manifold nature of the housing crisis and impending

15. Homeowners may lose their homes regardless of their thrift or might pay for them many times over, given the excessive balances of the underlying mortgages. See Hockett, *It Takes a Village*, *supra* note 11, at 133–36.

16. See generally Robert C. Hockett, *Recursive Collective Action Problems: The Structure of Procyclicality in Financial Markets, Monetary Systems, Macroeconomics and Formally Similar Contexts*, 5 J. APPLIED ECON. (forthcoming 2013) [hereinafter Hockett, *Recursive Collective Action Problems*] (addressing these “recursive collective action problems” and proposing coherent collective agency for their solution).

17. For a discussion of the two “loss-mitigation strategies,” loan modification and forbearance, see Foote et al., *supra* note 12, at 4, 19–26.

18. Preserving the value of an individual mortgage does not necessarily imply that an investor wants to maintain or improve the actual possibility that they will be paid the amount due under the mortgage’s terms. Rather, it may mean preserving the value merely in accounting terms, by preventing foreclosures or refusing to write-down the mortgage, especially if the investor is an entity composed of shareholders. See *generally id.* at 4 n.4. Of course, there is a paradox here: mortgage investors might improve their actual expected return on investment by modifying the loan in favor of the homeowner to greatly reduce the likelihood of foreclosure, but this entails writing-down and permanently impairing the very investment they are trying to preserve. See *id.* at 19.

19. For a succinct explanation of the respective interests in the microeconomics mortgage crisis, see Hockett, *It Takes a Village*, *supra* note 11, at 140–41.

20. *Id.* at 123; see also Hockett, *Recursive Collective Action Problems*, *supra* note 16 (describing large “debt overhang” requires collective action); Robert Hockett, *Bretton Woods 1.0: An Essay in Constructive Retrieval*, 16 N.Y.U. J. LEGIS. & PUB. POL’Y 401 (2012) (discussing Keynesian economic policy in dealing with collective action problems).

21. Hockett, *It Takes a Village*, *supra* note 11, at 149 (“The challenge, again, is effectively an enormous coordination problem faced by literally hundreds of thousands, if not millions, of dispersed interested parties. Each of these parties acting individually has good reason to wait for the others to act, and so the group as a whole fails to act.”).

22. For an incredibly pragmatic solution that could easily be implemented at the federal level, see Kenneth C. Kettering, *Securitization and Its Discontents: The Dynamics of Financial Product Development*, 29 CARDOZO L. REV. 1553 (2008) (arguing that asset-backed securities, in many instances, have themselves become “too big to fail” and should be amenable to the federal Bankruptcy Code).

wave of foreclosures have forced economists and legal scholars alike to propose solutions that consider the many conflicts and issues that a single ramshackle *federal* program could not encompass. Not that the federal government hasn't tried; it has.²³ However, going forward, plausible solutions to the foreclosure crisis at the federal level require both political-will and consensus—two qualities the federal government does not now possess.²⁴

One such proposal, advocated by Professor Robert Hockett,²⁵ has drawn attention in both public and private circles.²⁶ Professor Hockett recommends that municipal governments²⁷ use the power of eminent domain to seize “underwater” mortgages from mortgagees (presumably lenders or investors), after which the municipality will negotiate new mortgage terms with the homeowner-mortgagor dependent upon terms and financing that the homeowner can receive through private refinancing.²⁸ Unlike the existing mortgages, the refinanced mortgage obligations are intended to reflect the current market value of the underlying properties and similarly to reduce the principal amount owed by homeowners.²⁹ Essentially, the hope is that condemning the mortgage and then refinancing it at market terms will displace the homeowner's negative equity.³⁰ However, in order to achieve that outcome in an economical manner, municipalities must ensure that the amount paid to condemn the mortgage note is substantially below the face value of the mortgage obligation.³¹ The benefits of the proposal may be realized only if this condition can be consistently (and legally) satisfied.³² In sum, the homeowner's deliverance

23. For a discussion of various federal programs, see Hockett, *It Takes a Village*, *supra* note 11, at 143–49 (arguing that the federal government's plans in the form of the Home Affordable Mortgage Program (HAMP) and the Home Affordable Refinance Program (HARP), along with suggestions by the federal government to expand the mandates of either the government-sponsored enterprises (GSEs) or Federal Reserve System to preserve homeownership, have been ineffectual).

24. Of course, any major legislative action requiring agreement poses a different kind of collective action problem. Cf. Michael O'Brien, *Poll: If Government Careens off Fiscal Cliff, GOP to Shoulder Blame*, NBC NEWS (Nov. 13, 2012, 2:26 PM), http://nbcpolitics.nbcnews.com/_news/2012/11/13/15141771-poll-if-government-careens-off-fiscal-cliff-gop-to-shoulder-blame.

25. Robert C. Hockett is a Professor of Law at Cornell Law School.

26. Nick Timiraos, *Investor Group Calls Richmond, Calif., Eminent Domain Plan Unconstitutional*, WALL ST. J. (Aug. 7, 2013), <http://online.wsj.com/news/articles/SB10001424127887324522504578654690187664354>.

27. “We refer to the states and their municipalities—townships, cities, counties, and kindred units of local government.” Hockett, *It Takes a Village*, *supra* note 11, at 150.

28. *Id.* at 150–52.

29. *Id.*

30. *Id.* at 169.

31. *Id.* at 137–38 (arguing for large-scale principal reductions).

32. “[N]or shall private property be taken for public use, without just compensation.” U.S. CONST. amend. V (Takings Clause); see *Chi., B. & Q.R. Co. v. City of Chicago*, 166 U.S. 226 (1897).

requires that the mortgagee absorb the negative equity as a loss in the condemnation proceeding.³³

Apart from Professor Hockett, the private company Mortgage Resolution Partners (MRP)³⁴ is offering for a flat, per-loan fee to act as an intermediary that will consult municipalities on which mortgages are appropriate to condemn.³⁵ MRP has outlined its prospective role as an advisor to municipalities that are considering condemning mortgages.³⁶ The company foresees “Five Stages of Relief” whereby (1) MRP screens existing mortgages in a municipality so that the municipality can inform homeowners if they qualify; (2) then private investors (mortgage lenders) fund an escrow account while the municipality files a condemnation suit; (3) assuming the lawsuit is successful, the loan is transferred to a trustee (4) to be restructured and (5) (re)securitized as a mortgage-backed security.³⁷

Currently, Richmond, California, is considering implementing Professor Hockett’s general proposal.³⁸ Strangely enough, one of the implicit selling points of Professor Hockett’s proposal is that it retains some of the grace of a free-market,³⁹ or private-sector, solution—with the role of local government limited to condemning the mortgage, while private mortgage lenders and homeowners take on the risk of newly issued mortgages.⁴⁰ Unsurprisingly, not everyone sees mortgage condemnation as an appropriate use of government power, even if it is legally sound.⁴¹

33. See Hockett, *It Takes a Village*, *supra* note 11, at 156 (describing municipalities as possible conduits to negotiate write downs between lenders and borrowers).

34. Mortgage Resolution Partners LLC (MRP) is based in San Francisco, California, and markets itself as a “Community Advisory firm.” See MORTGAGE RESOL. PARTNERS, <http://mortgageresolutionpartners.com> (last visited Nov. 17, 2013).

35. MRP made a formal presentation entitled “Homeownership Protection Program.” See Mortgage Resolution Partners, *Homeownership Protection Program: A Solution to a Critical Problem*, AM. SECURITIZATION F., 9, http://www.americansecuritization.com/UPLOADEDFILES/MRP_POWERPOINT_BW.PDF (last visited Nov. 17, 2013).

36. *Id.*

37. *Id.* at 11.

38. Niraj Chokshi, *Things Are Bad for the 15 Communities That Explored a Desperate Housing Bailout*, WASH. POST (Oct. 24, 2013, 3:37 PM), <http://www.washingtonpost.com/blogs/govbeat/wp/2013/10/24/things-are-bad-for-the-15-communities-that-explored-a-desperate-housing-bailout/>.

39. Robert Hockett, Testimony at the Hon Maxine Waters’ Financial Services Panel: The Housing Crisis and Policy Solutions (Sept. 11, 2012), *available at* <http://www.lawschool.cornell.edu/spotlights/upload/Testimony-of-Robert-Hockett-11-September-2012-Third-Round.pdf> (“Private entities will provide all funding and take all risk to acquire and refinance the mortgage loans.”).

40. Hockett, *It Takes a Village*, *supra* note 11, at 152 (emphasis added) (“Municipalities or authorities acting on the [eminent domain] Plan will pay for the mortgage-associated loans and liens of which they take legal possession with funds supplied by the aforementioned *private sector investors*. Among these investing institutions—which, notably, may include current loan and lien holders themselves, indirectly through MBS—will be one or more of the following: public and private pension funds, insurances companies, mutual funds and other investment firms.”); *see also* David Reiss, *Eminently Reasonable*, NAT’L L.J., Sept. 24, 2012, at 35, *available at* <http://www.law.com/jsp/nlj/PubArticleNLJ.jsp?id>

The balance of this Note will first demonstrate the contingencies of a plan where the local government serves as an intermediary, condemning a mortgage from one recalcitrant mortgagee so that another lender may refinance or underwrite a new mortgage that reflects the current market value of the underlying home. Second, I propose a novel and comprehensive plan that utilizes the unique role that municipalities can play in the mortgage takings context. My proposal, too, foresees local governments condemning underwater mortgages. But instead of leaving them to be refinanced by private mortgage lenders, who will operate at arm's length, I argue that it might be more beneficial for local governments to simply hold onto such mortgages for their term of years, using them as collateral to secure municipal bonds, which will provide the primary source of financing for the mortgage takings.

Throughout the exposition of my proposed *publicly financed mortgage takings*, I outline the legal issues that both my and Professor Hockett's plan face. It is better left to economists to address the possible impact that publicly financed mortgage takings could have on society beyond those affected at the local level.⁴²

Part I highlights the effect that home prices and homeownership have on the financial integrity of local governments.⁴³ Communities with depressed home prices and high foreclosure rates often cannot generate sufficient tax revenues for their local government to provide a desirable level of public services. In short, the economic problem becomes a civic problem that further serves to reduce the incentive for existing and

=1202572203513&Eminently_reasonable ("A common argument by the investing community is that pro-borrower developments will destroy credit markets This long-term chilling of the credit markets has never actually happened. If lenders and investors think they can make money in the market, they will return to it like bears to honey.").

41. H.R. REP. NO. 112-6397, at 1 (2012), available at <http://www.gpo.gov/fdsys/pkg/BILLS-112hr6397ih/pdf/BILLS-112hr6397ih.pdf> ("To prohibit Fannie Mae and Freddie Mac from purchasing, the FHA from insuring, and the Department of Veterans Affairs from guaranteeing, making, or insuring, a mortgage that is secured by a residence or residential structure located in a county in which the State has used the power of eminent domain to take a residential mortgage.").

42. For a general discussion of the economics involved, see Hockett, *It Takes a Village*, *supra* note 11, at 137, 156; Robert C. Hockett, *Six Years on and Still Counting: Sifting Through the Mortgage Mess* 3–36 (Cornell Law Sch. Legal Studies Research Paper Series, Paper No. 12-11, 2012) [hereinafter Hockett, *Six Years*], available at <http://ssrn.com/abstract=2029262>; Alan C. Weinstein, *Current and Future Challenges to Local Government Posed by the Housing and Credit Crisis*, 2 ALB. GOV'T L. REV. 259 (2009) (exploring the various economic consequences and challenges that local governments are likely to have to deal with over the next several years resulting from a flagging housing market). *But see* Memorandum from Walter Dellinger et al., O'Melveny & Myers LLP to SIFMA 12–16 (July 16, 2012) [hereinafter OMM Memorandum], available at http://www.sifma.org/uploadedfiles/issues/capital_markets/securitization/eminent_domain/memorandumfromo'melvenymyerstosifmaresanbernardinoeminentdomainproposal071612.pdf (arguing that mortgage takings will cause burdensome litigation that is "time-consuming and expensive," while possibly making it more difficult to get favorable mortgage financing from lenders who wish to punish municipalities that exercise their power of eminent domain).

43. See Weinstein, *supra* note 42, at 275–76; Hockett, *It Takes a Village*, *supra* note 11, at 171–75.

prospective homeowners to inhabit that locality. With that in mind, municipalities considering mortgage condemnations are not doing so to remediate a nation-wide housing slump; they are doing what is in their own best interest and, at the same time, the best interests of their residents or constituencies—the public.⁴⁴

Part II outlines the condemnation proceeding that municipalities could exercise along with the constitutional and legal basis for that power at both federal and state levels. Specifically, I demonstrate that there is ample precedent for municipalities to condemn residential mortgages.⁴⁵ In addition, I argue that states should have the constitutional authority to condemn mortgages even where the original promissory note is outside the state, so long as the real property securing the note is within the state. Part II also covers the refinancing of the condemned home mortgages to the extent that municipalities can write-down mortgages. But which mortgages *ought* to be condemned or, alternatively, which homeowners should be the beneficiaries of the condemnation proceeding is beyond the scope of this Note—these are tough decisions which ultimately the citizens and leaders of local governments will have to make.⁴⁶

Part III explores the benefits of using public finance at the municipal level to fund mortgage condemnations, along with the prospective advantages that exist for municipalities retaining mortgages for the mortgages' term of years. There is also a brief overview of the legal capacity of municipalities to issue tax-exempt municipal bonds. I argue that municipalities will be able to get cost-effective financing because of their *possible* tax-exempt status and the fact that they can secure their bonds with the existing home mortgages—essentially, municipal bonds that are mortgage-backed securities.

44. Hockett, *It Takes a Village*, *supra* note 11, at 150 (“It is *cities* that must watch their residents being evicted, their homes being emptied, their houses deteriorating, their property values plummeting, their tax bases dwindling, their services retrenching, their crime levels spiking, and so on. But they don’t have to lie back and watch. They can act, and act now. They *exist* to address the problems like these. Protecting the citizenry and heading off blight is what municipal *eminent domain* authority is for.”).

45. *E.g.*, *Omnia Commercial Co. v. United States*, 261 U.S. 502 (1923); *City of Cincinnati v. Louisville & Nashville R.R.*, 223 U.S. 390, 400 (1912).

46. Professor Hockett has some recommendable suggestions regarding which mortgages should be condemned:

First, the Plan will apply only to single family, owner-occupied residences within each municipality’s jurisdiction. Second, all existing qualifying lien mortgage loans will have loan to value ratios (LTVs) greater than 100%. Third, the aggregate fair market value of loans or liens secured by any qualifying home should total 85% or less of the value of the home itself. . . . Finally, the value of the qualifying homes will not exceed 105.3% of FHA approved loan amounts—thus permitting a 95% new loan to value ratio.

Hockett, *It Takes a Village*, *supra* note 11, at 154–55.

I. THE MUNICIPALITY AND ITS HOMEOWNERS

The housing crisis, given the scale of the U.S. housing market as an investment for both domestic and international investors, has produced consequences on a local, national, and global scale.⁴⁷ The increasing macroeconomic relevance of home prices in the United States is largely due to the proliferation of mortgage-backed securities,⁴⁸ which repackage portfolios of home mortgages into more fungible securities.⁴⁹ Individual mortgages have unique qualities and risks that are diversified away or offset when aggregated with other mortgages that are facially similar—having borrowers and contract terms that are approximate.⁵⁰ Indeed, the securitization of mortgages into mortgage-backed securities gives investors from all around the world an opportunity to gain exposure to the U.S. housing market; the influx of investors simultaneously gives home buyers in the United States greater access to credit (investment capital) that may enable them to purchase a house.⁵¹

Regardless of the ubiquity of mortgage-backed securities, the financial perils that ensue when housing prices and home values decline are quite asymmetrical between investors and homeowners.⁵² The investors' mortgage-backed securities might be only fractionally composed of mortgages that face the prospect of default or a write-down in value. This

47. See Richard Dorfman et al., *MBS Fact Sheet*, SIFMA, 3, <http://www.sifma.org/workarea/downloadasset.aspx?id=8589934849> (last visited Nov. 17, 2013) (showing fourteen percent of mortgage-backed securities as “Foreign Holdings”).

48. As of 2011, of the approximately \$10.5 trillion of residential mortgage debt, about \$7.1 trillion is securitized in some form of a mortgage-backed security, while only \$3.4 trillion is “Not Securitized.” *Id.* at 2.

49. Kathleen C. Engel & Patricia A. McCoy, *Turning a Blind Eye: Wall Street Finance of Predatory Lending*, 75 *FORDHAM L. REV.* 2039 (2007).

50. Steven L. Schwarcz, *The Alchemy of Asset Securitization*, 1 *STAN. J.L. BUS. & FIN.* 133, 141–44 (1994) (explaining how “credit enhancement” is an indirect benefit of securitization).

51. See Anna Gelpern & Adam J. Levitin, *Rewriting Frankenstein Contracts: Workout Prohibitions in Residential Mortgage-Backed Securities*, 82 *S. CAL. L. REV.* 1075, 1084 (2009) (“Securitization can further reduce borrowing costs through financial engineering. Techniques such as the division of the [special purpose vehicle’s (SPV)] securities into senior and subordinate ‘tranches’ expand the potential investor base. They allow the SPV to target new investors with tailored payment structures and credit enhancements. In particular, they permit the issuance of some securities at a higher credit rating than the overall quality of the assets in the SPV. Such senior securities can be sold to institutional investors that may only buy investment-grade paper. Adding potential investors boosts overall demand and lowers the cost of financing.”).

52. “One study has found that even a single foreclosed home depresses prices of nearby homes from just under one to as high as 8.7 percent.” Hockett, *It Takes a Village*, *supra* note 11, at 173 (citing U.S. GOV’T ACCOUNTABILITY OFFICE, NO. GAO-12-34, *VACANT PROPERTIES: GROWING NUMBER INCREASES COMMUNITIES’ COSTS AND CHALLENGES* 44–45 (2011), available at <http://www.gao.gov/assets/590/586089.pdf>). Cf. Weinstein, *supra* note 42, at 267 (citing Dan Immergluck & Geoff Smith, *The External Costs of Foreclosure: The Impact of Single-Family Mortgage Foreclosures on Property Values*, 17 *HOUSING POL’Y DEBATE* 57, 67, 72 n.1 (2006)) (“[T]he value of surrounding properties declines by 0.9% on average for each foreclosed house in the vicinity, with the decline even greater in low-income neighborhoods at 1.44%.”).

ability to diversify by including mortgages with varied credit risks reduces investors' potential losses from mortgages likely or certain to default.⁵³

In contrast, given that a residential property is typically a homeowner's largest investment, only residence, and the collateral underlying their mortgage, a volatile housing market poses substantial financial risks for homeowners.⁵⁴ Homeowners who can make their mortgage payments and who have positive home equity are incentivized to continue making payments so long as they think that their home's value will remain stable or rise.⁵⁵ Whereas those homeowners with negative equity may benefit from selling their home or defaulting on their mortgage in order to divert their existing mortgage payments to the purchase of an asset (perhaps another home) that will accumulate equity.⁵⁶ Alternatively, depressed home prices or comparatively cheap rentals may make the opportunity cost of continuing homeownership much higher, thereby altering the transitive preferences of homeowners as they seek to reduce their living expenses.⁵⁷ In several states the preference default is considerably enhanced because lenders have no legal recourse against homeowners for the unpaid mortgage debt or deficiency.⁵⁸ For those homeowners who cannot make their payments, default is the consequence and foreclosure is imminent—whether they have negative or positive home equity, they face the grim reality of losing their home.⁵⁹

The risk of default or foreclosure is generally going to have a stronger correlation with default and foreclosure rates at the local rather than national level.⁶⁰ More importantly, the consequences of default and

53. See Schwarcz, *supra* note 50, at 141–44.

54. Foote et al., *supra* note 12, at 22.

55. *Id.* at 12 (emphasis added) (“Economic theory poses one categorical prediction about the relationship between negative equity and default, which is that negative equity is a necessary condition for default This conclusion follows simply from the fact that *positive equity* implies that a borrower can sell the house, pay off the mortgage, and keep the difference, a better outcome under any circumstance compared with stopping payment on the mortgage and leaving the home.”).

56. *Id.* at 12 (“The idea that one should continue making monthly mortgage payments even when the market value of the house is worth less than the outstanding balance on the mortgage seems puzzling to many people. Some commentators view the fact that most people with negative equity keep their homes as a ‘failure’ of the theory”).

57. See *id.* at 3.

58. *Id.*; see generally John Rao & Geoff Walsh, *Foreclosing A Dream: State Laws Deprive Homeowners of Basic Protections*, NAT'L CONSUMER L. CENTER (Feb. 2009), http://www.nclc.org/images/pdf/foreclosure_mortgage/state_laws/foreclosing-dream-report.pdf (nonrecourse or non-deficiency states include Alaska, Arizona, California, Hawaii, Minnesota, Montana, North Dakota, Oklahoma, Oregon, and Washington).

59. See Hockett, *It Takes a Village*, *supra* note 11, at 172 n.156 (citing Janet Currie & Erdal Tekin, *Is the Foreclosure Crisis Making Us Sick?*, NBER Working Paper No. 17310 (August 2011), <http://www.nber.org/papers/w17310>; G.T. Kingsley et al., *The Impacts of Foreclosures on Families and Communities*, URBAN INST. (May 2009), http://www.urban.org/UploadedPDF/411909_impact_of_foreclosures.pdf).

60. U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 52, at 19.

foreclosure are not diffuse or well-distributed across the broader housing market.⁶¹ Rather, foreclosures, defaults, and negative equity produce externalities that are felt first and foremost at the local level.⁶² The onset of defaults and foreclosures can further depress home values at the local level⁶³ as more and more houses go on the market, which are either sold or remain in inventory.⁶⁴ Again, this can drastically alter financial incentives for existing homeowners because they are often paying significantly more money for their home than it would cost them to buy at the reduced market price.⁶⁵ Reducing their “housing expense” to a level commensurate with the market becomes the rational alternative, since homeowners in plighted communities can no longer expect to preserve their home equity and may potentially lose their wealth as homes prices fall.⁶⁶

A. MUNICIPALITIES HAVE A VESTED INTEREST IN PRESERVING HOMEOWNERSHIP AND HOME EQUITY

The problem, of course, for municipalities is that much of the revenue and budget planning for conducting local government—or municipal infrastructure generally—is dependent upon residential property values as a function of property taxes.⁶⁷ Also of great significance is the psychological malaise that homeowners and citizens deal with as a result of worrying

61. See generally Pamela Lee, *Eminent Domain, The Debate Distracts from Pressing Problems*, URBAN INST., at 5–6 (Oct. 22, 2013), <http://www.urban.org/UploadedPDF/412937-Eminent-Domain-The-Debate-Distracts-from-Pressing-Problems.pdf> (documenting the geographic concentration of foreclosure and negative equity).

62. “By any measure, the epidemic of home losses is severe, and will not only harm the families who lose their homes, but also nearby homeowners who suffer drops in their property values and communities who suffer the impact of lower tax revenues.” *Subprime Spillover: Foreclosures Cost Neighbors \$223 Billion; 44.5 Million Homes Lose \$5,000 on Average* 5, CENTER FOR RESPONSIBLE LENDING (Nov. 13, 2007), http://www.pewtrusts.org/uploadedFiles/wwwpewtrustsorg/Reports/Subprime_mortgages/subprime-spillover111307.pdf.

63. Thomas Deutsch of the American Securitization Forum provided his insights to Congress:

The primary factors our members have identified that have combined to put severe strain on homeowners and drive rising delinquencies, defaults and foreclosures include: 1) unavailability of mortgage credit for refinancing opportunities; 2) declining home values; 3) high levels of non-mortgage credit outstanding (e.g., credit card, auto loan, other debt); 4) prevalence of 2nd liens; and 5) rising unemployment levels and reductions in income, making mortgage payment unaffordable.

Private Sector Cooperation with Mortgage Modifications—Ensuring That Investors, Servicers, and Lenders Provide Real Help for Troubled Homeowners: Hearing Before the H. Comm. on Fin. Servs., 110th Cong. 64–65 (2008) (statement of Thomas Deutsch, Deputy Executive Director, American Securitization Forum), available at <http://www.gpo.gov/fdsys/pkg/CHRG-110hhr46592/pdf/CHRG-110hhr46592.pdf>.

64. Kingsley et al., *supra* note 59, at 19 (citing numerous effects of local foreclosures).

65. See Foote et al., *supra* note 12, at 3, 12.

66. *Id.*

67. “The most obvious repercussion from the housing/credit crisis for local government is its affect [sic] on municipal revenues.” Weinstein, *supra* note 42, at 266.

about the value of their homes.⁶⁸ Homeowners who are not confident in their largest investment (their home) are more conservative consumers,⁶⁹ which may negatively impact local economies and tax revenues.⁷⁰ Municipalities, therefore, have incentives to stave off the continued collapse of property values and, at the same time, contain the conflagration of ill effects resulting from a fiscal crisis in local government.⁷¹ The encompassing communities, too, surely want to see home values stabilize, along with preserving homeownership and the demographics or social fundamentals that homeownership helps to anchor within communities.⁷² Though each community⁷³ is in a unique position to assess the equities and challenges posed by the housing crisis, “[f]or the problem itself is essentially, in its first instance, local in character.”⁷⁴

**B. LOCAL GOVERNMENTS ARE PROPERLY SUITED TO PLAY THE
ROLE OF AN INTERMEDIARY FOR CONDEMNING MORTGAGES
AND FORCING PRINCIPAL REDUCTIONS**

Those who oppose the use of eminent domain to condemn mortgages are correct to point out that the promise, and indeed the risk, of exercising municipal power in such a situation is relative to the time, expense, and overall efficiency of the condemnation proceedings.⁷⁵ By definition, a

68. Foote et al., *supra* note 12, at 22 (describing instances when homeowners with negative equity “remained vulnerable to adverse life events, like job loss, illness, and divorce, all of which create cash-flow problems”).

69. Weinstein, *supra* note 42, at 267–68. In a sense, homeowners dealing with negative equity have already taken a big risk and lost. They are therefore less able to borrow money and engage in commerce or start new business ventures. However small or inconsequential a small entrepreneur might seem, small businesses run by such individuals help maintain both the social and economic fabric of communities. Foote et al., *supra* note 12 (discussing the homeowner’s financial “inertia” when owning a home with negative equity).

70. “First, as homes are the most valuable asset for most families, the reduction in home value makes them feel less wealthy and reduces their ability to tap into the home’s equity—factors that lead households to cut back on expenditures.” Weinstein, *supra* note 42, at 266.

71. “Across California, the recession that ended in 2009 and the foreclosure crisis have depleted property-tax revenue even as municipalities are burdened with rising costs.” Brian Chappatta & Kathleen Hays, *California Muni Bankruptcies a Growing ‘Disease,’ Kotok Says*, BLOOMBERG (October 3, 2012, 2:35 PM), <http://www.bloomberg.com/news/2012-10-03/california-muni-bankruptcies-a-spreading-disease-kotok-says.html> (discussing three coinciding municipal bankruptcies in California—Stockton, San Bernardino, and Mammoth Lakes).

72. See Dan Immergluck & Geoff Smith, *The Impact of Single-family Mortgage Foreclosures on Neighborhood Crime*, 21 HOUSING STUD. 851, 859–62 (2006); Kingsley et al., *supra* note 64, at 15–21 (listing crime, social disorder, population turnover, and deterioration of governmental services as negative effects associated with foreclosures).

73. See Christopher Serkin, *Big Differences for Small Governments: Local Governments and the Takings Clause*, 81 N.Y.U. L. REV. 1624, 1648 (2006) (“The source of homeowners’ incentive to control local politics is their common goal of preserving the value of their property. The financial stakes alone are enormous.”).

74. Hockett, *It Takes a Village*, *supra* note 11, at 150.

75. See OMM Memorandum, *supra* note 42, at 12–15; see also *Judicial Versus Non-Judicial Foreclosure*, MORTGAGE BANKERS ASS’N, <http://www.mbaa.org/files/ResourceCenter>

municipality is a devolutionary form of government subject to overriding county and state law,⁷⁶ which means that a municipality's administrative authority, including the power of eminent domain, is likely constrained by state and county law.⁷⁷ As a result, local governments should evaluate the legal and economic viability of a mortgage takings plan by first examining eminent domain law in their respective jurisdictions.⁷⁸ Furthermore, since local governments are mainly administrative entities, many of the bureaucratic functions required for carrying out the condemnation proceedings, along with finalizing mortgage principal reductions, are within the capacity of a municipal corporation or can be sought at the local or county level.⁷⁹ Basic procedural matters such as serving process or notice, attaching the mortgage note and underlying deed of trust, or recording changes therein are functions that a municipality can often handle directly without having to seek prior approval from a state legislature.⁸⁰

Additionally, municipalities that levy property taxes are in an advantageous position to decide whether or not to use their eminent domain power because they already have annual assessments of property values.⁸¹ The assessments, as well as the factors that are used to determine real estate values in a locality, can be used during the condemnation proceeding as evidence of the mortgage collateral's "fair value."⁸² Part III of this Note covers some of the aspects of property valuation for condemnation proceedings.⁸³

Even before the condemnation proceeding begins, establishing the fair value of a particular residential property is essential for ascertaining the value of the mortgage instrument and the corresponding likelihood that a homeowner will default or have any chance of realizing positive home-

/ForeclosureProcess/JudicialVersusNon-JudicialForeclosure.pdf (last visited Nov. 17, 2013) (estimating the foreclosure process as taking anywhere from 480 to 700 days).

76. *E.g.*, N.Y. GEN. CONSTR. LAW § 66 (McKinney 2012) ("A 'municipal corporation' includes a county, city, town, village and school district."). Similarly, California law puts emphasis on a unit of government's incorporation status. Counties and cities are incorporated, while towns are unincorporated, with counties being the largest unit of incorporated political government. CAL. GOV. CODE §§ 19–21 (West 2012).

77. Again, this varies amongst the states. Some states vest eminent domain powers with counties, and the small subunits within the county, such as cities and school districts. *E.g.*, WASH. REV. CODE § 8.08.010 (West 2013) ("Every county is hereby authorized and empowered to condemn land and property within the county for public use . . ."). Other states, like New York, focus on the delineation of incorporated local government to provide a measure of uniformity throughout the state, rather than county-by-county balkanization. *E.g.*, N.Y. EM. DOM. PROC. LAW § 101 (McKinney 2012) (Eminent Domain's Purpose).

78. *E.g.*, CAL. CIV. PROC. § 1255.410 (West 2012) (California's "quick take" provision).

79. See OSBORNE M. REYNOLDS, JR., LOCAL GOVERNMENT LAW § 96 (3d ed. 2009).

80. See *id.* §§ 129–30.

81. See *id.* § 96.

82. "Fair market value, however, is a moving target." Stewart E. Sterk & Mitchell L. Engler, *Property Tax Reassessment: Who Needs It?*, 81 NOTRE DAME L. REV. 1037, 1066 (2006).

83. See *id.* at 1068–70.

equity over the life of the mortgage.⁸⁴ Local governments are well positioned to account for the cumulative factors that can be used to ascertain property values and to screen homeowners⁸⁵ who are the most eligible for condemnation proceedings.⁸⁶ That local governments are already properly scaled to assess property values adds to both the efficiency and efficacy of the mortgage taking's proposal because the benefits of the combined condemnation proceedings and principal reductions are precisely relative to both (1) the ability of target homeowners to afford their restructured mortgages and (2) the stability of the new loan-to-value ratio on the restructured mortgages.⁸⁷ Local government's role in property assessment is vital for assuring that both of those elements are met. Realizing the value of (or revaluing) residential properties is the very thing that many financial institutions or investors in mortgage-backed securities have been unwilling to accept, as it may implicate a write-down on their investment.⁸⁸

For those wary of eminent domain being used to condemn mortgage notes without paying just compensation, a municipality's interest in securing low property assessments is checked by the amount of property taxes that it can levy with that same assessment.⁸⁹ A municipality is deterred from making fraudulently low assessments solely to condemn property on the cheap because it would effectively nullify the municipality's ability to raise revenues and engage in budget planning.⁹⁰

84. See generally Tomasz Piskorski et al., *Securitization and Distressed Loan Renegotiation: Evidence from the Subprime Mortgage Crisis* 1–5 (Chi. Booth Sch. of Bus., Research Paper No. 09-02, 2010), available at <http://ssrn.com/abstract=1321646> (discussing factors to be considered in mortgage renegotiation).

85. Recall that the Mortgage Resolution Partners' proposed role as an intermediary was to screen homeowners that were good candidates for mortgage condemnation. See Mortgage Resolution Partners, *supra* note 35, at 9. Given that the local governments have as good an estimation of property values as any other organization, it is not beyond comprehension that municipalities themselves could also handle *some* of the aspects of credit screening homeowners for the appropriate loan modifications, pursuant to the mortgage condemnation.

86. Hockett, *It Takes a Village*, *supra* note 11, at 154–55.

87. See Foote et al., *supra* note 12, at 1–5.

88. Hockett, *Six Years*, *supra* note 42, at 10 n.19 (discussing the “extend and pretend” mentality of financial institutions).

89. Sterk & Engler, *supra* note 82, at 1066–74 (discussing the difficulties of reassessing property values for tax purposes).

90. *Id.* at 1070 (“[T]ax assessment is a political process; the ultimate responsibility for assessments rests on the shoulders of elected officials, and they have incentives to minimize any damage to their political careers that reassessment might generate.”). It is “fairly easy to forecast in advance the amount of revenue that the real-property tax in a particular locality will produce, thus facilitating the budget process.” *Id.*

C. JURISDICTION-TO-JURISDICTION, EMINENT DOMAIN POWERS VARY WITH RESPECT TO ONE-TO-ONE PROPERTY TRANSFERS

It is important to point out that Professor Hockett's plan may run afoul of many states' "anti-*Kelo*" statutes because it advocates one-to-one property transfers.⁹¹ Such statutes limit local governments' ability to condemn the property of one private party for the purpose of transferring it to another private party.⁹² Prohibitions on one-to-one property transfers are not necessarily specific to either tangible or intangible property and are certainly not limited to condemned mortgages.⁹³ However, local governments can satisfy anti-*Kelo* provisions if they can keep the mortgages without making a private transfer or conveyance.⁹⁴

II. MORTGAGE TAKINGS

Part II first demonstrates that the use of eminent domain to take intangible property such as contracts and mortgages is constitutional and given the same legislative deference as the taking or condemnation of real property.⁹⁵ Local governments and municipalities that wish to condemn home mortgages have to overcome the same constitutional hurdles to legitimately effect a taking but are subject to other limitations by the states. Secondly, this Part outlines condemnation proceedings generally and

91. *E.g.*, CAL. CONST. art. I, § 19 ("The State and local governments are prohibited from acquiring by eminent domain an owner-occupied residence for the purpose of conveying it to a private person."); MICH. CONST. art. X, § 2 ("Public use' does not include the taking of private property for transfer to a private entity for the purpose of economic development or enhancement of tax revenues."); *Norwood v. Horney*, 853 N.E.2d 1115, 1140-42 (Ohio 2006) (agreeing with Justice O'Connor's dissent in *Kelo v. City of New London*, 545 U.S. 469 (2005)).

92. It has been suggested that Professor Hockett's proposal would not work in the case of San Bernardino County because of a provision in the county charter that prohibits one-to-one property transfers by the county where the owner does not consent. OMM Memorandum, *supra* note 42, at 11. However, article VI, section 5 of the San Bernardino Charter lists the "Owner" as the "owner(s) of the fee title interest in the property to be acquired." SAN BERNARDINO CNTY. CHARTER art. VI, § 5, available at <http://www.co.sanmateo.ca.us/bos.dir/CharterReviewCommittee/SanBernardinoCharter.pdf>. In the case of either a deed of trust or a mortgage, the mortgagor-borrower is going to have equitable title. More importantly, the property being acquired is not the real estate property itself, as the San Bernardino Charter suggests, but the mortgage note, in which there is no "fee title interest" to speak of.

93. *Kelo* emphasized deference to legislatures when determining whether a taking was for a "public purpose." *Kelo*, 545 U.S. at 480. State legislatures are free to put limitations on the use of eminent domain; as mentioned, *supra* note 91, Michigan's Constitution has a public use provision that applies to private property generally. MICH. CONST. art. X, § 2. However, intuition about the force of anti-*Kelo* provisions is probably most relevant to real property takings.

94. If the property is not transferred, then *Kelo* analysis is avoided. Where there is a transfer, arguments that the taking advances local economics may not be sufficient. *See Bd. of Cnty. Comm'rs v. Lowery*, 136 P.3d 639, 642 (Okla. 2006) (holding in part that economic development was not considered a public use where the condemned property was transferred to a private party).

95. "The state or federal legislature may initially determine what constitutes a public use, but the courts have the final authority to decide whether this legislative determination is correct." Shelley Ross Saxer, *Eminent Domain, Municipalization, and the Dormant Commerce Clause*, 38 U.C. DAVIS L. REV. 1505, 1514 (2005).

expounds the legal precedent for condemning intangible property, like mortgage notes. Part II also surveys the procedural and jurisdictional challenges that are specific to condemnation proceedings of intangible property, as opposed to real property.

A. THE TAKINGS CLAUSE OUTLINED: PUBLIC PURPOSE, NECESSITY, AND COMPENSATION

The Fifth Amendment's Takings Clause requires that a taking of private property have a public purpose;⁹⁶ that the taking is in fact necessary to achieve that purpose;⁹⁷ and that just compensation⁹⁸ is made to the property owners for the taking.⁹⁹ For prospective mortgage condemnations under Professor Hockett's proposal, the most pertinent of these requirements is the public purpose requirement because mortgages will be condemned from one mortgagee to be refinanced by a new (private) mortgagee.¹⁰⁰

1. Public Purpose

In 2005, the Supreme Court addressed the legitimacy of one-to-one takings in *Kelo v. City of New London*:

On the one hand, it has long been accepted that the sovereign may not take the property of A for the sole purpose of transferring it to another private party B, even though A is paid just compensation. On the other hand, it is equally clear that a State may transfer property from one private party to another if future "use by the public" is the purpose of the taking¹⁰¹

The Court held that the City of New London's taking of residential properties, which the city intended to give to private developers as part of a larger economic program,¹⁰² was constitutional.¹⁰³ The Court reasoned that promoting economic development was a traditional government power and sufficient public purpose given that the city had "carefully formulated" an economic plan aimed at creating jobs and increasing tax revenue.¹⁰⁴ Just as

96. *Kelo*, 545 U.S. at 480 ("The disposition of this case therefore turns on the question whether the City's development plan serves a 'public purpose.' Without exception, our cases have defined that concept broadly . . .").

97. By inference, if a taking is for a public purpose, then it was necessary to accomplish that public purpose. *E.g.*, *Berman v. Parker*, 348 U.S. 26, 36 (1954) (stating that it is not for the courts to determine whether a taking is necessary to achieve the legislature's goal).

98. *United States v. Commodities Trading Corp.*, 339 U.S. 121, 123 (1950) ("This Court has never attempted to prescribe a rigid rule for determining what is 'just compensation' under all circumstances and in all cases. Fair market value has normally been accepted as a just standard.").

99. See REYNOLDS, *supra* note 79, at 525.

100. Hockett, *It Takes a Village*, *supra* note 11, at 156.

101. *Kelo*, 545 U.S. at 477.

102. *Id.* at 483–85.

103. *Id.* at 477.

104. *Id.* at 483–85.

important, the Court acknowledged that the use of eminent domain to effect a one-to-one transfer of property may benefit private parties and that such benefit is often incidental but necessary to achieving the underlying public purpose.¹⁰⁵

The *Kelo* decision—besides its analysis of one-to-one property transfers—was a reminder that the Supreme Court’s conception of public purpose is expansive enough to allow for novel justifications for the use of eminent domain. Two crucial precedents the *Kelo* Court cited, *Berman v. Parker*¹⁰⁶ and *Hawaii Housing Authority v. Midkiff*,¹⁰⁷ were also cases in which eminent domain was used to make one-to-one transfers of property interests. In *Berman v. Parker*, the Court upheld the District of Columbia Redevelopment Act of 1945,¹⁰⁸ which sought to condemn blighted areas for redevelopment, with some of the property being sold or leased to private parties.¹⁰⁹ The *Berman* Court characterized the District of Columbia’s exercise of eminent domain as a legitimate use of its “police power.”¹¹⁰ The Court further described it as “fruitless” to “attempt to define” the police powers with exactitude, including eminent domain, because such a “definition is essentially the product of legislative determinations addressed to the purposes of government—purposes neither abstractly nor historically capable of definition.”¹¹¹

In *Hawaii Housing Authority v. Midkiff*, the Court followed the *Berman* approach, upholding a Hawaii statute that condemned fee title in real property from lessors and transferred to lessees “in order to reduce the concentration of ownership of fee simple in the State.”¹¹² The statute’s purpose was to mitigate the “evils” of Hawaii’s centuries-old land oligopoly.¹¹³ The Court reiterated that its role is *not* to determine if the taking will actually fulfill the public purpose,¹¹⁴ nor is it for the Court to second-guess the legislature and its judgment about what steps should be taken to advance such purposes or whether those steps include eminent

105. *Id.* at 485 (citing *Ruckelshaus v. Monsanto Co.*, 467 U.S. 986, 1014 (1984)); *cf.* *Haw. Hous. Auth. v. Midkiff*, 467 U.S. 229, 245 (1984) (“A purely private taking could not withstand the scrutiny of the public use requirement; it would serve no legitimate purpose of government and would thus be void.”).

106. *Berman v. Parker*, 348 U.S. 26 (1954).

107. *Midkiff*, 467 U.S. 229.

108. District of Columbia Redevelopment Act of 1945, Pub. L. No. 79-592, 60 Stat. 790 (codified as amended at D.C. CODE § 6-101.01(a) (2001)).

109. *Berman*, 348 U.S. at 28.

110. *Id.* at 32.

111. *Id.*

112. *Midkiff*, 467 U.S. at 232.

113. *Id.* at 242.

114. *Id.*

domain.¹¹⁵ In sum, like *Kelo*, *Berman* and *Midkiff* exemplify the notion that eminent domain is “merely”¹¹⁶ a means to an end.¹¹⁷

The Supreme Court’s “broad and inclusive”¹¹⁸ conception of public purpose bodes well for mortgage condemnation proposals that envision private lenders stepping in to assume the condemned mortgages. In fact, much of what Professor Hockett has written about mortgage condemnations gets at the very core of the public purpose and welfare that is at stake for homeowners, mortgagees, and municipalities that consider mortgage takings as an option.¹¹⁹ The social consequences of foreclosure, default, and large sums of negative equity implicate the traditional purview of a local government’s police powers. Condemning mortgages to mitigate such circumstances is certainly no more novel an exercise of the eminent domain power than the aforementioned Supreme Court precedents. However, many *state* constitutions specifically limit one-to-one property transfers to a much greater extent than the Takings Clause.¹²⁰ Consequently, my proposal of publicly financed mortgage condemnations, with the mortgages held indefinitely by the municipalities, completely ameliorates the restrictions on one-to-one transfers and will likely reduce judicial scrutiny.

2. Necessity

The requirement of necessity for property takings is not centrally concerned with the Fifth Amendment’s Takings Clause as much as it is with constitutional or legislative obstacles posed by the states.¹²¹ Some states do not impose judicial scrutiny for the necessity requirement, while others require a taking to be *reasonably necessary* to carry out the designated public purposes.¹²² Generally, with the exception of egregious

115. *Id.* at 244 (“In such cases, government does not itself have to use property to legitimate the taking; it is only the taking’s purpose, and not its mechanics, that must pass scrutiny under the Public Use Clause.”); *cf. Berman*, 348 U.S. at 33 (“We do not sit to determine whether a particular housing project is or is not desirable.”).

116. *Berman*, 348 U.S. at 33.

117. This turn of phrase “means to an end” is used later in the discussion of possible dormant Commerce Clause challenges. *See infra* text accompanying note 200. In both instances, the phrase represents the idea that eminent domain itself is neither legitimate nor illegitimate, but rather the essential inquiry is in regards to the broader goals that condemnation accomplishes.

118. *Berman*, 348 U.S. at 33.

119. *See Hockett, It Takes a Village, supra* note 11, at 171–75.

120. *See REYNOLDS, supra* note 79, at 547 (“These measures, which have been enacted in one form or another in at least 42 states, have limited, or outright prevented, the use of condemnation to acquire property for economic development, and many have also re-defined what constitutes ‘blight’ for purposes of condemning property for urban renewal.”).

121. In *Berman v. Parker*, the necessity language is used in passing when referring to the legislatures determinations. *Berman*, 348 U.S. at 36. The necessity requirement has been somewhat collapsed into the public purpose analysis. *Id.* (“If the Agency considers it necessary in carrying out the redevelopment project to take full title to the real property involved, it may do so.”).

122. REYNOLDS, *supra* note 79, at 547–48.

abuses of eminent domain not consistent with plausible public purposes, courts accord great deference to a legislature or municipality's finding of necessity.¹²³

3. Just Compensation

The “*Armstrong* principle”¹²⁴ animates the just compensation provision of the Fifth Amendment’s Taking Clause, ensuring that the government does not make individual citizens bear the cost of a taking.¹²⁵ But this principle does not determine what compensation ought to be paid, or what compensation might be called *just*.¹²⁶ Rather, the Supreme Court has held that just compensation is synonymous with “fair market value.”¹²⁷ In *United States v. Miller*,¹²⁸ the Court explained fair market value as “what a willing buyer would pay in cash to a willing seller.”¹²⁹

The Supreme Court’s market-oriented language seems to assume a degree of efficiency and liquidity that permits a monetary value to be assigned as in an arm’s-length transaction. But the *Miller* Court recognized that condemnations, given the timing of the condemnations or the type of property or its location, present untold vagaries when assessing fair market value.¹³⁰ Each situation requires its own fact-intensive inquiry. This is certainly true for mortgage condemnations, where the value of the mortgage is not based on the underlying home’s value but on the present value of future payments—adjusted for the risk that those payments will not be made.¹³¹

123. *Id.* at 548 (“An example of such abuse of discretion is the situation in which a local government attempts to condemn land because the governing officials want to rid the community of the landowner, or because they find his use of the land undesirable.”).

124. John D. Echeverria, *Public Takings of Private Contracts*, 38 *ECOLOGY L.Q.* 639, 648 (2011) (using the phrase “*Armstrong* principle”).

125. “The Fifth Amendment’s guarantee that private property shall not be taken for a public use without just compensation was designed to bar Government from forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole.” *Armstrong v. United States*, 364 U.S. 40, 49 (1960).

125. *E.g.*, *United States v. Chandler-Dunbar Water Power Co.*, 229 U.S. 53, 81 (1913).

126. U.S. CONST. amend. V (Takings Clause).

127. *Chandler-Dunbar Water Power Co.*, 229 U.S. at 81.

128. *United States v. Miller*, 317 U.S. 369 (1943).

129. *Id.* at 374.

130. “Where, for any reason, property has no market resort must be had to other data to ascertain its value; and, even in the ordinary case, assessment of market value involves the use of assumptions, which make it unlikely that the appraisal will reflect true value with nicety.” *Id.*

131. $PV_0^{\text{due}} = C \left[\frac{1 - \frac{1}{(1+i)^n}}{i} \right] (1+i)$, where PV = present value; n = number of periods; C = monthly mortgage payment; and i = interest rate. KENT A. HICKMAN ET AL., *FOUNDATIONS OF CORPORATE FINANCE* 117 (2d ed. 2001).

A good analogy to valuing a single mortgage¹³² is the manner in which a bond market values a single bond issuance—the value of the single issuance is relative to the value of all other possible investments.¹³³ The liquidity and efficiency of the market, of course, influence what a “willing” purchaser would pay, but so do the hard numbers that lay behind the mortgage: the term of years, the mortgage’s interest rate, the risk-free rate, the yield curve, the mortgagor’s income, the home value, prospects for the housing market, and so on.¹³⁴ As important are the *soft* characteristics of the mortgage, such as the mortgagor’s marital status, job security, health, and credit history.¹³⁵ Consequently, valuing a mortgage is an actuarial feast for analysts, mathematicians, and speculators. In a condemnation proceeding, the financial engineering is left to the judge or the jury, who can review evidence and arguments submitted by the government and the condemnee to decide the monetary value.¹³⁶

B. THE POWER TO CONDEMN INTANGIBLE PROPERTY AND MORTGAGES

The power of both federal and state governments to condemn intangible forms of property under the Fifth Amendment’s Taking Clause is longstanding.¹³⁷ The abundance of Supreme Court precedent¹³⁸ supporting

132. Individual mortgages are not fungible instruments, unlike mortgage-backed securities or bonds. See Schwarcz, *supra* note 50, at 143 (explaining how the structure of mortgage-backed securities can permit more variance among parties and debt obligations).

133. See generally HICKMAN ET AL., *supra* note 131, at 137–57 (“Time Value Applications: Security Valuation and Expected Returns”).

134. Yuliya Demyanyk et al., *Determinants and Consequences of Mortgage Default*, SSRN, 2–18 (Jan. 2011), <http://ssrn.com/abstract=1706844> (demonstrating that a mortgagor’s credit score, which accounts for many factors, is a good predictor of default).

135. See Jason N. Houle & Danya Keene, *Getting Sick and Falling Behind: Health and the Risk of Mortgage Default and Home Foreclosure* 13 (Apr. 12, 2013) (unpublished manuscript), available at <http://paa2013.princeton.edu/papers/130301> (“The findings of this study show that worsening health, as measured by changes in health limitations from 2006–2008 and changes in chronic conditions from the age of 40–50 significantly increases the risk of default and home foreclosure between 2007–2010.”).

136. See CAL. CON. art. I, § 19 (“Private property may be taken or damaged for a public use and only when just compensation, ascertained by a jury unless waived, has first been paid to, or into court for, the owner.”). Cf. N.Y. EM. DOM. § 512 (West 2013) (“The court, after hearing the testimony and weighing the evidence, shall determine the compensation due the condemnees for damages as the result of the acquisition.”); CAL. CIV. PROC. § 1263.320 (West 2013) (“The fair market value of property taken for which there is no relevant, comparable market is its value on the date of valuation as determined by any method of valuation that is just and equitable.”).

137. For a comprehensive overview of contract takings, see Echeverria, *supra* note 124.

138. “All of this has been so long settled as to need only the citation of the many cases.” *City of Cincinnati v. Louisville & Nashville R.R.*, 223 U.S. 390, 400 (1912) (citing *Offield v. N.Y., New Haven, & Hartford R.R.*, 203 U.S. 372 (1906); *Long Island Water-Supply Co. v. City of Brooklyn*, 166 U.S. 685 (1897); *New Orleans Gas-light Co. v. La. Light & Heat Producing & Mfg. Co.*, 115 U.S. 650 (1885); *W. River Bridge Co. v. Dix*, 47 U.S. 507 (1848)); *Proprietors of Charles River Bridge v. Proprietors of Warren Bridge*, 36 U.S. 420 (1837).

the condemnation of intangibles, including franchises,¹³⁹ contracts,¹⁴⁰ options,¹⁴¹ rights of way,¹⁴² and titles in real property,¹⁴³ demonstrates that the ability of local governments to condemn home mortgages is a natural and foreseen extension of the power of eminent domain.¹⁴⁴ Indeed, the Court has explicitly recognized that the power of eminent domain embraces all forms of property to the extent that the condemned property (or property rights) can be defined:

[T]he right of every state to authorize the appropriation of *every description of property* for a public use is one of those inherent powers which belong to state governments, without which they could not well perform their great functions. It is a power not surrendered to the United States, and is untouched by any of the provisions of the Federal Constitution, provided there be due process of law; that is, a law authorizing it, and provision made for compensation. *This power extends to tangibles and intangibles alike.* A chose in action, a charter, or *any kind of contract*, are, along with land and movables, within the sweep of this sovereign authority.¹⁴⁵

Even so, eminent domain is often confounded in the context of contract takings¹⁴⁶ because the Contract Clause prohibits state governments from altering contract rights.¹⁴⁷ But the Contract Clause “is not a limitation upon the power of eminent domain.”¹⁴⁸ In *Omnia Commercial Co. v. United States*,¹⁴⁹ the Supreme Court divined the modern standard for determining when a contract is effectively condemned or “appropriated.”¹⁵⁰ In *Omnia*, the federal government “requisitioned” a steel company’s production of steel for an entire year, effectively displacing a purchaser who had contracted with the steel company to lock in a price for the entirety of 1918.¹⁵¹ World War I, of course, made steel a very scarce and valuable commodity, which meant that the purchaser, having lost the contract to the

139. *Dix*, 47 U.S. 507.

140. *Lynch v. United States*, 292 U.S. 571, 579 (1934) (“Valid contracts are property, whether the obligor be a private individual, a municipality, a state, or the United States.”).

141. *United States v. Petty Motor Co.*, 327 U.S. 372, 384 (1946).

142. *Louisville & Nashville R.R.*, 223 U.S. 390.

143. *Haw. Hous. Auth. v. Midkiff*, 467 U.S. 229 (1984).

144. *Legal Tender Cases*, 79 U.S. 457, 561 (1870) (“Can the poor man’s cattle, and horses, and corn be thus taken by the government when the public exigency requires it, and cannot the rich man’s bonds and notes be in like manner taken to reach the same end . . . ? Is it anything more than putting the securities of the capitalist on the same platform as the farmer’s stock?”).

145. *Louisville & Nashville R.R.*, 223 U.S. at 400 (emphasis added).

146. See Echeverria, *supra* note 124, at 654.

147. U.S. CONST. art I., § 10, cl. 1.

148. *Louisville & Nashville R.R.*, 223 U.S. at 400; see also *U.S. Trust Co. of N.Y. v. New Jersey*, 431 U.S. 1, 29 n.27 (1977) (“The States remain free to exercise their powers of eminent domain to abrogate such contractual rights, upon payment of just compensation.”).

149. *Omnia Commercial Co. v. United States*, 261 U.S. 502 (1923).

150. *Id.*

151. *Id.* at 507.

government, was forced to buy steel at higher market rates.¹⁵² The Court held that the requisition terminated the contract and that there was no taking because the government was not filling the shoes of one of the parties to the contract.¹⁵³ The Court distinguished between the “appropriation” and “frustration” of contracts, reasoning that the contract at issue was frustrated because the government was condemning the steel and not the contract rights to the steel—the subject matter of the contract instead of the contract itself.¹⁵⁴

The *Omnia* appropriation/frustration distinction elucidates a fundamental difference between the taking of real property and the taking of contracts.¹⁵⁵ When real property is condemned, the rights of all possible parties—in fact the entire world—are affected by the taking.¹⁵⁶ Conversely, when contracts such as promissory notes (debt) are condemned, only the rights of the contracting parties are affected.¹⁵⁷ These contract rights represent an intangible property interest in the contract that can be extinguished when the contract is condemned.¹⁵⁸ Practically, the taking of real property has a unilateral effect in the sense that the government exercises sole ownership over said property exclusive of everyone else.¹⁵⁹ However, a contract taking has bilateral effects since the government replaces a contracting party, assuming their rights and duties, while the remaining counterparty is still bound to perform under the contract.¹⁶⁰

These conceptual differences have crucial implications for the procedural aspects of mortgage condemnations, even though municipalities need only proceed in personam against the mortgagee to extinguish the mortgagee’s rights in the note. In order to adjudicate those rights, municipalities must first establish their authority or jurisdiction over both the mortgagee and the mortgage note.

C. SUBJECT-MATTER JURISDICTION

Unlike real property, the original mortgage notes owned by non-resident mortgagees are often physically outside the territorial jurisdiction or geographic boundaries of a state. A state’s power to condemn property within its boundaries is well established.¹⁶¹ Outside that territorial jurisdiction, courts have been unwilling to allow states to take movable

152. Echeverria, *supra* note 124, at 641.

153. *Omnia Commercial Co.*, 261 U.S. at 511–13.

154. *Id.* at 511 (“If the steel company had failed to comply with the requisition, what would have been the remedy? Not enforcement of the contract, but enforcement of the statute.”).

155. See Echeverria, *supra* note 124, at 667–69.

156. *Id.* at 642.

157. *Id.*

158. *Id.* at 642–43.

159. *Id.* at 667–69.

160. *Id.*

161. NICHOLS ON EMINENT DOMAIN § 2.02 (3d ed. 2013) (providing extensive case law).

personal or intangible property, as it abrogates the sovereignty of other states.¹⁶² Thus, each state's geographic borders also represent the scope of its subject-matter jurisdiction when exercising eminent domain.¹⁶³ Within each state, local or municipal governments can be authorized to condemn property beyond their territorial limits.¹⁶⁴ But extraterritorial takings must fulfill a local purpose, or be necessary to effect that purpose, for the condemning governmental authority.¹⁶⁵

Knowing the scope of subject-matter jurisdiction, it is still necessary to determine where the movable or intangible property is located, since unlike real property it can exist as a legally cognizable interest under multiple states' jurisdictions or can be physically moved from one jurisdiction to another.¹⁶⁶ Both federal and state laws traditionally have assigned a location or situs to the various forms of movable property in the varied contexts of property taxation, escheatment, and distribution of property in divorce proceedings.¹⁶⁷ For taxation and divorce, situs can exist in multiple jurisdictions simultaneously, but in the eminent domain context there is thought to be only one legal situs for each type of property.¹⁶⁸ This prevents multiple states from condemning such property and protects property owners from multiple condemnation actions against the same property.¹⁶⁹ But it requires using a situs rule, like in escheatment, that permits only one location, which consequently allows only one state to exercise subject-matter jurisdiction over the property.¹⁷⁰ For example, the doctrine of *mobilia sequuntur personam* is one method for determining situs that follows "the general principle that rights of ownership and transfer of movable property are determined by the law of the owner's domicile."¹⁷¹ In short, the owner's last known domicile determines which state has subject-matter jurisdiction over the owner's movable property.¹⁷²

Although it is somewhat antique, limiting situs to a single location is a fairly intuitive approach for most types of movable property and in most

162. See, e.g., *Mayor of Balt. v. Balt. Football Club, Inc.*, 624 F. Supp. 278, 284–85 (D. Md. 1985) (citing NICHOLS ON EMINENT DOMAIN, *supra* note 161, § 2.1).

163. NICHOLS ON EMINENT DOMAIN, *supra* note 161, § 2.07.

164. Marjorie A. Shields, *Validity of Extraterritorial Condemnation by Municipality*, 44 A.L.R. 6th 259 (2009).

165. *City of Oakland v. Oakland Raiders*, 646 P.2d 835, 844 (Cal. 1982) ("[E]xtraterritorial condemnation has been acknowledged when necessary to implement local condemnation.").

166. See Ellen Mufson, *Jurisdictional Limitations on Intangible Property in Eminent Domain: Focus on the Indianapolis Colts*, 60 IND. L.J. 389, 395–99 (1985) (discussing the situs of intangibles for tax purposes and arguing that intangibles should have the same situs as they would under the law of escheat).

167. *Id.* at 395–405; *Williams v. North Carolina*, 317 U.S. 287, 316 (1942).

168. NICHOLS ON EMINENT DOMAIN, *supra* note 161, § 2.07.

169. See *Mayor of Balt. v. Balt. Football Club, Inc.*, 624 F. Supp. 278, 287 (D. Md. 1985) (endorsing *mobilia sequuntur personam* in the context of condemning a sports franchise).

170. See Mufson, *supra* note 166, at 403–07.

171. BLACK'S LAW DICTIONARY 1094 (9th ed. 2009).

172. See *Balt. Football Club, Inc.*, 624 F. Supp. at 287.

cases wouldn't seem to offend either states' interests or property owners.¹⁷³ But it rests upon the legal fiction¹⁷⁴ that all condemned property interests are in only one place at any given time.¹⁷⁵ Again, for most forms of property this fiction is quite workable, but I argue that for modern mortgages it is unwieldy.¹⁷⁶ One need only consider the numerous and rarified property rights to which a mortgage note appertains, including the right to be paid, the right to a security interest, and the right to foreclose on real property.¹⁷⁷ These rights are formed under the state law where the homeowner and real property are located; and, perhaps more importantly, the enforcement of such rights, especially foreclosure, is naturally accomplished in the jurisdiction (forum) where the homeowner and real property are located.¹⁷⁸

The equities of adopting a bright-line situs rule for mortgage notes sufficiently ameliorate concerns that the exercise of eminent domain would violate states' rights and the due process rights of a non-resident mortgagee. First, the bright-line rule would provide the certainty to both states and mortgagees that, for the purposes of condemnation, the property rights in the mortgage note are not severable from the location of the real property. As distinguished from the other situs rules, like *mobilia sequuntur personam*, this proposed rule extinguishes any further inquiries into where the mortgagee is and their current domicile. Eminent domain purists can continue to proclaim that property can only be condemned in one state's jurisdiction, to the exclusion of all other states. Inversely, if the situs were determined by *mobilia sequuntur personam*, then the non-resident mortgagee's state of domicile would be able to exercise subject-matter

173. See Mufson, *supra* note 166, at 395–405.

174. “An assumption that something is true even though it may be untrue, made esp. in judicial reasoning to alter how a legal rule operates” BLACK'S LAW DICTIONARY, *supra* note 171, at 976 (definition of “legal fiction”).

175. *Texas v. Florida*, 306 U.S. 398, 429 (1939) (“In view of the enormous extent to which intangibles now constitute wealth, and the increasing mobility of men, particularly men of substance, the necessity of a single headquarters for all legal purposes, particularly for purposes of taxation, tends to be a less and less useful fiction.”).

176. See RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 222 (1971) (“The interests of the parties in a thing are determined, depending upon the circumstances, either by the ‘law’ or by the ‘local law’ of the state which, with respect to the particular issue, has the most significant relationship to the thing and the parties”); see also Mufson, *supra* note 166, at 394 (acknowledging that the Supreme Court has never reached the issue of whether it was permissible for states to condemn intangibles that are associated with several jurisdictions).

177. See Form No. 3200, *Single Family Multistate Fixed Rate Note*, FANNIE MAE, at 2, https://www.fanniemae.com/content/legal_form/3200w.doc (last visited Nov. 17, 2013) (“In addition to the protections given to the Note Holder under this Note, a Mortgage, Deed of Trust, or Security Deed (the ‘Security Instrument’), dated the same date as this Note, protects the Note Holder from possible losses which might result if I do not keep the promises which I make in this Note.”).

178. See GRANT S. NELSON & DALE A. WHITMAN, REAL ESTATE FINANCE LAW 135–44 (5th ed. 2007) (outlining mortgage theories and the rights mortgagees are entitled to under each theory).

jurisdiction to condemn the mortgage (and for what unearthly purpose?), to the exclusion of the state where the homeowner and real property are physically located. In sum, a rule like *mobilia sequuntur personam* does not account for the legal rights that mortgage transactions embody.¹⁷⁹

Second, the mortgagee's due process rights would not be obviated by my proposed bright-line situs rule because, already, the mortgagee's substantive rights meaningfully exist only in the state where the real property is located. Practically, this means that in order to collect on the debt or foreclose on the home to satisfy that debt, the mortgagee must rely on the courts and procedure within the same jurisdiction as the real property. These rights and interests, as will be demonstrated below, also allow those same courts to exercise personal jurisdiction over the mortgagee. Moreover, without considering the convenience of each jurisdictional venue, it is unclear how giving those courts subject-matter jurisdiction to condemn a mortgage note from a non-resident mortgagee would be either unconstitutional or unfair. In such a scenario, the mortgage note is condemned and the mortgagee can contest the taking. If the condemnation is affirmed, then the mortgagee will receive compensation.

Regardless of the mortgage note's situs, mortgagees already face the prospect that they will lose their security interest in the event that the mortgaged real property is condemned.¹⁸⁰ Condemning the mortgage note would present no additional hardships for the mortgagee.

D. DUE PROCESS & PERSONAL JURISDICTION

In addition to having subject-matter jurisdiction and complying with substantive due process when condemning notes, municipalities must accord mortgagees adequate procedural due process as guaranteed by the Fourteenth Amendment's Due Process Clause.¹⁸¹ A court or tribunal condemning the promissory note will be proceeding in personam against the mortgagee to take and extinguish their ownership interest in the note and mortgage.¹⁸² The preliminary issue then is whether state courts can

179. ROBERT KRATOVIL & RAYMOND J. WERNER, *MODERN MORTGAGE LAW AND PRACTICE* 147 (2d ed. 1981) ("The mortgage was drafted as an instrument given to secure a separate document that evidenced the mortgage debt. This separate document ultimately took the form a negotiable note. If default and foreclosure occurred, the sale reduced part, but not all, of the mortgage debt.").

180. NICHOLS ON EMINENT DOMAIN, *supra* note 161, § 5.03 ("When mortgaged property is taken by eminent domain, the mortgagee's rights against the land follow the award in equity, and he or she may, in suitable proceedings, have the mortgage debt satisfied out of that fund in advance of other creditors of the mortgagor or of an assignee of the award.").

181. U.S. CONST. amend. XIV, § 1.

182. *Shaffer v. Heitner*, 433 U.S. 186, 199 (1977) ("If a court's jurisdiction is based on its authority over the defendant's person, the action and judgment are denominated 'in personam' and can impose a personal obligation on the defendant in favor of the plaintiff. If jurisdiction is based on the court's power over property within its territory, the action is called 'in rem' or 'quasi in rem.'").

assert personal jurisdiction over a mortgagee or other party holding the promissory note, who is presumably a real person, a corporation, or a securitization trust; again, particularly when that party is outside the state's territory. Though states may choose to permit their respective courts to assert personal jurisdiction over litigants to the extent that the Constitution allows, states can also curtail that jurisdiction with a "long-arm" statute.¹⁸³ Such long-arm statutes vary by state, but are probably not an obstacle to condemnation proposal. Instead, greater challenges are posed by explicit state level limitations on eminent domain as discussed above.

In order to assert personal jurisdiction over a defendant, due process requires that a defendant—here the mortgagee—have sufficient or "minimum" contacts with the state that is exercising jurisdiction.¹⁸⁴ Determining whether there are minimum contacts requires an analysis of the "quality and nature of the activity" that a defendant has in or with the state.¹⁸⁵ In the context of condemning a mortgage note, the fact that a note is by definition a contract secured or collateralized by the underlying real property—the house within the municipality's jurisdiction—gives local courts a plausible means to assert jurisdiction over an out-of-state mortgagee, whose only connection with the forum is ownership of the mortgage's promissory note.¹⁸⁶ The in personam nature of asserting personal jurisdiction over the mortgagee's promissory note and the in rem nature of the real property, as the security interest embodied in the mortgage, seems to be an adequate combination of contacts and interests, which the Supreme Court said in *Shaffer v. Heitner*¹⁸⁷ could sustain quasi in rem (personal) jurisdiction.¹⁸⁸ The *Shaffer* Court foresaw a situation where

183. *E.g.*, CAL. CIV. PROC. § 410.10 (West 2013) ("A court of this state may exercise jurisdiction on any basis not inconsistent with the Constitution of this state or of the United States."); N.Y. C.P.L.R. § 302 (McKinney 2013).

184. *Int'l Shoe Co. v. Wash.*, Office of Unemployment Compensation & Placement, 326 U.S. 310, 316 (1945) (quoting *Milliken v. Meyer*, 311 U.S. 457, 463 (1940) ("[D]ue Process requires only that in order to subject a defendant to a judgment *in personam*, if he be not present within the territory of the forum, he have certain minimum contacts with it such that the maintenance of the suit does not offend 'traditional notions of fair play and substantial justice.'")).

185. *Id.* at 319.

186. "The note and mortgage are inseparable; the former as essential, the latter as an incident. An assignment of the note carries the mortgage with it, while an assignment of the latter alone is a nullity." *Carpenter v. Longan*, 83 U.S. 271, 274 (1872); *cf.* *Hockett, It Takes a Village*, *supra* note 11, at 165 (citing *Carpenter* and arguing that mortgage debt has situs in the state where the debtor is domiciled).

187. "[The Court's decision] should not be read to invalidate *quasi in rem* jurisdiction where real estate is involved." *Shaffer*, 433 U.S. at 219 (Stevens, J. concurring); *but see id.* at 220 (Brennan, J. concurring in part and dissenting in part) (declaring that quasi in rem jurisdiction was no longer "constitutionally viable").

188. RESTATEMENT (FIRST) OF JUDGMENTS § 32 (1942) ("Where a thing is subject to the power of a State, a proceeding may be brought to affect the interests in the thing not merely of particular persons but of all persons in the world. Such a proceeding is called a proceeding *in rem*, as distinguished from a proceeding brought to affect the interests in the thing of particular persons only, which is called a proceeding *quasi in rem*.").

personal jurisdiction could not be sustained purely in personam, though a party's rights to property within the forum would permit a court to legitimately assert jurisdiction:

[P]resence of property in a State may bear on the existence of jurisdiction by providing contacts among the forum State, the defendant, and the litigation. For example, when claims to the property itself are the source of the underlying controversy between the plaintiff and the defendant, it would be unusual for the State where the property is located not to have jurisdiction. In such cases, the defendant's claim to property located in the State would normally indicate that he expected to benefit from the State's protection of his interest.¹⁸⁹

So similar to the Court's hypothetical is a local government's condemnation of a mortgage or the mortgagee's promissory note where the mortgagee is a non-resident or otherwise unsusceptible to personal jurisdiction because the secured interest (in real property) is a significant contact with the forum.¹⁹⁰ Crucially, the Court discouraged dependence on the traditional forms of personal jurisdiction that attempt to rigidly classify contacts as between persons (or property) and a state.

The case for applying to jurisdiction *in rem* the same test of "fair play and substantial justice" as governs assertions of jurisdiction *in personam* is simple and straightforward. It is premised on recognition that "[t]he phrase, 'judicial jurisdiction over a thing', is a customary elliptical way of referring to jurisdiction over the interests of persons in a thing." This recognition leads to the conclusion that in order to justify an exercise of jurisdiction *in rem*, the basis for jurisdiction must be sufficient to justify exercising "jurisdiction over the interests of persons in a thing."¹⁹¹

If this were not enough,¹⁹² there is precedent supporting personal jurisdiction over a non-resident defendant on the sole basis that the resident

189. *Shaffer*, 33 U.S. at 207–08.

190. The *Shaffer* Court also suggests a separate policy argument: "The State's strong interests in assuring the marketability of property within its borders and in providing a procedure for peaceful resolution of disputes about the possession of that property would also support jurisdiction, as would the likelihood that important records and witnesses will be found in the State." *Id.* at 208.

191. *Shaffer*, 33 U.S. at 207.

192. THOMAS D. ROWE, JR. ET AL., CIVIL PROCEDURE 433 (2d ed. 2008) (citing *FleetBoston Fin. Corp. v. fleetbostonfinancial.com*, 138 F. Supp. 2d 121, 131–35 (D. Mass. 2001) and *Cable News Network L.P. v. cnews.com*, 162 F. Supp. 2d 484, 491 (E.D. Va. 2001)) ("Language in *Shaffer* suggests that minimum contacts analysis applies to both *in rem* and quasi *in rem* cases, and the whole approach of *Shaffer* seems to emphasize contacts rather than formal rules. But true *in rem* suits—those that are about ownership of the property, including ownership of a trademarked domain name—are quite different from *Shaffer*: A court determining ownership of property within its jurisdiction can argue that it must have jurisdiction over anyone with claims on the property. Courts are split on this question.")

plaintiff was indebted to the defendant.¹⁹³ Also, in *McGee v. International Life Insurance Co.*, the Supreme Court held that a California court asserting personal jurisdiction over a Texas insurance company was valid, where the insurer never maintained an office or agent in California, nor had it ever solicited or done business in California to obtain the disputed insurance policy.¹⁹⁴ The Court reasoned, “It is sufficient for purposes of due process that the suit was based on a contract which had substantial connection with that State.”¹⁹⁵ For condemnation purposes, this suggests that a mortgagee or an assignee who owns the mortgage’s promissory note ought to have some inclination that her rights are likely subject to the jurisdiction of the state or forum where the mortgaged residential property is located.¹⁹⁶ The municipality’s (or forum’s) interest in the real property and in having the power to adjudicate the rights of the resident-mortgagor validates the exercise of jurisdiction.¹⁹⁷

E. POSSIBLE DORMANT COMMERCE CLAUSE CHALLENGES ARE VAGUE AND CONTINGENT UPON THE ACTIONS OF EACH INDIVIDUAL STATE AND LOCAL GOVERNMENT

As is evident from the jurisdictional analysis, mortgage condemnation has the possibility of including mortgagees who are non-residents of a forum. Any extraterritorial effects from condemning mortgages bring concerns that local governments could directly or indirectly impact interstate commerce and thus violate the dormant Commerce Clause.¹⁹⁸ Without existing factual examples, a likely argument is that “eminent domain will be viewed as ‘merely the means to the end’ and courts would focus on whether the end, protecting the state interest . . . , violates the dormant Commerce Clause.”¹⁹⁹ Of course, under the proposed mortgage condemnation plans, nothing, and especially not interstate commerce, is being regulated.²⁰⁰ However, it is important to clarify that *any* power, no

193. “Indebtedness due from a resident to a non-resident of which bank deposits are an example is property within a State.” *Penning v. Fourth Nat’l Bank*, 243 U.S. 269, 271 (1917) (citing *Chi., R.I. & P. Ry. Co. v. Sturm*, 174 U.S. 710 (1899)); *see also* *Hockett, It Takes a Village*, *supra* note 11, at 165 n.128 (citing *Sturm*).

194. *McGee v. Int’l Life Ins. Co.*, 355 U.S. 220, 221–22 (1957).

195. *Id.* at 223.

196. *Cf. id.*; *Hanson v. Denckla*, 357 U.S. 235, 253 (1958).

197. “The State’s strong interests in assuring the marketability of property within its border and in providing a procedure for peaceful resolution of disputes about the possession of that property would also support jurisdiction, as would the likelihood that important records and witness will be found in the State.” *Shaffer*, 433 U.S. at 208 (1977).

198. OMM Memorandum, *supra* note 42, at 9–12.

199. *Saxer*, *supra* note 95, at 1523 (quoting *Berman v. Parker*, 348 U.S. 26, 33 (1954)).

200. “The Commerce Clause, however, permits only *incidental* [sic] regulation of interstate commerce by the States; direct regulation is prohibited.” *Edgar v. MITE Corp.*, 457 U.S. 624, 640 (1982) (citing *Shafer v. Farmers Grain Co.*, 268 U.S. 189, 199 (1925)); *but see* *Piedmont Triad Airport Auth. v. Urbine*, 554 S.E.2d 331, 344 (N.C. 2001) (“The dormant, or negative, Commerce

less than eminent domain, can be ill-used as a pretext for otherwise unconstitutional ends.²⁰¹

The Supreme Court's dormant Commerce Clause jurisprudence cautions local governments that their undertakings, if they cause extraterritorial effects or regulatory consequences for interstate commerce, must possess a legitimate local purpose and have an impact that is not disproportionately burdensome to interstate commerce.²⁰² Where both the underlying real property and homeowner-mortgagor are physically within the same municipality, there is no a priori basis to sustain a dormant Commerce Clause challenge.²⁰³ Moreover, municipalities have broad discretion when selecting which mortgages to condemn and can therefore avoid conflict; at least facially, there isn't a systematic preference for in-state mortgagees versus out-of-state mortgagees.²⁰⁴ But here, precedent provides minimal guidance.

F. THE CONDEMNATION PROCEEDING

In most jurisdictions, the first step on the path to condemnation is filing a petition, after which notice is given to the property owners.²⁰⁵ Condemning residential real estate typically has few obstacles regarding notice.²⁰⁶ However, with intangible properties like a mortgage, notifying the owner is less practical;²⁰⁷ with real estate, one knows at the very least where the property is located.²⁰⁸ Certainly, providing notice in mortgage condemnation proceedings requires notifying the homeowner (mortgagor),

Clause is awakened only when Congress has not acted 'to regulate Commerce . . . among the several States.'").

201. *Calder v. Bull*, 3 U.S. 386, 400 (1798) (Iredell, J. concurring) ("Without the possession of this power the operations of Government would often be obstructed, and society itself would be endangered. It is not sufficient to urge, that the power may be abused, for, such is the nature of all power, such is the tendency of every human institution . . . We must be content to limit power where we can, and where we cannot, consistently with its use, we must be content to repose a salutary confidence. It is our consolation that there never existed a Government, in ancient or modern times, more free from danger in this respect, than the Governments of America.").

202. *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970) (outlining the balance of local and interstate interests).

203. See *Leading Cases*, 122 HARV. L. REV. 276, 276–85 (2008).

204. See *Urbine*, 554 S.E.2d at 344 ("We find no case law that supports the proposition that the Commerce Clause is a sustainable defense to the condemnation of real property.").

205. JESSE DUKEMINIER & JAMES E. KRIER, *PROPERTY* 1116 (5th ed. 2002).

206. CAL. CIV. PROC. § 1240.030 (West 2012) (requirements of eminent domain); *id.* § 1245.235 (notice requirement for eminent domain); N.Y. EM. DOM. PROC. LAW § 501 (McKinney 2012) (vesting exclusive jurisdiction over eminent domain proceedings with the court of claims); *id.* § 202 (notice requirements for real property).

207. "In all acquisitions in which the court of claims has jurisdiction . . . , the condemnor . . . shall serve either by personal service or by certified mail, upon each condemnee a notice of acquisition" N.Y. EM. DOM. PROC. LAW § 502 (McKinney 2012) (service of notice of acquisition); *cf.* CAL. CIV. PROC. § 1245.235 (West 2012) (requiring first-class mail).

208. See *Pennoyer v. Neff*, 95 U.S. 714 (1878) (a good example of real property being the object of notice rather than the defendant).

lender (mortgagee), and, if need be, any third party that carries the deed of trust on the mortgage. This could be the original lender or some other institution like a title company or escrow service.²⁰⁹ Barring the unforeseen, finding the homeowner is elementary—he or she lives in the house. However, with the advent and proliferation of mortgage-backed securities, effecting notice may require an inquiry as to *where* the mortgagee is and *who* they are, since the original *mortgage lender of record* has sold the mortgage to a securitization trust or some other investor.²¹⁰

It was once common for deeds to be recorded with the actual or original mortgagee as the mortgagee of record, with any future assignment of the mortgage being recorded afterward.²¹¹ As the secondary market for mortgages has grown in recent years, it is more common for mortgage lenders to record a nominee, like Mortgage Electronic Registration Systems, Inc. (MERS),²¹² as the mortgagee of record so that assignees of the mortgage—often securitization trusts—are able to identify which mortgage they actually own.²¹³ Besides acting as a nominee for the original lender and for subsequent purchasers of the mortgage note, MERS has developed its own private recording system that has effectively displaced the function of public land recording offices.²¹⁴ Participants in both the primary and secondary mortgage markets have become accustomed to MERS, so much so that it is the de facto recording and information system

209. See *MBA Fact Sheet: The Role of Electronic Mortgage Registrations* MORTGAGE BANKERS ASS'N, 1–2 (Oct. 29, 2010), <http://www.mbaa.org/files/ResourceCenter/ForeclosureProcess/FactsontheroleofElectronicMortgageRegistration.pdf> [hereinafter *MBA Fact Sheet*].

210. Statutes requiring that the condemnee (here the mortgagee) be notified by certified mail is likely enough to rule out due process challenges. See *Mullane v. Cent. Hanover Bank & Trust Co.*, 339 U.S. 306, 314 (1950) (ruling that notice must employ a means that actually desires to inform the party and reasonably apprise them of suit). Where the condemnee is a large financial institution, Rule 4(h)(1)(B) of the Federal Rules of Civil Procedure provides some guidance. FED. R. CIV. P. 4(h)(1)(b) (providing that summons can be made on an agent authorized by law).

211. See *MBA Fact Sheet*, *supra* note 209, at 1–2.

212. See *id.* at 2–3. For an excellent example of the legal ambiguities that surround Mortgage Electronic Registration Systems' (MERS') role in the mortgage market, see *Bain v. Metro. Mortgage Grp., Inc.*, 285 P.3d 34, 36–41 (Wash. 2012) (Where MERS was listed as the “beneficiary” of the deeds of trust, the court held that MERS was in fact not the lawful beneficiary because it was not the holder of the promissory note on the mortgage.).

213. This practice is analogous to the manner in which The Depository Trust & Clearing Corporation holds publicly traded stocks in “street name” to clear and settle trades. See *Sample Offering Document Language Describing DTC and Book-Entry-Only-Issuance*, DEPOSITORY TR. COMPANY, at 3 (Dec. 2007), http://www.dtcc.com/downloads/legal/rules_proc/eligibility/Sample%20Language.pdf.

214. *FAQ, MERSCORP HOLDINGS, INC.*, <http://www.mersinc.org/information-for-homeowners/faq-information-for-homeowners#whatismers> (last visited Nov. 17, 2013); see also *MBA Fact Sheet*, *supra* note 209, at 2–3 (“Allowing [MERS] to serve as the mortgagee of record has relieved the pressures on the public land records caused by repeated transfers of mortgage rights (such as servicing and ownership rights), and thereby helps protect the accuracy and integrity of the chain of title.”).

for mortgages.²¹⁵ A large portion of mortgage assignments that were once recorded in public record offices (for a fee) are now handled by MERS, the perpetual nominee.²¹⁶ The practical consequence of the shift away from public recording is that it's no longer obvious (or publicly known) who the actual mortgagee is—the real party in interest.²¹⁷

Mortgage investors and securitization trusts that hold the mortgage notes can simply use MERS's eighteen-digit "mortgage identification number" to get the record information of the homeowner, as well as the trustee or custodian holding the deed underlying the mortgage.²¹⁸ Likewise, when a homeowner defaults, a lender or servicer can notify the mortgage investor so that the investor can exercise its rights in the mortgage—foreclosure, forbearance, loan modification, etc.²¹⁹ Fortunately, this private recording system can also be accessed by homeowners and government entities that are trying to find out who owns a particular mortgage.²²⁰

After finding the parties with an interest in the mortgage note—the homeowner, mortgage investor, and mortgage servicer—providing notice is typically not much more than sending them a notice of acquisition.²²¹ In many jurisdictions this can be done by mail, either first-class or certified.²²² Notified parties have an opportunity to protest the condemnation, sometimes first at a formal public hearing, then at trial.²²³

The procedural variations of condemnation trials are as numerous as the different jurisdictions. A summary of the trial is as follows:

[A] trial is held, at which the government must establish its authority to condemn (which means, in some jurisdictions, that the government must show that a taking is "necessary"). The court can give the government permission to enter and inspect the subject property; it may require the government to make a deposit as security for the eventual condemnation, in an amount based on the compensation estimated to be awarded at the end of the proceedings. Jurisdictions differ on the availability of a jury trial in condemnation actions (none is required under the United State Constitution). If there is a jury trial, it is typically the jury that determines just compensation; issues of public use and necessity are decided by the court. At the conclusion of a successful condemnation action (or within a prescribed time thereafter), the government must pay the compensation

215. See *MBA Fact Sheet*, *supra* note 209, at 2–3.

216. See *id.*

217. NELSON & WHITMAN, *supra* note 178, at 465–66.

218. *FAQ*, *supra* note 214.

219. NELSON & WHITMAN, *supra* note 178, at 465–66.

220. *MBA Fact Sheet*, *supra* note 211, at 2–3.

221. *E.g.*, N.Y. EM. DOM. PROC. LAW § 502 (McKinney 2012).

222. *E.g.*, *id.*; CAL. CIV. PROC. § 1245.235(b) (West 2012).

223. *E.g.*, CAL. CIV. PROC. § 1245.235(a).

awarded, plus interest, if any, accrued from the time of the taking
Dissatisfied condemnees may, of course, appeal.²²⁴

The trial often requires the condemning authority to provide extensive documentation that helps to determine and define the property being condemned.²²⁵ Here, a copy of the promissory note or mortgage documents is necessary, the *taking* of which may not be so much physical as legal.²²⁶ The judgment would extinguish the mortgagee's rights in the mortgage.²²⁷ The corollary here is that if the taking is deemed legitimate, the condemnee will spend much of her effort at trial arguing the fair market value of the property.²²⁸ In fact, both the government and the condemnee are mainly looking to the trial as a means to establish the requisite, or *just*, compensation—the condemnee desires as much compensation as possible, and the government seeks to pay what it can afford or a lesser amount. Again, valuing a mortgage is actuarial in nature and fact-intensive.²²⁹ Both local governments and sophisticated mortgage investors are well-suited to argue the value of mortgage notes, each having access to information that indicates the relevant value of the mortgages.²³⁰ The condemnee can appeal a condemnation judgment, though an appeal is almost certainly going to be a replay of the just compensation inquiry.²³¹

III. FINANCING MORTGAGE TAKINGS WITH MORTGAGE-BACKED MUNICIPAL BONDS

Municipalities are well advised to exhaust all of their options in pursuing a mortgage condemnation plan,²³² and Professor Hockett is right to point out that private lenders are a viable source of refinancing for condemned mortgages intended to be modified.²³³ The cost of private refinancing is totally dependent on the homeowner's financial circumstances and the value of residential property at the time of refinancing.²³⁴ Both the value of the residential property and a

224. DUKEMINIER & KRIER, *supra* note 205, at 1116.

225. CAL. CIV. PROC. § 1250.310 (listing what must be in the condemnation complaint); N.Y. EM DOM. §§ 401–06.

226. CAL. CIV. PROC. § 1268.210; N.Y. EM. DOM. § 405.

227. CAL. CIV. PROC. § 1268.210 (court order for possession); N.Y. EM. DOM. §§ 403–05.

228. CAL. CIV. PROC. §§ 1260.210–.250 (compensation procedure); N.Y. EM. DOM. §§ 501–14 (compensation procedure).

229. See Part II's discussion of just compensation and fair market value, *supra* notes 131–135.

230. See Part I's discussion of local government. Expert witnesses, such as financial analysts, might be capable of shedding light on the value of the mortgage. However, valuing one mortgage is an entirely different task than valuing a pool of mortgages. See *supra* notes 131–135.

231. CAL. CIV. PROC. § 1255.470; N.Y. EM. DOM. § 604.

232. Hockett, *It Takes a Village*, *supra* note 11, at 143–49.

233. *Id.* at 150.

234. *Id.* at 151 (describing how the municipalities can discount the condemned mortgage to the amount “corresponding to the level at which the mortgagor can obtain new financing in the mortgage loan market”).

homeowner's finances are subject to fluctuation, especially considering that the residential property is likely a distressed asset, and homeowners' finances can dramatically change if they are no longer overburdened by their existing mortgage.²³⁵ The implication is that private lenders are given the extremely difficult task of deciding rational lending terms for homeowners who could not afford their previous mortgages.

Private lending, therefore, is certainly an option, but it cannot be evaluated in a vacuum. The benefits and risks require a fact-intensive inquiry relevant to each situation, specific to each individual locality, residential property, and homeowner. Relatedly, my proposal to publicly finance mortgage condemnations through municipal bonds cannot be said to be inherently more economical than private lending. However, it does offer local governments a degree of certainty if they are concerned that private lenders will not be prepared to refinance the condemned mortgages on a scale that materially preserves homeownership in their community. It also assures that homeowners and citizens cannot be forced from their homes on the whim of a bank or servicer, since the mortgages, promissory notes, and deeds of trust would be all effectively under the ownership of the municipality.

The basic concept of publicly financed mortgage condemnations is to issue municipal bonds that will be used either to fund mortgage condemnations or to offset funds already used to condemn mortgages. The bonds that finance condemnations would be in a form very similar to *revenue bonds* in that refinanced mortgages would be used to pay down the bonds with their payment streams, while the residential property (or deeds) would collateralize the bond issuance.²³⁶ Functionally, this is quite similar to a mortgage-backed security. But unlike the private, mortgage-backed security, some municipal bond issuances allow for federal tax subsidy—or, more accurately, federal tax exemption.²³⁷

Federal tax exemptions for municipal bonds are governed by the Internal Revenue Code (the IRC).²³⁸ In order for municipal bonds to maintain federal tax exemptions, it is generally required that proceeds from bond issuances are neither used to fund private business nor made as loans to private entities.²³⁹ This policy of non-exemption for “private activity” bonds²⁴⁰ is designed to ensure that government entities do not subsidize

235. Foote et al., *supra* note 12, at 12.

236. JOEL A. MINTZ ET AL., FUNDAMENTALS OF MUNICIPAL FINANCE 3–6 (2010).

237. *See generally id.* at 93–106 (explaining federal taxation of municipal bonds).

238. I.R.C. § 149 (2012).

239. SHARON STANTON WHITE, PRIVATE ACTIVITY BOND TESTS § 1:5 (2012) (citing I.R.C. §§ 103(a), (b)(1), 141(c)(1)); *see also* Daniel Knepper, *Eliminating the Federal Subsidy in Kelo: Restricting the Availability of Tax-Exempt Financing for Redevelopment Projects*, 94 GEO. L.J. 1635, 1649–56 (2006) (explaining the private business use test and the private payment or security test).

240. *See* I.R.C. § 141(a).

their projects with tax proceeds the federal government would otherwise collect.²⁴¹ Still, there are certain exceptions or qualifications to the private activity policy, allowing for so-called “qualified” bonds,²⁴² which use bond proceeds to fund private activities that the IRC specifically subsidizes through federal tax exemption.²⁴³ The IRC even recognizes a municipal bond used to fund mortgage lending called a *qualified mortgage bond*.²⁴⁴ Unfortunately, these qualified mortgage bonds cannot be used to finance mortgage condemnations in the manner I propose because of two caveats stipulating that the bonds (1) cannot be used to replace existing mortgages²⁴⁵ and (2) the mortgagor-homeowner cannot recently have had a present ownership interest in the financed property.²⁴⁶ Qualified mortgage bonds are an ingenious carve-out in the tax code but are mainly designed for first-time homebuyers.²⁴⁷ Meeting the stipulations and requirements for a valid issuance of qualified mortgagor bonds is probably too onerous for the purposes of mortgage condemnations, though the IRC does admit some exceptions.²⁴⁸

A more appropriate bond for financing mortgage condemnations appears to be the *qualified redevelopment bond*.²⁴⁹ Qualified redevelopment bonds allow for tax-exempt municipal bond issuances where there is an adequate “redevelopment purpose”²⁵⁰ for designated areas of blight.²⁵¹ The two general requirements to achieve tax-exempt status under the qualified

241. Sean Carey, Note, *Post-Davis Conduit Bonds: At the Intersection of the Dormant Commerce Clause and Municipal Debt*, 78 *FORDHAM L. REV.* 121, 131 (2009) (“While the federal government ultimately bears the cost of this exemption, it gains a foothold in the municipal bond market. By setting the parameters for the federal tax exemption, the federal government can influence the purchases of bondholders; by influencing these purchases, the federal government influences the type of projects state and local governments fund.”).

242. See I.R.C. § 141(e); Knepper, *supra* note 239, at 1649 (“The Code calls these private activity bonds that are eligible for tax exemption ‘qualified private activity bonds.’”).

243. See Carey, *supra* note 241, at 130–34.

244. I.R.C. § 143.

245. *Id.* § 143(i)(A).

246. *Id.* § 143(d) (stating 3-year requirement).

247. The requirement that financing not be used for those who have had a present property interest in the underlying property for the previous three years infers a preference for first-time homebuyers.

248. Section 143(d)’s “3-year requirement” excepts financing that involves “targeted area residents.” I.R.C. § 143(d)(A), (j). Section 143(i)(1)’s requirement for new mortgages admits exceptions where the financing is for “bridge loans or similar temporary initial financing” and for the “qualified rehabilitation” of the underlying property. *Id.* § 143(i)(1)(B)(ii), (iii).

249. See *id.* §§ 141(e)(1)(F), 144(c).

250. See *id.* § 144(c)(3)(A). The redevelopment purpose conceivably satisfied by mortgagor condemnations is “the acquisition (by a governmental unit having the power to exercise eminent domain) of real property located in such area” *Id.* § 144(c)(3)(A)(1). Although a municipality would not be taking *possession* of the real property as such, it would be taking (acquiring) an interest in real property as a result of the mortgage condemnation.

251. Under section 144(c), blight is a broad condition “on the basis of the substantial presence of factors” including abandoned or vacant buildings and, most crucially, “delinquencies in payment of real property taxes.” *Id.* § 144(c)(4)(B).

redevelopment bond provision are (1) state authorization of such bond issuances²⁵² and (2) the formulation of a redevelopment plan that outlines how the blighted area will be remediated.²⁵³ Municipalities that intend to use qualified redevelopment bonds can first assess the level of economic distress or blight within their community, after which they can conjunctively structure their redevelopment plans and mortgage condemnation proposal to legitimize a bond issuance.²⁵⁴

The practical limitation for qualified redevelopment bonds is that they are capped at the state level to ensure that municipalities are not overusing the bonds as a loophole to excessive redevelopment—or development veiled as redevelopment.²⁵⁵ Whatever the limitations, municipalities should consult the IRC to see if their community could benefit from qualified bonds because the tax exemptions for such bonds ostensibly provide the cheapest cost of capital for refinancing condemned mortgages.

If municipalities cannot achieve tax-exempt status specifically for mortgage condemnation, they might nevertheless benefit from holding a portfolio of mortgages. Municipalities that have enough capital reserves to condemn and refinance mortgages might be able to attract lower interest rates on their general obligation bonds (that are tax-exempt). Local governments that demonstrate they are committed to reversing the housing decline in their respective communities may persuade investors that their local economies are stabilizing. Preserving homeownership, after all, is likely to improve property tax revenues and the overall fiscal health of a locality, making it a more attractive credit risk and a better place to reside.

Municipalities that engage in mortgage condemnation as part of a larger economic plan would be able to sell publicly refinanced mortgages at a later date—allowing municipalities to avoid the threat of insolvency or illiquidity as a result of holding too many mortgages. Even if none of these opportunities present themselves, municipalities could still use taxable municipal bonds to procure capital for mortgage condemnations.

CONCLUSION

The fate of mortgage condemnation proposals is uncertain. Such proposals have never been implemented, and there is no case law specific to the aforementioned legal issues in the context of mortgage takings. Moreover, tremendous public and private pressure may ultimately render mortgage condemnations as unpopular schemes of local governments or, more likely, financially and politically impractical. That I or anyone else finds plausible the condemnation proposals considered by Richmond,

252. *Id.* § 144(c)(2)(A)(i).

253. *Id.* § 144(c)(2)(A)(ii).

254. *See* Knepper, *supra* note 239, at 1656–58.

255. *See* I.R.C. § 146(a); Knepper, *supra* note 239, at 1658–60.

California, does not vitiate the very real obstacles posed outside the world of legal theory. Beyond the bounds of a mere academic or political exercise, the *worst* can and does happen, even when the law appears uniform and unambiguous. Accordingly, it is recommendable to be vigilant of legal contingencies that arise in the context of mortgage takings. For these reasons, the successful implementation of mortgage condemnation proposals would require—even more than plausible legal arguments—extremely adroit statecraft on the part of municipalities. And with conditions so variable at the local level, defining “success” is a judgment call to be made by citizens, who are unlikely to provide a consensus. Finally, it is a fair admonition that mortgage condemnations are not ideal. But I implore the reader to bear in mind that those unfortunate enough to be involved in circumstances fraught with financial and likely other personal or social conflicts might not be looking for an ideal solution.

*Jourdain B. Poupore**

* B.B.A., Gonzaga University, 2010; J.D. Candidate, Brooklyn Law School, 2014. This Note is dedicated to the memory of my loved ones who encouraged my legal studies but who I lost along the way: Grandma Susie, Uncle Frank, Uncle Jim, Cousin Lynn, and Aunt Cindy. I must thank the past and present leadership and staff of this Journal for making everything possible. In addition, I thank the numerous individuals who helped me as I stumbled through my research, including Professor David Reiss, Professor Matthew Keller, Professor Neil B. Cohen, Professor Beryl Jones-Woodin, and my friend Christopher Boling. I’m especially grateful for the opportunity to learn from the unfailing example set by Professor Alan Trammell, whose brilliance is only matched by his kindness. Finally, I thank my Mom, my Dad, and my brother Joey for showing me how to persevere.