# MUNICIPAL LIFEGUARDS: THE CONSTITUTIONALITY OF CONDEMNING AND REFINANCING UNDERWATER MORTGAGES


## ABSTRACT

*The recent foreclosure crisis has had a substantial effect on millions of individual homeowners and devastated communities across America. A solution to the problem of mass foreclosures has been elusive, but a recent proposal for municipalities to use their eminent domain authority to condemn underwater mortgages—a significant symptom of most foreclosures—and allow homeowners to refinance attempts to mitigate continued foreclosures. Opponents of the proposal argue that it fails the constitutional requirement that exercises of eminent domain be for "public use." This Note analyzes the purpose and mechanics of the eminent domain proposal in light of the U.S. Supreme Court's public use jurisprudence and concludes that the proposal would survive a constitutional challenge.*


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## I. INTRODUCTION

Currently, about one in every seven homes in the United States (about 7.1 million homes) is "underwater,"[1] meaning the homeowner owes

1. CORELOGIC, EQUITY REPORT: SECOND QUARTER 2013 2 (2013), *available at* http://www.corelogic.com/research/negative-equity/corelogic-q2-2013-equity-report.pdf.

more on the home than its market value.[2] There is a strong correlation between underwater mortgages and foreclosure,[3] and home foreclosures have a devastating effect not only on individuals, but on neighborhoods, cities, states, and the country as a whole.[4] The solution to this foreclosure crisis has eluded nearly everyone since it began, but a unique new plan proposes to slow the rate of foreclosures. The plan, which is being pitched to municipalities by Mortgage Resolution Partners (MRP),[5] proposes that municipalities use their eminent domain power to seize underwater mortgages, refinance the loans, and transfer the loans to new entities.[6] Proponents argue that this plan is well within municipalities' authority under the U.S. Constitution to take private property for public use, an authority known as eminent domain.[7] However, many of the banks holding these underwater mortgages, as well as other critics, argue that using eminent domain to seize underwater mortgages is unconstitutional because the mortgages are not being taken for a "public use" as required by the Takings Clause of the Fifth Amendment.[8] Further, opponents of this

2. The term "negative equity" is also used to describe the situation in which a homeowner's home is worth less than the amount of the loan it is securing. *See* Ruth Jackson, *The Return of Negative Equity*, MONEYWK. (Apr. 23, 2008), http://www.moneyweek.com/investments/property/the-return-of-negative-equity ("In short, if your house is currently worth less than your outstanding mortgage balance then you are in *negative equity*. Say you bought a house for [$]250,000 six months ago using a 100% 'interest-only' mortgage, so your repayments only cover the mortgage interest each month rather than reducing the original loan. If today the market value of the house has dropped to [$]245,000 then you are in negative equity to the tune of [$]5,000 (the property is worth [$]5,000 less than the loan that finances it).").

3. *See infra* Part III.

4. *See infra* Part IV.

5. MORTG. RESOLUTION PARTNERS, http://mortgageresolutionpartners.com/ (last visited Nov. 30, 2013). MRP is a self-described "Community Advisory firm working to stabilize local housing markets and economies by keeping as many homeowners with underwater mortgages in their homes as possible." *Id.* The company has more often been described as a venture-capital firm. *See, e.g.*, Alan Zibel, *Eminent Domain Furor Hits Capitol Hill*, WALL ST. J.: DEVELOPMENTS (Sept. 13, 2012), http://blogs.wsj.com/developments/2012/09/13/eminent-domain-furor-hits-capitol-hill/.

6. *See infra* Part II.

7. U.S. CONST. amend. V.

8. *See* Letter from Sec. Indus. & Fin. Mkts. Ass'n et al. to Alfred Pollard, Gen. Counsel, Fed. Hous. Fin. Agency 5 (Sept. 7, 2012), *available at* http://www.sifma.org/issues/item.aspx?id=8589940214 (follow "SIFMA and Other Associations Submit Comments to the FHFA on the Use of Eminent Domain to Restructure Performing Loans" hyperlink). The Securities Industry and Financial Markets Association is an association of securities firms, banks, and asset managers, with the main goal of "develop[ing] policies and practices which strengthen financial markets

proposal argue that it will have a contradictory effect on the housing market by introducing lenders and investors to "an unquantifiable new risk," which would "reduce the sources of funding for mortgage originators. This will cause originators to underwrite in a defensive manner, thereby reducing credit availability" in the jurisdictions that adopt such a plan.[9]

This Note does not offer comment on the utility of the proposed use of eminent domain to seize and refinance underwater mortgage loans in order to mitigate the rate of foreclosures in American cities, nor does it offer any projections on the likely effect its implementation would have. Rather, it discusses the proposal's details and whether it would survive a constitutional challenge under the U.S. Supreme Court's current Takings Clause jurisprudence. Part II of this Note details the "Municipal Plan" to seize and refinance underwater mortgage loans using eminent domain. Part III analyzes the correlation between negative equity and foreclosure, followed by a discussion of the negative externalities of foreclosures in Part IV. Supreme Court decisions detailing the scope of the Fifth Amendment's public use requirement are examined in Part V. Finally, Part VI discusses the likelihood that this exercise of eminent domain would fall within the Court's definition of "public use" and pass constitutional muster.

## II. THE MUNICIPAL PLAN

Professor Robert Hockett of Cornell Law School has provided a blueprint detailing the process by which municipalities seize underwater mortgages and work with the homeowner to refinance the home in an attempt to avoid foreclosure.[10]

### A. *Mechanics of the Plan*[11]

The Plan consists of three steps: condemnation, compensation, and mortgage loan modification.[12]

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and which encourage capital availability, job creation and economic growth while building trust and confidence in the financial industry." *Mission*, SIFMA, http://www.sifma.org/about/mission/ (last visited Nov. 30, 2013).

9. Letter from Sec. Indus. & Fin. Mkts. Ass'n et al., *supra* note 8, at 2.

10. Robert 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, 149–57 (2012).

11. Going forward, the Author refers to the Municipal Plan proposal as simply "the Plan."

12. Hockett, *supra* note 10, at 149.

The first step, condemnation, involves municipalities identifying qualifying underwater mortgage loans and then acquiring them from their current holders.[13] Originally, it was MRP's intent that municipalities purchase all underwater mortgages; however, each local government must independently determine the scope of its own Plan.[14] Financial realities and prudential concerns might require a government to develop more narrow criteria that mortgages should meet to qualify for inclusion in the Plan.[15]

In identifying mortgages for condemnation, a local government might focus on three criteria, identifying loans that are (1) deeply underwater, defined as having a loan-to-value ratio greater than 125 percent; (2) securitized; and (3) current, meaning the homeowner has not yet missed a mortgage payment.[16] These criteria are designed to provide realistic assistance to both homeowners and municipalities.[17]

The first criterion targets mortgage loans that are deeply underwater. This is arguably the most important criterion because the ultimate goal of the Plan is to prevent foreclosure, and there is a strong correlation between negative equity and the likelihood of default, which is the first step of a process that results in foreclosure.[18]

The second criterion, that the mortgage loans be securitized, is

13. *Id.* at 150–51. The Plan can be executed by individual local units of government or by forming a "Joint Powers Authority," as was done by the Cities of Fontana, Ontario, and the County of San Bernardino in California. HOMEOWNERSHIP PROTECTION PROGRAM JOINT POWERS AUTHORITY, http://www.homeownershipjpa.org/home.aspx (last visited Nov. 30, 2013).

14. Interview with John Vlahoplus, Founder and Chief Strategy Officer, Mortgage Resolution Partners, in Des Moines, Iowa (Sept. 28, 2012) [hereinafter Vlahoplus Interview].

15. *Id.*

16. *Id.* These criteria are based on an analysis by the Federal Housing Finance Agency. FHFA Analyses of Principal Forgiveness Loan Modifications 6, 11 tbl.7, *in* Letter from Edward J. DeMarco, Acting Dir., Fed. Hous. Fin. Agency, to Elijah E. Cummings, Ranking Member, U.S. House Comm. on Oversight & Gov't Reform (Jan. 20, 2012), *available at* http://www.fhfa.gov/webfiles/23056/principalforgivenessltr12312.pdf (showing that lenders would have a greater than 50 percent reduction in losses by modifying "[s]ecuritized loans that are fewer than 90 days delinquent and have a [loan-to-value ratio greater than or equal to] 125").

17. *See infra* notes 19–24 and accompanying text for an explanation of why these criteria were chosen.

18. *See infra* Part III for a more in-depth discussion of the relationship between negative equity and foreclosure.

necessitated by the nature of securitized loans themselves.[19]

> When a mortgage is securitized, the borrower does not have a direct relationship with the person who is receiving the borrower's payments. Instead, the mortgage loans are gathered into a pool that is owned by a trust. The trust issues certificates that are purchased by investors and that entitle them to be paid according to specified terms and a specified seniority structure. A servicer is engaged to service the loans on behalf of the trust and the certificateholders.[20]

Hockett describes the "collective action problem[s]" resulting from the "uncoordinated decisions" of multiple lenders, which prevent lenders from modifying individual mortgages to prevent foreclosure despite the fact that doing so would be ultimately beneficial to the lenders.[21] He describes the issue as such:

> Because securitized creditors are too dispersed to act in concert . . . the pooling and servicing agreements (PSAs) pursuant to which mortgage loans are aggregated vest authority to collect loan payments in a single collective agent—the servicer, typically a banking institution. But the same PSAs' terms often flatly prohibit, or otherwise strictly limit—for example, through supermajority consent requirements—servicers from modifying pooled loans. They also prohibit or limit their *selling* such loans.[22]

These limitations make it very difficult for a homeowner to work with his or her loan servicer to modify the homeowner's mortgage in order to avoid default.

The third criterion is a prudential concern. Homeowners who have already defaulted, or who have not made a mortgage payment in more than

19. *See* Hockett, *supra* note 10, at 139.

20. JOHN P. HUNT, BERKELEY CTR. FOR LAW, BUS. & ECON., WHAT DO SUBPRIME SECURITIZATION CONTRACTS ACTUALLY SAY ABOUT LOAN MODIFICATION?: PRELIMINARY RESULTS AND IMPLICATIONS 1 (2009), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1369286.

21. Hockett, *supra* note 10, at 127.

22. *Id.* at 139–40 (footnote omitted); *see also* Tomasz Piskorski et al., *Securitization and Distressed Loan Renegotiation: Evidence from the Subprime Mortgage Crisis* 28 (Chi. Booth Sch. of Bus., Research Paper No. 09-02, 2010), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1321646 (analyzing data from the Office of the Comptroller of the Currency and Office of Thrift Supervision and finding a much higher rate of modification for nonsecuritized loans, corresponding to a higher rate of foreclosures among securitized loans).

three months, may be unlikely to avoid foreclosure.[23] Again, the ultimate goal of the Plan is to prevent foreclosure. Therefore, going through the process of condemning and refinancing mortgage loans that remain highly likely to foreclose does not benefit either the homeowner or the municipality.

According to both Hockett and John Vlahoplus, the founder and chief financial officer of MRP, the Plan is simply a blueprint, but in practice each municipality will use its own criteria and evaluate its ability to attract capital when deciding which types of mortgages it will seize.[24]

The next step in the process is providing just compensation to the mortgage holder, as required by the Constitution.[25] This is the role of companies like MRP, who act as advisors to individual municipalities and attract investors to provide the up-front capital needed to condemn the mortgages identified by the municipality.[26] Just compensation is determined based on an appraisal of the loans' value and is paid to the holder of the loans out of an account administered by each municipality consisting of the investors' funds.[27]

Finally, the homeowner whose mortgage was condemned will seek refinancing that will ultimately reduce his or her principal, thereby rescuing the homeowner from the underwater mortgage and, theoretically, preventing foreclosure.[28] The proceeds of the refinancing are then conveyed to the investors as repayment for the up-front capital they provided to finance the condemnations.[29]

23. Vlahoplus Interview, *supra* note 14; *see also* FHFA Analyses of Principal Forgiveness Loan Modifications, *supra* note 16, at 11 tbl.7 (showing the longer a borrower is delinquent, the less likely a lender is able to mitigate its losses by modifying the loan).

24. Vlahoplus Interview, *supra* note 14; Hockett, *supra* note 10, at 155 ("[T]he Plan enables localities flexibly to tailor criteria to varying local circumstances," and "over time [municipalities] will presumably adjust the criteria in keeping with their own local needs and legislative judgments.").

25. U.S. CONST. amend. V ("[P]rivate property [shall not] be taken for public use, without just compensation."); *see infra* note 75 for an explanation of why the constitutionality of the Plan's compensation scheme is outside the scope of this Note.

26. Vlahoplus Interview, *supra* note 14.

27. Hockett, *supra* note 10, at 154.

28. *Id.* at 151.

29. *Id.*

### B. *HAMP and HARP*

In addition to the collective action problems described above, the Plan is also a response to what Hockett and others see as the failure of federal attempts at foreclosure mitigation, most notably the Home Affordable Mortgage Program (HAMP) and the Home Affordable Refinance Program (HARP).[30] HAMP is a voluntary program through which qualifying borrowers have their monthly payments reduced to 31 percent of their income.[31] HARP allows homeowners to refinance if (1) their mortgages are owned or guaranteed by Fannie Mae or Freddie Mac, (2) they have insufficient equity to qualify for a traditional refinance, and (3) they are current on their payments.[32] HARP's shortcoming, according to Hockett, is that it does not address the most serious need of homeowners with negative equity—principal reduction.[33] HAMP, despite being designed to incentivize principal reduction, is a voluntary program and therefore is restrained by the same collective action problems preventing borrowers and lenders from negotiating principal reduction themselves.[34]

## III. NEGATIVE EQUITY AND FORECLOSURE

The purpose of the Plan is to prevent, or at least mitigate, the effects mortgage foreclosures have on communities.[35] While the Plan does not necessarily address homes already in foreclosure, it addresses a significant symptom of many foreclosures—negative equity.[36] By targeting mortgages

30. *Id.* at 136 n.67, 146–47.

31. FED. RESERVE BD., THE U.S. HOUSING MARKET: CURRENT CONDITIONS AND POLICY CONSIDERATIONS 18 (2012), *available at* http://www.federalreserve.gov/publications/other-reports/files/housing-white-paper-20120104.pdf.

32. *Id.* at 15.

33. Hockett, *supra* note 10, at 146.

34. *See id.* at 146; *supra* notes 19–22 and accompanying text (discussing the collective action problems facing borrowers and lenders interested in loan modification).

35. See *infra* Part IV for a discussion of the negative effects foreclosures have on communities.

36. *See* Helen Mason, *No One Saw It Coming*—Again*: Systemic Risk and State Foreclosure Proceedings: Why a National Uniform Foreclosure Law Is Necessary*, 67 U. MIAMI L. REV. 41, 65 (2012) ("Price declines and loss of homeowner equity are central contributors to mortgage default."); Stan Liebowitz, Op-Ed., *New Evidence on the Foreclosure Crisis*, WALL ST. J. (July 3, 2009), http://online.wsj.com/article/SB124657539489189043.html (examining a national database of individual loans and concluding "the single most important factor" in foreclosures is whether the

with negative equity, the Plan seeks to prevent foreclosures and the negative externalities that result.[37] Before examining the effect of foreclosures on municipalities, a more detailed look at the connection between present negative equity and future foreclosure is necessary.

For the Plan to survive constitutional scrutiny, there must be a rational basis for refinancing underwater mortgages to avoid foreclosure.[38] For that rational basis to exist, there must be a correlation between negative equity and foreclosure.

In a report to Congress on the root causes of the foreclosure crisis, the Department of Housing and Urban Development noted "there is always a strong association between negative home equity and the likelihood of foreclosure."[39] Negative equity, however, is rarely the lone impetus for default,[40] as studies indicate most homeowners will continue making payments on an underwater mortgage to avoid foreclosure.[41] Rather, the most common circumstance for default occurs when negative

homeowner had negative equity).

37. *See* Hockett, *supra* note 10, at 166.

38. *See* Kelo v. City of New London, 545 U.S. 469, 487–88 (2005) (holding that the courts' role in examining an exercise of eminent domain is simply to determine whether "the legislature's purpose is legitimate and its means are not irrational" (quoting Haw. Hous. Auth. v. Midkiff, 467 U.S. 229, 242–43 (1984))).

39. OFFICE OF POLICY DEV. & RESEARCH, U.S. DEP'T OF HOUS. & URBAN DEV., REPORT TO CONGRESS ON THE ROOT CAUSES OF THE FORECLOSURE CRISIS 16 (2010).

40. The technical definition of a mortgage default is when the homeowner "has missed three payments and a fourth is due." *Id.* at 15 n.26. While a majority of defaults are resolved before a foreclosure occurs, a default will result in the initiation of the foreclosure process. *Id.* In other words, default describes the status of a homeowner, while foreclosure is a bank-initiated process ultimately resulting in the acquisition of the home by the bank.

41. *See, e.g.*, Brent T. White, *Underwater and Not Walking Away: Shame, Fear, and the Social Management of the Housing Crisis*, 45 WAKE FOREST L. REV. 971, 972, 976 (2010) (showing fewer than one-fourth of underwater homeowners voluntarily walk away from underwater mortgages and arguing most underwater homeowners choose not to default (1) to avoid the negative stigma associated with foreclosure, and (2) because of their fear of the perceived consequences of foreclosure); Neil Bhutta et al., The Depth of Negative Equity and Mortgage Default Decisions 27 (Fed. Reserve Bd. Divs. of Research & Statistics & Monetary Affairs, Fin. & Econ. Discussion Series No. 2010-35, 2010), *available at* http://www.federalreserve.gov/pubs/feds/2010/201035/201035pap.pdf (finding that the median homeowner will not walk away from an underwater mortgage until equity in the home drops to -62 percent of the home's value).

equity is coupled with a "triggering event."[42] A triggering event is one that causes significant financial difficulty for the homeowner, such as job loss or major healthcare expenses.[43] However, a triggering event alone, without negative equity, is typically insufficient to result in default because homeowners with positive equity can absorb the financial shock by selling their home to meet their mortgage obligation or can refinance to a more affordable rate.[44] Homeowners with negative equity are less likely to be able to absorb a financial blow without default because refinancing is not an option, and selling will not fully cover their mortgage obligation.[45]

What these studies show is that "for the vast majority of homeowners, negative equity is a necessary . . . condition for default,"[46] which itself is a necessary condition of foreclosure.[47]

## IV. EFFECTS OF FORECLOSURE

Hockett succinctly described the effects of home foreclosures on a local economy: "Mass foreclosures and expected foreclosures further depress home prices, which further depress consumer expenditures, which further depress employment and income, which further heighten the incidence of default and foreclosure, which further depress home prices—and so on, snowballing again."[48] These effects are borne out by a number of studies.

A 2007 special report from the Joint Economic Committee of the United States Congress measured the impact foreclosures have on families, businesses, local governments, and neighboring homeowners, and determined that each foreclosure has an economic cost of up to $80,000 when combining the effect on each group.[49]

42. OFFICE OF POLICY DEV. & RESEARCH, *supra* note 38, at 15; *see also* White, *supra* note 41, at 976 (noting that three quarters of all defaults are the result of a combination of negative equity and some triggering event).

43. White, *supra* note 41, at 976; *see also* FED. HOUS. FIN. AGENCY, FORECLOSURE PREVENTION REPORT: SECOND QUARTER 2012 36 (2012) (showing that the top five reasons for delinquency are curtailment of income, excessive obligations, unemployment, illness of principal mortgagor or family member, and marital difficulties).

44. *See* OFFICE OF POLICY DEV. & RESEARCH, *supra* note 39, at 15.

45. *See id.*

46. White, *supra* note 41, at 976–77.

47. *See* OFFICE OF POLICY DEV. & RESEARCH, *supra* note 39, at 15.

48. Hockett, *supra* note 10, at 135–36 (footnote omitted).

49. JOINT ECON. COMM., SHELTERING NEIGHBORHOODS FROM THE

A 2006 study, conducted by Dan Immergluck and Geoff Smith, measured the impact of a foreclosure on nearby property values over a two-year period in Chicago and conservatively estimated that there is a 0.9 percent decrease in value of every single-family home within an eighth of a mile of each foreclosure.[50] Over the period of the study, 3,750 homes were foreclosed, amounting to a $598 million reduction in property values—an average of $159,000 per foreclosure.[51] A less conservative estimate of the same study suggests that a foreclosure results in a 1.136 percent decline in property values within an eighth of a mile, resulting in a $1.39 billion loss in property value in Chicago over the two-year period—an average of $371,000 per foreclosure.[52] Aside from the substantial impact on property values, the Immergluck and Smith study also found that an "increase of one standard deviation in the foreclosure rate (about 2.8 foreclosures for every 100 owner-occupied properties in one year) corresponds to an increase in neighborhood violent crime of approximately 6.7 percent."[53]

Another study, also focused on Chicago, measured the direct costs of a single foreclosure on the city. The study found that "foreclosures trigger significant direct expenditures for increased policing and fire suppression, demolition contracts, building inspections, legal fees, and expenses associated with managing the foreclosure process (*e.g.*, recordkeeping/updating)."[54] Analyzing the direct expenditures that would need to be made by the city in the event of a foreclosure, the study found that the municipal costs can range from $27, if the home transfers smoothly from the borrower to a foreclosure investor, to $34,199, if the home is both abandoned and damaged by fire.[55]

The study also noted "foreclosures tend to cluster in low-income and/or minority neighborhoods, [therefore] many of the outsider effects

SUBPRIME FORECLOSURE STORM 17 (2007), *available at* http://www.jec.senate.gov/archive/Documents/Reports/subprime11apr2007revised.pdf.

50. 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 (2006).

51. *Id.*

52. *Id.* at 58.

53. *Id.* at 59.

54. WILLIAM C. APGAR & MARK DUDA, HOMEOWNERSHIP PRES. FOUND., COLLATERAL DAMAGE: THE MUNICIPAL IMPACT OF TODAY'S MORTGAGE FORECLOSURE BOOM 6 (2005), *available at* http://www.995hope.org/wp-content/uploads/2011/07/Apgar_Duda_Study_Short_Version.pdf.

55. *Id.* at 12, 15.

are concentrated among the nation's most vulnerable households."[56] This unfortunate fact is due largely to the growth of "subprime" mortgage loans, which have been given disproportionally to those in minority and lower income communities.[57] For instance, a study of home mortgage loans given across the country in 2006 shows "a majority of African Americans (53.7 percent) and a near majority of Latinos (46.6 percent) received loans described in the data as [subprime]. The corresponding measurement among white non-Latino borrowers was 17.7 percent."[58]

Subprime mortgages are categorized by both the type of borrower and the type of loan.[59] A subprime borrower is one "who, according to a particular lender's underwriting standards and the lender's assessment and categorization of the borrower, does not qualify for a loan at a conventional mortgage rate."[60] And the "hallmark of a subprime loan is a high interest rate and high points or fees charged at the time the loan is closed."[61] Another typical characteristic of subprime loans is that they require little or no down payment.[62] For a borrower with an initial loan-to-value ratio of 100 percent, any decrease in the home's value will immediately cause the homeowner to be in negative equity.[63] Subprime loans, according to Immergluck and Smith, are between 10 and 40 times more likely than prime loans to foreclose.[64] According to a 2012 Fannie Mae report, nearly 70 percent of the subprime mortgages held in private-label securities are projected to default.[65]

56. *Id.* at 9 (footnote omitted).

57. Immergluck & Smith, *supra* note 50, at 63. To illustrate the extent of the foreclosure crisis in urban, predominantly minority areas, Immergluck and Smith included a map showing the high concentration of foreclosures in predominately minority areas in Chicago and surrounding communities. *Id.* at 62 fig.2.

58. Keith S. Ernst & Deborah N. Goldstein, *The Foreclosure Crisis and Its Challenge to Community Economic Development Practitioners*, 17 J. AFFORDABLE HOUSING & COMMUNITY DEV. L. 273, 276 (2008) (footnotes omitted).

59. *See* Cathy Lesser Mansfield, *The Road to Subprime "HEL" Was Paved with Good Congressional Intentions: Usury Deregulation and the Subprime Home Equity Market*, 51 S.C. L. REV. 473, 532–34 (2000).

60. *Id.* at 532–33 (footnote omitted).

61. *Id.* at 535 (footnote omitted).

62. *See* Christopher Mayer et al., *The Rise in Mortgage Defaults*, J. ECON. PERSP., Winter 2009, at 27, 31 & tbl.2B (showing that the median subprime home buyer in 2005 and 2006 made no down payment on his loan).

63. *See supra* Part III for a discussion of the correlation between negative equity and foreclosure.

64. Immergluck & Smith, *supra* note 50, at 63.

65. Fed. Nat'l Mortg. Ass'n, Quarterly Report Pursuant to Section 13 or

The discussion above demonstrates the perfect storm facing major metropolitan areas around the country: high concentrations of minority residents who were targeted for and received a disproportionately high percentage of subprime mortgages, the high likelihood that those subprime mortgages will result in foreclosure, and the adverse effects of foreclosures on the surrounding community.

## V. U.S. SUPREME COURT "PUBLIC USE" JURISPRUDENCE

A government's authority to take private land for public use predates the U.S. Constitution.[66] Recognition of the authority can be found as early as 1625.[67] The power of the government to take private land is "inherent in sovereignty, and exists in a sovereign state without any specific recognition."[68] Nonetheless, the Framers chose to codify this inherent power in the Constitution and limit its exercise to takings for public use and require that just compensation be paid.[69] On its face, the Fifth Amendment, which authorizes eminent domain, applies only to the federal government.[70] However, through the Due Process Clause of the Fourteenth Amendment, the Court has applied the limitations of the Fifth Amendment's Due Process Clause to state and local governments.[71]

Three elements must be met for a governmental unit to constitutionally exercise authority under the Takings Clause: there must be an actual taking;[72] the property must be taken "for public use;"[73] and "just

15(d) of the Securities Exchange Act of 1934 (Form 10-Q) 111 (Aug. 8, 2012), *available at* http://www.fanniemae.com/resources/file/ir/pdf/quarterly-annual-results/2012/q22012.pdf.

66. *See* 26 AM. JUR. 2D *Eminent Domain* § 3 (2004).

67. *See* Hockett, *supra* note 10, at 157 & 157 n.107 (quoting HUGO GROTIUS, DE JURE BELLI AC PACIS (Francis W. Kelsey trans., Clarendon Press 1925) (1625), *available at* http://www.lonang.com/exlibris/grotius/index.html).

68. 26 AM. JUR. 2D, *supra* note 66, § 3.

69. U.S. CONST. amend. V.

70. *Id.*; *see* Barron v. City of Baltimore, 32 U.S. 243, 247 (1833) ("[T]he fifth amendment must be understood as restraining the power of the [federal] government, not as applicable to the states.").

71. *See* Fallbrook Irrigation Dist. v. Bradley, 164 U.S. 112, 158 (1896) ("[T]he citizen is deprived of his property without due process of law, if it be taken by or under state authority for any other than a public use . . . .").

72. The Court has identified three significant factors in determining whether a government action amounts to a "taking" within the meaning of the Fifth Amendment: (1) the "economic impact" of the government action on the property owner, (2) the "extent to which the [government action] has interfered with distinct investment-backed expectations," and (3) the "character of the governmental action."

compensation" must be paid to the property owner.[74]

### A. Kelo v. City of New London

The Supreme Court's most recent decision determining the bounds of the Takings Clause was *Kelo v. City of New London*.[75] At issue in *Kelo* was an economic development plan designed to revitalize the Fort Turnbull area of New London.[76] In 1990, a Connecticut state agency designated New London a "distressed municipality."[77] In 1996, the Naval Undersea Warfare Center was closed, resulting in the loss of 1,500 jobs in the city.[78] By 1998, the city's unemployment rate was nearly twice that of Connecticut as a whole, and its population was "at its lowest since 1920."[79]

This combination of factors led the city to reactivate the New London

Penn Cent. Transp. Co. v. City of New York, 438 U.S. 104, 124 (1978). The *Penn Central* test is designed to assist courts in determining whether governmental regulation is such that just compensation must be paid to a property owner who is subject to the regulation. *See id.* at 122. The Plan discussed in this Note is clearly a taking for which municipalities must intend to pay just compensation.

73. U.S. CONST. amend. V.

74. "Just compensation" has been defined as the seized property's "fair market value," and is intended to put the owner of the property "in as good position pecuniarily as he would have occupied if his property had not been taken." United States v. Miller, 317 U.S. 369, 373 (1943). A discussion of whether the Plan meets the constitutional requirement that mortgage holders be paid just compensation for the seized mortgages is outside the scope of this Note. However, there is disagreement about whether the Plan provides just compensation. *Compare* Memorandum from Walter Dellinger et al., Attorneys, O'Melveny & Myers LLP, to Sec. Indus. & Fin. Mkts. Ass'n 6 (July 16, 2012) [hereinafter O'Melveny Memorandum], *available at* http://www.sifma.org/issues/item.aspx?id=8589939523 (arguing the MRP proposal assumes that municipalities will be able to seize mortgages for 75 to 80 percent of the homes' market value, but that just compensation must be determined based on the market value of the loan itself, not the market value of the home that secures it), *with FAQs*, MORTGAGE RESOL. PARTNERS, http://mortgageresolutionpartners.com/faqs (click hyperlink "What is the fair market value of a loan, and how will you determine it?") (last visited Nov. 30, 2013) ("Similar sales of troubled loans in the secondary market exist and are good evidence of fair value. These sales occur at a significant discount to the fair value of the home because of the 'foreclosure discount'—the market's recognition of the cost in time, money and effort to foreclose on the homeowner and thereafter to maintain and sell the property.").

75. Kelo v. City of New London, 545 U.S. 469 (2005).

76. *Id.* at 473–75.

77. *Id.* at 473.

78. *Id.*

79. *Id.*

Development Corporation (NLDC) to assist the city in its economic development efforts.[80] During the planning process, pharmaceutical giant Pfizer announced that it would be building a $300 million research facility in the Fort Turnbull area.[81] Hoping to take advantage of the pending arrival of the Pfizer facility, the NLDC's finalized economic development plan included space reserved for an urban village, a state park, a museum, residential and commercial buildings, and other amenities.[82] The NLDC's intention in promulgating this plan was to "creat[e] jobs, generat[e] tax revenue, and help[] to build momentum for the revitalization of downtown New London."[83] To effectuate the plan, a number of privately owned properties had to be purchased by the city.[84] The NLDC negotiated with a majority of landowners in the area encompassed by the economic development plan, but Susette Kelo and nine other homeowners refused to sell, so the NLDC initiated condemnation proceedings to take the properties by eminent domain.[85] Kelo's home, and the homes of the other holdouts, were not taken for any reason other than that they were in the area designated for development by New London; there was no allegation of blight or public nuisance.[86]

In finding that the takings constituted "public use" within the meaning of the Fifth Amendment, the Court emphasized that "[f]or more than a century, [its] public use jurisprudence ha[d] wisely eschewed rigid formulas and intrusive scrutiny in favor of affording legislatures broad latitude in determining what public needs justify the use of the takings power."[87] Given the deference afforded to legislative decisions, the Court found New London's condemnation of the petitioners' homes as part of a broader economic development plan satisfied the public use requirement.[88]

The Court was not persuaded by the petitioners' argument that using eminent domain for the purpose of economic development "blurs the boundary between public and private takings."[89] Collateral, or even "direct and significant," benefits may be conferred on individual private parties in

80. *Id.*
81. *Id.*
82. *Id.* at 474.
83. *Id.* (internal quotation omitted).
84. *See id.* at 475.
85. *Id.*
86. *Id.*
87. *Id.* at 483.
88. *Id.* at 484.
89. *Id.* at 485.

pursuit of a public purpose without necessarily violating the Takings Clause.[90] In fact, "[t]he public end may be as well or better served through an agency of private enterprise."[91]

Another argument made by the *Kelo* petitioners, but rejected by the Court, was that governments should have to show "reasonable certainty that the expected public benefits will actually accrue."[92] The Court held that such a determination would be contrary to their role, which is simply to determine whether "the legislature's purpose is legitimate and its means are not irrational" and not to judge "the wisdom of takings."[93]

Much of the Court's reasoning in *Kelo* was based on two prior decisions, *Berman v. Parker* and *Hawaii Housing Authority v. Midkiff*, which involved exercises of eminent domain that resulted in private-to-private transfers.[94]

### B. Berman v. Parker

In 1945, due to extensive blight in the Washington, D.C. area, Congress passed the District of Columbia Redevelopment Act.[95] Congress determined that the best way to alleviate blight was to condemn a number of properties and turn them over to developers as part of a broader redevelopment plan.[96] The first phase of the redevelopment plan involved Project Area B in southwest D.C., specified the boundaries, and allocated the land use restrictions throughout the project area.[97] The Act was challenged by property owners who owned a department store within Area B and whose property was to be seized, transferred to a private entity, and redeveloped for private use.[98] The department store was not itself blighted, but it was nonetheless included in D.C.'s acquisition plan as part of the

90. *Id.*

91. *Id.* at 485–86 (quoting Berman v. Parker, 348 U.S. 26, 33–34 (1954)).

92. *Id.* at 487 (internal quotation marks omitted).

93. *Id.* at 487–88 (quoting Haw. Hous. Auth. v. Midkiff, 467 U.S. 229, 242–43 (1984)).

94. *See Midkiff*, 467 U.S. at 233–45; *Berman*, 348 U.S. at 29.

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

96. *Id.* at 29.

97. *Id.* at 30. "Surveys revealed that in Area B, 64.3% of the dwellings were beyond repair, 18.4% needed major repairs, only 17.3% were satisfactory; 57.8% of the dwellings had outside toilets, 60.3% had no baths, 29.3% lacked electricity, 82.2% had no wash basins or laundry tubs, 83.8% lacked central heating." *Id.*

98. *Id.* at 31.

larger redevelopment scheme.[99]

In unanimously finding the taking of the appellant's property satisfied the public use requirement, the Court noted that the "role of the judiciary in determining whether [the power of eminent domain] is being exercised for a public purpose is an extremely narrow one" because "when the legislature has spoken, the public interest has been declared in terms well-nigh conclusive."[100]

### C. Hawaii Housing Authority v. Midkiff

At issue in *Midkiff* was Hawaii's Land Reform Act of 1967.[101] The Act was passed in response to legislative findings that 47 percent of the state's land was owned by only 72 landowners (the state or federal government owned another 49 percent of the land).[102] Further, the legislature found that 18 of those landowners owned more than 40 percent of the land, and that 72.5 percent of the land on Oahu (the most urbanized island) was owned by only 22 landowners.[103]

Hawaii's legislature concluded that this high concentration of land ownership in so few hands "was responsible for skewing the State's residential fee simple[104] market, inflating land prices, and injuring the public tranquility and welfare."[105] In response to these concerns, the Land Reform Act of 1967 was passed.[106] The Act "created a mechanism for condemning residential tracts and for transferring ownership of the condemned fees simple to existing lessees."[107] The Act enabled tenants within a tract to apply to the Hawaii Housing Authority (HHA) for condemnation of the land on which they lived, and if enough tenants filed the appropriate applications, the "HHA [was] to hold a public hearing to determine whether acquisition by the State of all or part of the tract will

99. *See id.* at 34.
100. *Id.* at 32.
101. Haw. Hous. Auth. v. Midkiff, 467 U.S. 229, 233–35 (1984).
102. *Id.* at 232.
103. *Id.*
104. A "fee simple" is a present possessory interest in real property and "represent[s] the entire and absolute interest and property in the land." 28 AM. JUR. 2D *Estates* § 13 (2011). This "absolute interest" in 47 percent of Hawaii's land was held by only 72 landowners, while everyone else leased land from those landowners. *Midkiff*, 467 U.S. at 232.
105. *Midkiff*, 467 U.S. at 232.
106. *See id.* at 233.
107. *Id.*

'effectuate the public purposes' of the Act."[108] If the HHA determined that the public purposes would be served, it was authorized to condemn the land, provide just compensation to the landowner, and then sell it to the tenants who had applied for fee simple ownership.[109]

As in *Kelo*, the Court noted that the "starting point for our analysis of the Act's constitutionality is [our] decision in *Berman v. Parker*."[110] The Court reaffirmed *Berman*'s deference to legislative judgment, saying "the Court has made clear that it will not substitute its judgment for a legislature's judgment as to what constitutes a public use 'unless the use be palpably without reasonable foundation.'"[111] In these circumstances, the Court unanimously found that the Land Reform Act was rationally related to Hawaii's interest in remedying the "artificial deterrents to the normal functioning of the State's residential land market" caused by the concentration of land ownership in only a small number of persons.[112]

In *Midkiff*, the Court not only reaffirmed the narrow role courts have in determining whether a use is public, but also further explained the breadth of public use.[113] It noted that use by "the entire community, [or] even any considerable portion" of condemned property is not essential for it to constitute a public use,[114] so long as the condemnation "by its class or character [is] a public affair."[115] The LRA involved a transfer from the landowner to the tenant, but it was the public purpose of the transfer (alleviation of the land oligopoly) that the Court focused on, not the way in which the public purpose was effectuated.[116]

The Court emphasizes two very important rationales for its decisions in *Kelo*, *Berman*, and *Midkiff*: (1) The role of the courts in determining whether an exercise of eminent domain satisfies the public use requirement

108. *Id.* (citing HAW. REV. STAT. § 516-22 (1977)).

109. *Id.* at 233–34 (citing HAW. REV. STAT. § 516-25). In theory, no public money was to be used for the condemnation process, as the compensation paid to the landowners "ha[s] been supplied entirely by lessees." *Id.* at 234.

110. *Id.* at 239; *see* Kelo v. City of New London, 545 U.S. 469, 480–82 (2005) (beginning the analysis of whether the city's development plan constituted "public use" with an extensive review of the holding in *Berman*).

111. *Midkiff*, 467 U.S. at 241 (quoting United States v. Gettysburg Elec. Ry., 160 U.S. 668, 680 (1896)).

112. *Id.* at 242.

113. *See id.* at 244.

114. *Id.* (quoting Rindge Co. v. Los Angeles Cnty., 262 U.S. 700, 707 (1923)).

115. *Id.* (quoting Block v. Hirsh, 256 U.S. 135, 155 (1921)).

116. *See id.* at 245.

is minimal because "when the legislature has spoken, the public interest has been declared in terms well-nigh conclusive";[117] and (2) "[i]t is only the taking's purpose, and not its mechanics . . . that matters in determining public use."[118] These two rationales will be central to the analysis of the Municipal Plan's constitutionality.

Also worth noting is that while eminent domain is most often exercised to seize real property,[119] as was done in the cases discussed above, the Supreme Court has also upheld the use of eminent domain for mortgage loans, so long as the public use and just compensation requirements are met.[120]

Part VI discusses the constitutionality of the Plan under the federal Constitution as interpreted by the Court in the cases discussed above. However, this Note will not address whether the Plan would survive a challenge on the state level, as many states took steps after the *Kelo* decision to assure that the broad reading of "public use" used by the *Kelo* Court did not apply to their state constitutional or statutory eminent domain provisions.[121]

## VI. CONSTITUTIONALITY OF THE MUNICIPAL PLAN

At least two local governments—Chicago and the Joint Powers Authority (JPA) formed by San Bernardino County and the cities of Fontana and Ontario in California—that have been particularly affected by

117. *Id.* at 239 (quoting Berman v. Parker, 348 U.S. 26, 32 (1954)).

118. Kelo v. City of New London, 545 U.S. 469, 482 (2005) (quoting *Midkiff*, 467 U.S. at 244).

119. "Real property . . . consists of such things as are permanent, fixed, and immovable, including lands, tenements, and hereditaments of all kinds, which are not annexed to the person or cannot be moved from the place in which they exist." 63C AM. JUR. 2D *Property* § 11 (2009).

120. Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555, 602 (1935) ("If the public interest requires, and permits, the taking of property of individual mortgagees in order to relieve the necessities of individual mortgagors, resort must be had to proceedings by eminent domain . . . .").

121. *See, e.g.*, City of Norwood v. Horney, 853 N.E.2d 1115, 1140–41 & n.12 (Ohio 2005) (explicitly rejecting the rationale of the *Kelo* majority and holding that "economic benefits alone" are not a valid public use under Ohio law); Bd. of Cnty. Comm'rs v. Lowery, 136 P.3d 639, 653–54 (Okla. 2006) (holding "takings for the purpose of economic development alone . . . do not constitute a public use" under Oklahoma's constitution or statutes). For a more in-depth discussion of the post-*Kelo* reaction amongst state courts and legislatures, see Ilya Somin, *The Judicial Reaction to* Kelo, 4 ALB. GOV'T L. REV. 1 (2011).

the foreclosure crisis have taken official action to consider the Municipal Plan.[122] The City of Chicago noted that between September of 2006 and May of 2012, average home prices had declined 39 percent, and that 44.5 percent of the homes in Cook County were underwater, resulting in $37 billion in lost equity.[123] Given statistics such as those, the city voted to consider implementing the Plan in order to "save homeowners substantial money, reduce the risk of foreclosures, help people remain in their homes, and revitalize [the] local economy."[124] The JPA found that in the past four years there has been a historic drop in revenue to local governments due to widespread foreclosures and plummeting home values.[125] Additionally, the JPA found that negative equity "increas[es] the likelihood of further foreclosures, inhibit[s] the ability to refinance, and dampen[s] consumer confidence and economic activity."[126] Based on these findings, the JPA also resolved to consider implementation of the Plan.[127] On September 11, 2013, Richmond, California became the first local government to authorize use of eminent domain to seize underwater mortgages.[128]

Other studies discussed above demonstrate the broad-based effects a foreclosure can have on a community.[129] For example, the Immergluck and Smith study found that foreclosures cost the city of Chicago between $598

122. Joint Comm. of Fin. & Hous. & Real Estate, Chi., Ill., Resolution: Call for Hearing(s) on Implementation of Program for Acquisition of Underwater Mortgages through Eminent Domain (July 25, 2012) [hereinafter Chicago Resolution], *available at* http://mortgagebankers.org/files/ChicagoEminentDomainResolution.pdf; Bd. of Supervisors, San Bernardino Cnty., Cal., Resolution No. 2012-135 (June 19, 2012) [hereinafter Joint Powers Resolution], *available at* http://www.homeownershipjpa.org/Portals/18/Documents/Resolution.pdf.

123. Chicago Resolution, *supra* note 121, at 1.

124. *Id.* at 2.

125. Joint Powers Resolution, *supra* note 121, at 1.

126. *Id.* at 2.

127. *See id.* Ultimately, however, the JPA decided not to pursue any foreclosure mitigation plans involving the use of eminent domain. Alejandro Lazo, *San Bernardino County Abandons Mortgage Plan*, L.A. TIMES (Jan. 25, 2013), http://articles.latimes.com/2013/jan/25/business/la-fi-eminent-domain-20130125.

128. Lydia DePillis, *After 7-Hour Meeting, It's On: Richmond Sticks with Its Plan to Seize Mortgages Through Eminent Domain*, WASH. POST: WONKBLOG (Sept. 11, 2013), http://www.washingtonpost.com/blogs/wonkblog/wp/2013/09/11/after-7-hour-meeting-its-on-richmond-sticks-with-its-plan-to-seize-mortgages-through-eminent-domain/.

129. *See supra* Part IV (discussing, among other things, the decrease in surrounding property values and increase in violent crime incident to each foreclosure).

million and $1.39 billion in decreased property values,[130] Cleveland has been trying to alleviate increased crime and squatting in its 10,000 to 15,000 vacant homes,[131] and Congress's Joint Economic Committee estimated the cost of each foreclosure at $80,000 when considering the impacts on homeowners, loan servicers, lenders, neighbors, and local governments.[132]

Two common threads run through *Kelo*, *Berman*, and *Midkiff*: (1) judicial deference is at its pinnacle when deciding whether a legislative exercise of eminent domain satisfies the public use requirement;[133] and (2) an inquiry into a taking's purpose, not its mechanics, will be determinative of whether the public use requirement is satisfied.[134]

Legislative pronouncements such as the Chicago and JPA resolutions are what the Court has looked to in determining whether a particular taking is for the public use,[135] and with the action taken by these local governments, "the public interest has been declared in terms well-nigh conclusive."[136] Additionally, as emphasized by both Chicago and the JPA, the scope of the problem, as well as the extent of its consequences, have been significant for municipalities.[137] Therefore, given the deference afforded local governments in determining whether a taking is public in character, as well as the magnitude of the effects of foreclosure being borne by municipalities, it is likely that an implementation of the Plan would satisfy the public use requirement.

Despite the strong language used by the Court over the last 50 years and the magnitude of the problem being addressed, the unique and unprecedented method of foreclosure mitigation proposed by the Plan has

130. Immergluck & Smith, *supra* note 50, at 57–58.

131. Alex Kotlowitz, *All Boarded Up*, N.Y. TIMES, Mar. 4, 2009, http://www.nytimes.com/2009/03/08/magazine/08Foreclosure-t.html?pagewanted=all&_r=1&.

132. JOINT ECON. COMM., *supra* note 49, at 17.

133. Kelo v. City of New London, 545 U.S. 469, 483 (2005); Haw. Hous. Auth. v. Midkiff, 467 U.S. 229, 239 (1984); Berman v. Parker, 348 U.S. 26, 32 (1954).

134. *Kelo*, 545 U.S. at 482; *Midkiff*, 467 U.S. at 244; *see Berman*, 348 U.S. at 33.

135. *See, e.g.*, *Kelo*, 545 U.S. at 483–84 (recognizing New London's stated purpose of creating new jobs and increasing tax revenue as a valid public use); *Midkiff*, 467 U.S. at 241–42 (recognizing that Hawaii was attempting "to reduce the perceived social and economic evils of a land oligopoly").

136. *Berman*, 348 U.S. at 32.

137. Chicago Resolution, *supra* note 121, at 1–2; Joint Powers Resolution, *supra* note 121, at 1–2.

drawn strong criticism.[138]

One of the strongest opponents of the Plan is the Securities Industry and Financial Markets Association (SIFMA), an association of securities firms, banks, and asset managers.[139] The SIFMA, along with a group of 25 other organizations that oppose the use of eminent domain to seize mortgages, warn that implementation of the Plan "would reduce the sources of funding for mortgage originators, and cause originators to underwrite in a defensive manner, therefore reducing credit availability," and that "[l]enders and investors will pull back from funding mortgage lending in jurisdictions that implement such plans."[140]

The SIFMA hired former U.S. Solicitor General Walter Dellinger[141] to draft a memorandum (the O'Melveny Memo) discussing the constitutionality of the Plan.[142] The O'Melveny Memo concludes that the Plan would not satisfy the Constitution's public use requirement for an acceptable government taking because it is not "one part of a 'comprehensive' economic development plan" similar to what was upheld in *Kelo*.[143] The memo argues that the Court approved the one-to-one property transfer in *Kelo* only because it was "just one component of an integrated program to develop and improve one specific area of the city," while the Plan itself is merely a "systematic transfer of property from A to B," which the *Kelo* majority "specifically rejected" as satisfying the public use requirement.[144] Another argument made in the O'Melveny Memo attacks the Plan's targeting of only those mortgage loans meeting certain criteria, noting the Plan "is limited to *performing* loans—those much less likely to default—on the theory that forcibly transferring and discounting them now will reduce the risk that they *could* default."[145]

The major flaw in both of these arguments is they both focus on the

138. *See infra* notes 138–44, 153–54 and accompanying text.

139. *About SIFMA*, SIFMA, http://www.sifma.org/about/ (last visited Nov. 30, 2013).

140. Letter from Sec. Indus. & Fin. Mkts. Ass'n et al., *supra* note 8, at 2.

141. Dellinger was acting Solicitor General under President Bill Clinton during the 1996–1997 term of the Supreme Court, and is currently a member of the Appellate Practice group in the Washington, D.C. law firm of O'Melveny & Myers LLP. *Walter Dellinger*, O'MELVENY & MYERS LLP, http://www.omm.com/walter dellinger/ (last visited Nov. 30, 2013).

142. O'Melveny Memorandum, *supra* note 74.

143. *Id.* at 3 (citing Kelo v. City of New London, 545 U.S. 469, 483–84 (2005)).

144. *Id.* at 4 (citing *Kelo*, 545 U.S. at 486–87).

145. *Id.*

Plan's mechanics and not its purpose, an analysis explicitly rejected by the Court in both *Kelo* and *Midkiff*.[146] Nowhere in the O'Melveny Memo are the effects of foreclosures on an entire community discussed, nor is the strong correlation between underwater mortgages and foreclosures. The O'Melveny Memo focuses on the undesirability of the Plan's method of seizing preselected mortgages meeting certain criteria, but fails to address—as this Note has attempted to highlight and as the Plan is designed to mitigate—the undeniable connection between negative equity and foreclosure and the harmful community-wide effects of foreclosure.[147] In addition, each local government will determine which loans to purchase and may choose to purchase delinquent as well as current loans.[148]

If a municipality selected individual mortgages for seizure and refinance, as opposed to selecting mortgages meeting preselected criteria, those takings would not be part of a "comprehensive" plan designed to benefit the public generally as required by *Kelo*, *Midkiff*, and *Berman*.[149] However, the Plan, as contemplated, provides for takings that "would be executed pursuant to a 'carefully considered' development plan."[150]

The fact that private benefits are being conferred on both MRP and each homeowner included in the Plan is also irrelevant to the constitutional analysis.[151] Each of the cases discussed in Part V involved private-to-private transfers of property through eminent domain, and in each case the Court disregarded the private-to-private nature of the transfers and focused on the public evil sought to be remedied.[152] The evil at issue here is clear and substantial,[153] and the Plan's primary purpose is mitigation of that evil.

Another argument, made by both the O'Melveny Memo and the

146. *See Kelo*, 545 U.S. at 482; Haw. Hous. Auth. v. Midkiff, 467 U.S. 229, 244 (1984).

147. O'Melveny Memorandum, *supra* note 74, at 4; *see supra* Part IV.

148. *See supra* notes 12–16 and accompanying text.

149. *See Kelo*, 545 U.S. at 484; *Midkiff*, 467 U.S. at 242; Berman v. Parker, 348 U.S. 26, 29 (1954).

150. *Kelo*, 545 U.S. at 478 (quoting Kelo v. City of New London, 843 A.2d 500, 536 (Conn. 2004)). See *supra* Part II for a discussion of the Plan's proposed criteria, designed to aid in the formation of a comprehensive foreclosure mitigation scheme for each municipality.

151. *Kelo*, 545 U.S. at 485–86.

152. *Id.* at 473 (focusing on the city's economic development purposes); *Midkiff*, 467 U.S. at 232 (highlighting Hawaii's land oligopoly); *Berman*, 348 U.S. at 28 (discussing blight in the area).

153. *See supra* Parts III–IV.

respondents in *Kelo*, is that the purported public benefits are unlikely to actually accrue, and therefore the public use requirement is not satisfied.[154] The Court in *Kelo* quickly dismissed this argument, holding that the role of the courts is not to judge "the wisdom of takings," as that would be a policy judgment outside the province of the judiciary.[155] Although the Plan in theory will prevent numerous foreclosures, it need not actually prevent a single homeowner from going into foreclosure in order to survive judicial scrutiny.[156]

To support the legitimacy of the Municipal Plan further, Vlahoplus analogizes those holding subprime mortgages in private label trusts to a developer who owns 100 buildings filled with flammable materials.[157] An actuary tells the developer that eventually 70 of those buildings will burn to the ground and spread fire to multiple neighboring properties, but the developer decides he will make enough money on the remaining 30 buildings that the cost and hassle of remedying the hazard would not be worth it.[158] No one would doubt in that situation that the municipality has the authority to require the developer to clean out the flammable materials, or to condemn the buildings to mitigate the public safety concerns.[159] This developer is no different than a servicer of securitized subprime mortgages. Fannie Mae predicts approximately 70 percent of all subprime mortgages will default[160] (ultimately leading to foreclosure), yet the servicers of these mortgages are either unwilling or unable to change the terms of individual mortgages so homeowners can avoid default.[161]

154. *Kelo*, 545 U.S. at 487; *see* O'Melveny Memorandum, *supra* note 74, at 4.

155. *See Kelo*, 545 U.S. at 488 (quoting *Midkiff*, 467 U.S. at 242–43).

156. If close judicial scrutiny or post hoc review was the standard of takings, the *Kelo* decision would certainly have been different because the Pfizer facility that drove the economic development plan in New London shut its doors in 2009 and left behind a "swath of barren land that was cleared of dozens of homes to make room for a hotel, stores and condominiums that were never built." Patrick McGeehan, *Pfizer to Leave City That Won Land-Use Case*, N.Y. TIMES, Nov. 12, 2009, http://www.nytimes.com/2009/11/13/nyregion/13pfizer.html?_r=0.

157. Vlahoplus Interview, *supra* note 14.

158. *Id.*

159. *See, e.g.*, Jack W. Shaw, Jr., Annotation, *Gasoline or Other Fuel Storage Tanks as Nuisance*, 50 A.L.R.3d 209, § 3[a] (1973) (compiling caselaw holding the storage of fuel to be a public nuisance).

160. Fed. Nat'l Mortg. Ass'n, *supra* note 65, at 111.

161. Vlahoplus Interview, *supra* note 14; *see also* Hockett, *supra* note 11, at 139–40 (noting the PSAs pursuant to which mortgages are pooled and securitized often restrict or prohibit the modification or sale of individual mortgage loans).

The far-reaching negative effects of foreclosure on such a community are at least comparable to the potential conflagration in this analogy, if not worse. And while municipalities have the legal tools to prevent foreclosures, they have no legal tools to mitigate the damage caused by foreclosures.[162]

## VII. CONCLUSION

This nation's housing crisis has devastated individuals and communities for nearly a decade. The Municipal Plan, designed to prevent default for homeowners with negative equity by condemning their current mortgages and refinancing at an affordable rate, is a modest proposal with the possibility of mitigating the effects of continuing foreclosures being borne by cities and counties across the country. Other attempts to alleviate these effects have been largely unsuccessful, and the Plan is therefore a final effort—a life vest—designed to rescue municipalities drowning in foreclosures. Should an implementation of the Plan come under constitutional scrutiny, more than five decades of precedent on the subject should weigh in favor of the Plan's constitutionality.

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162. *See* Immergluck & Smith, *supra* note 50, at 75.

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