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Can't Live Without Air: Title Insurance and the Bursting of the Real Estate Bubble

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UNSETTLING MORTGAGE LAW: IMPLICATIONS FOR PRACTITIONERS AND TITLE INSURERS

Can't Live Without Air: Title Insurance and the Bursting of the Real Estate Bubble

Marvin N. Bagwell*

"Can't live, can't breathe with no air."[1]

I. Prologue

A few months ago, I wrote a brief article originally titled "*A Fairy Tale*," which ended up being published in *The Bulletin*, *The Journal of the New York State Land Title Association*—a title industry publication. Several people who read the article prior to its publication advised me against releasing it to the public. The pre-publication readers were hesitant because I made a startling admission in the article: that people in the title industry knew that the real estate bubble was about to burst.[2] Their concern was that my admission could be used

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1. JORDIN SPARKS DUET WITH CHRIS BROWN, NO AIR (Jive Records 2007).

2. Marvin N. Bagwell, *Weaving a Tale of Woe from Today's Economic Crisis – Can this Possibly Be True? Is this a Fairy Tale?*, BULL.: J. N.Y. STATE LAND TITLE ASS'N, Summer 2008, at 3.

against the entire industry in a court of law or, more importantly, in the court of public opinion.

Under the system that we employ to conduct real estate closings or settlements in New York, with all parties sitting around a closing table, a title company representative is present at every closing from the smallest residential refinance to a multi-million dollar acquisition and mortgaging of a Manhattan skyscraper. After the closing, title closers would often return to their offices, wondering how in the world the borrowers were going to afford their mortgage. How could a security guard clearing $35,000 annually afford a half-million dollar mortgage? Was the GM building really worth a billion and a half dollars? The time came when title people would wager on how long it would take the borrower to go into foreclosure after the closing date. "He won't make the first payment. I bet we will receive an order for a foreclosure search on this property within ninety days. Where are the lenders obtaining the money to make all of these stupid loans?" Those of us in the title industry knew that something was up, but we did not know exactly what was going on. As it turns out, we were right—the bubble was about to burst, but we did not know as much as we had thought, nor did we fully know exactly when or why. In any event, had we known and issued warnings to raise red flags, we would have been ignored. Forces much greater than any title closer, or even title company, were at work. Warnings would have been ignored and we know what happens to the messenger.

Yes, the intent of this Article is to apply some salve to the conscience of title personnel everywhere by describing (at probably too great a length) exactly what forces had been unleashed in the economy that led to the creation and, eventually, to the bursting of the real estate bubble. The bursting of the real estate bubble, which many experts think led to the current financial crisis, was not the title industry's fault, but rather, the blame lies with us all.

The history of the bursting of the real estate bubble in 2007 is still being written. Many of the sources cited in this Article are from newspapers, especially the papers of record, the *New York Times* and the *Wall Street Journal*. Since we are still in the midst of the financial crises, definitive studies and

books are still being written. To describe what happened, and what is happening, we will work with what we have.

II. Introduction

It is axiomatic; bubbles require air. Without air, bubbles, like the pop version of teenage love, could not exist. Indeed a bubble is mostly air. One way to define a bubble is as a globule of liquid inflated with air or gas. When the pressure of the liquid or air within the bubble becomes too much for the globule's skin, the bubble will burst. Economically, we are living in the aftermath of the real estate bubble's bursting. This is certainly not the first time that an economy was brought low by the bursting of a bubble. Most historical discussions of economic bubbles bursting start with Holland's tulip mania of the eighteenth century, then move on to England's encounter with the South Seas bubble of the nineteenth century and the American railroad bond bubble of the nineteenth century, followed by the mother of all bubbles, the 1929 stock market crash, which led to the Great Depression of the twentieth century. The commonality of each bubble is that each left economic and financial devastation in its wake.

The purpose of this Article is not to propose a solution to prevent bubbles from occurring so as to prevent the havoc caused by their bursting, but to describe what exactly contributed to the air that inflated the real estate bubble and which led to its inevitable bursting. For those of you expecting charts and references to government studies and Ph.D dissertations, please prepare to be disappointed. Those of us in the title industry are a simple lot. Our primary references will be the press reports, the anachronistic printed word. Hopefully, the flavor of what happened will not be lost on too many.

Our discussion to come will focus on four "ations": securitization, globalization, speculation, regulation; one "ism": consumerism; and one word that speaks for itself: fraud. Here is a warning to the reader: things will not be, as Tina Turner was known to hope for, "nice and easy." There will be overlap. Economic collapses in the real world are messy. Benjamin Franklin once commented, "success has many parents, but

failure is an orphan." Our goal in identifying the sources of the air that inflated the bubble, and that led to its inevitable bursting, is to empty out the orphanage.

III. Securitization

Air is comprised of many chemical components, some of which are conducive to life, such as oxygen, nitrogen, and carbon dioxide; and others that may lead to the extinction of humanity, such as carbon monoxide, ozone, and chlorides. Securitization started out as providing life-giving oxygen to the financial system, but over the course of three decades evolved into pumping life-depriving ozone into the system instead.

Securitization works in the following way. We can start with one set of homebuyers. In order to finance the purchase of their home, the homebuyers take out a loan. The obligation to repay the loan is represented by a note. The note, in turn, is secured by a mortgage on the home. In the 1970s, Lew Ranieri, then a prominent bond trader at the Wall Street firm Salomon Brothers,[3] developed the process of taking hundreds and thousands of mortgages and pooling or packaging the mortgages into bonds. The bonds were then sold to institutional investors. This process had the benefit of taking the mortgages off the hands and the books of the local lender and putting them into the hands of investors who could be located anywhere. The local bank sold the mortgage to investors who, in turn, paid for the bond, thereby providing the bank with funds to make more mortgage loans. Everyone involved in the process, from the local bank to the investor, and especially the Wall Street middlemen who packaged the mortgages into bonds and who then sold the bonds to the investor, made money.[4]

The rules of evolution govern on Wall Street as well.

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3. The tale of Salomon Brothers's rise and fall is immortalized in Michael Lewis's book, LIAR'S POKER: RISING THROUGH THE WRECKAGE ON WALL STREET (1989). As in the case of many financial immortals, Salomon no longer exists as an independent entity. It is buried somewhere within Citigroup, which, by the time this Article is read, may no longer exist as a private financial company either.

4. *See* Nancy Gibbs, *25 People to Blame*, TIME, Feb. 22, 2009, at 20, 25 (describing Mr. Ranieri and the process).

Relatively simple financial tools evolve into more complex machinery. Mortgage-backed securities or bonds in turn were grouped into packages of Collateralized Mortgage Obligations ("CMOs") or Collateralized Debt Obligations ("CDOs").[5] Therefore, investors had the opportunity to purchase a debt instrument such as a CDO for which the underlying source of payment was not one mortgage, but several thousand of them. In fact, the underlying obligation of a CDO might not be individual mortgages, but bonds secured by individual mortgages.[6] And of course, CDOs grew in terms of complexity and intricacy. Any type of debt that a consumer or corporation owed, from automobile loans to credit card debt to multi-billion dollar commercial lease financing, were turned into CDOs. Even Alan Greenspan, the former Chairman of the Federal Reserve, said that CDOs were "bewildering."[7] It was thought that such obligations carried little risk because, while one mortgage might go into foreclosure, it would not taint the entire pool. This turned out not to be the case because, as the financial crisis deepened, larger and larger percentages of the mortgages in the pools began to go "bad" or go into default. For example, in one series of mortgage-backed securities sold by Bank of America in 2007, 16% of the loans in the pool were sixty or more days overdue.[8] In 2007, Citigroup issued a mortgage-backed security in which 31% of the underlying loans were sixty or more days delinquent.[9] Of course, the higher the delinquency rate, the less likely the return on the security will turn out as initially predicted, and the more likely the

5. Drexel Burnham Lambert issued the first CDO in 1987 for Imperial Savings Association. Gregory Cresci, *Merrill, Citigroup Record CDO Fees Earned in Top Growth Market*, BLOOMBERG, Aug. 30, 2005, http://www.bloomberg.com/apps/news?pid=10000103&sid=a.FcDwf1.ZG4&refer=us. Drexel later went defunct and its most famous broker, junk bond king Michael Milken, went off to prison in 1988 for racketeering and securities fraud. Alison Leigh Cowan, *Milken to Pay $500 Million More In $1.3 Billion Drexel Settlement*, N.Y. TIMES, Feb. 18, 1992, at A1.

6. *See* Stephen Gandel, *One Bad Bond*, TIME, Mar. 9, 2009, at 30 (providing an excellent description of the process, from home mortgages to bonds and more).

7. Alessandra Stanley, *Economists Try Target Practice in a Fun-House Mirror*, N.Y. TIMES, Feb. 16, 2009, at C1.

8. James R. Hagerty & Dan Fitzpatrick, *BofA Feels Bite of Move into Mortgage-Backed Securities*, WALL ST. J., Feb. 25, 2009, at C8.

9. *Id.*

security's holder will incur a loss. Also, as one can see, the financial instruments are moving further away from the traditional one mortgage for one homeowner system. In the process, homeowners' allegiances to their local lenders and willingness to stretch themselves to make the payments when under economic duress becomes tenuous at best.[10]

How big of a problem will losses from securitization become? No one knows for sure, but "[a]ccording to Inside Mortgage Finance, some eight million nonprime mortgages were put into securities pools in 2005 and 2006 and sold to investors. The value of these loans was $797 billion in 2005 and $815 billion in 2006."[11]

To complicate matters further, and partially to protect investors from losing money if that one mortgage went into default, Wall Street began to slice and dice the mortgage pools into "tranches." The tranches are slices of the same pool of mortgages divided into parts based on the probability that the mortgages will be paid and not go into foreclosure. The highest rated mortgages, those that were least likely to go into foreclosure, would be sold to investors at the lowest interest rate because the risk of default was the smallest. Conversely, those mortgages with the highest probability of default were sold at the highest interest rates to account for the risk that the homeowners might default and go into foreclosure. Wall Street also created tranches from the interest due on the mortgage or from the principal.[12] The types, numbers, and parts of mortgages divided into tranches, and indeed the process itself, became so dizzying that it became entirely conceivable that several investors might own identical or different parts of the same mortgage.[13] As we will soon see, for

10. According to some, when a person's income becomes stressed, he or she is less inclined to "stick-it-out" with his or her lender if that lender has become a faceless international concern as opposed to his or her local banker. *See* Walter Kirn, *My Debt, Their Asset*, N.Y. TIMES, June 11, 2006, § 6 (Magazine), at 26.

11. Gretchen Morgenson, *Guess What Got Lost in the Loan Pool*, N.Y. TIMES, Mar. 1, 2009, at BU1.

12. *See generally* Floyd Norris, *In Turnabout, Thain Caved In*, N.Y. TIMES, Aug. 1, 2008, at C1; Anise Wallace, *Market Place; Making 'Junk Bonds' Respectable*, N.Y. TIMES, Dec. 15, 1989, at D1.

13. *See* Lingling Wei & Alex Frangos, *Hancock at Center of 'Tranche Warfare'*, WALL ST. J., Jan. 21, 2009, at C1 (describing the havoc now on the

those investors, the complexity of CMOs, CDOs, and the tranches they inspired would make the foreclosure process even more of a nightmare.

It takes more than debt for securitization to work. Other actors are required. First, investors want to know that the debt will be repaid. The credit rating agencies, particularly Moody's Investor's Service, Standard & Poor's and, to a lesser extent, Fitch Ratings Services, evolved to provide this service. Indeed, they were basically empowered by federal law as the only entities that were allowed to rate securities.[14] Their job was to independently assess the ability of borrowers to repay their loans and to report that ability to lenders in the form of ratings, generally from "AAA" or "Triple A," basically meaning that the debt would be repaid, to "C" which translated to junk status where repayment would be problematic. Even parts of CDOs, such as the tranches discussed above, could be rated. Of course, the better or higher the rating, the lower the corresponding interest rate.[15]

Unfortunately, it developed that the rating agencies were to become victims of a built-in conflict of interest. The sellers of the securities paid the rating agencies to rate the securities the sellers would offer to the public. The question became: to whom did the rating agencies owe their allegiance—to the public or to the Wall Street firms that paid the rating agencies their fees and added to the agencies' ever-increasing profit coffers? In the aftermath of the bursting of the real estate bubble, the conclusion reached by the House Committee on Oversight and Government Reform was that the Wall Street security sellers benefitted from the conflict of interest. As for the public and investors, the performance of the rating agencies was a "colossal failure" according to the House Subcommittee's chairman, Henry Waxman.[16] However, the most searing indictment of the rating agencies' performance came from one of their own. In an internal e-mail, a Standard

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legal horizon which was ignited by the use of tranches); Gandel, *supra* note 6.

14. *See* James Surowiecki, *Ratings Downgrade*, NEW YORKER, Sept. 28, 2009, at 25.

15. *Id.*

16. Gretchen Morgenson, *Credit Rating Agency Heads Grilled by Lawmakers*, N.Y. TIMES, Oct. 23, 2008, at B1; Gretchen Morgenson, *Debt Watchdogs: Tamed or Caught Napping?*, N.Y. TIMES, Dec. 7, 2008, at A1.

& Poor's analyst wrote that "[a bond] could be structured by cows and we would rate it."[17] No wonder *Time* magazine chose Kathleen Corbet, who ran Standard & Poor's, the largest rating agency, as one of the twenty-five people to blame for the financial meltdown.[18]

Bond insurance companies, principally Mortgage Guarantee Insurance Corporation ("MGIC") and Ambac Assurance ("Ambac"), were the second actors. For decades, these companies labored in the plain vanilla vineyard of insuring municipal bonds issued by governmental borrowers.[19] The business provided a steady but reasonable income, primarily because claims were rare and far between. Orange County, California's bankruptcy in 1994 proved the exception and simultaneously served to promote the necessity for bond insurance.[20] However, in the drive for more profits, both MGIC and Ambac began to insure more exotic indentures such as CMOs and CDOs.[21] The fact that MGIC or Ambac insured the bond issues, thereby saying that if the issuer defaulted and did not make payments when due, the insurance companies would do so, made it easier for Wall Street to sell the securities to the public. However, as early as 2006, CDO losses began to raise concerns on Wall Street, ironically about MGIC and Ambac's own solvency—that is, their own ability to pay if their insured bond issuers defaulted. By late 2007, MGIC and Ambac were in real distress and their survival was in question.[22] It took a major investment offer by Warren Buffet, billions in recapitalization, and the intervention of the New York State Insurance Department to steady the bond insurers.[23] The bond

17. Gibbs, *supra* note 4, at 23.

18. *Id.*

19. *See, e.g.*, Michael Lewis & David Einhorn, Op-Ed, *The End of the Financial World As We Know It*, N.Y. TIMES, Jan. 4, 2009, WK 9.

20. Michael Quint, *Orange County's Debacle Could Prove a Boon for Bond Insurers*, N.Y. TIMES, Dec. 8, 1994, at D6.

21. *See* Lewis & Einhorn, *supra* note 19.

22. Vikas Bajaj, *Two Bond Insurers End the Week Severely Weakened*, N.Y. TIMES, Jan. 19, 2008, at C2.

23. Vikas Bajaj, *Buffett Offers to Reinsure Bonds*, N.Y. TIMES, Feb. 12, 2008, *available at* http://www.nytimes.com/2008/02/12/business/12cnd-buffett.html; Karen Richardson & Damian Paletta, *Spitzer Warns Bond Insurers; Governor Says Firms have 3 to 5 Days to Raise Capital*, WALL ST. J., Feb. 15, 2008, at A1; Press Release, N.Y. State Ins. Dep't, Department

insurance companies, by enabling securitization, had become one of its victims.[24] As of this date, the companies are still not out of the woods. Moody's recently cut MGIC's credit rating to junk status.[25]

If the borrowers and sellers of CDOs could buy insurance plans to ensure the lenders that they would be paid, why not offer those lenders their own opportunities to buy insurance to ensure that the borrowers would pay them? This essentially defines a credit default swap. To use AIG as an example, a company may sell insurance to lenders, providing them with protection in the event that a borrower does not make payments under a CDO or CMO when due. AIG will then make the payments in the event that the borrower defaults. In effect, AIG *swaps* its Triple A *credit* rating for that of the borrower if the borrower *defaults*. Theoretically, this is great business, until borrowers begin to default.

In September 2008, it became obvious to the Treasury Department that homeowners, by the millions, were beginning to default on their mortgage payments.[26] The credit markets also began to take notice that the mortgage insurers, Ambac and MGIC, did not have the capital to pay all of the losses.[27] They were in trouble themselves. The markets noted that AIG, which had insured trillions of dollars of CDOs and CMOs, only had billions in capital to pay the losses.[28] If AIG collapsed, lenders throughout the world, including sovereign governments and lenders to the United States such as China, Japan, Saudi Arabia, and South Korea, all of whom held billions in U.S. debt, would have to immediately recognize trillions of dollars of loses.[29] The situation was untenable. If it were to occur, the

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Facilitates, Supervises MBIA Split; Should Add Capacity to Municipal Bond Insurance Market (Feb. 18, 2009), *available at* http://www.ins.state.ny.us/press/2009/p0902181.htm.

24. Mark Landler & David D. Kirkpatrick, *Lobbyists Swarm the Treasury For a Helping of the Bailout Pie*, N.Y. TIMES, Nov. 12, 2008, at A22.

25. Kathy Shwiff, *Crisis on Wall Street: Moody's Slashes Ratings on Mortgage Insurers*, WALL ST. J., Feb. 17, 2009, at C3.

26. *See* Lewis & Einhorn, *supra* note 19.

27. *See id.*

28. Edmund L. Andrews, Michael J. de la Merced & Mary Williams Walsh, *Fed's $85 Billion Loan Rescues Insurer*, N.Y. TIMES, Sept. 17, 2008, at A1.

29. *Id.*

Federal National Mortgage Association ("Fannie Mae") and the Federal Home Loan Mortgage Corporation ("Freddie Mac") (more on them later) might default on their debt and bring the world economy to its knees. To prevent that from happening, the Treasury Department bailed out AIG to the tune (to date) of $150 billion dollars.[30] This may not be sufficient. Both the *Wall Street Journal* and the *New York Times* have reported that AIG will report a $60 billion loss for the fourth quarter of 2008.[31] If AIG is unable to obtain the capital to cover the losses and is forced into bankruptcy, the domino effect would be horrendous. Other lenders who hold AIG's credit swaps as insurance against the losses in their portfolio would have to take the losses on their own books, thereby eroding their own capital base and possibly leading to their failure as well.[32] In effect, an AIG failure could bring down many other institutions with it. This explains why the Treasury advanced funds to AIG so quickly in late 2008 and may have to do more of the same in 2009.[33]

Contrary to the explanations offered to the public, the advanced funds to AIG were meant to benefit the American public only secondarily, if at all. The real intention of the AIG bailout was to send the message to the international community that the United States would stand behind AIG's credit swaps. If AIG failed, bonds issued by Fannie Mae and Freddie Mac, among others, would have lost their value, thereby adversely affecting security holders such as central banks throughout the world. In the case of AIG, history will show that the profits were indeed privatized with the losses being passed on to the public. In time, the public will know that mortgage foreclosures were the furthest thing from Secretary Paulson's mind that fateful weekend in September when the bubble burst. His eyes were on Beijing, not Peoria.

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30. Andrew Ross Sorkin & Mary Williams Walsh, *Giant Insurer May Get More in U.S. Bailout*, N.Y. TIMES, Nov. 10, 2008, at A1.

31. Matthew Karnitschnig, Liam Pleven, & Serena Ng, *A.I.G. Seeks to Ease Its Bailout Terms*, WALL ST. J., Feb. 24, 2009, at A1; Mary Williams Walsh & Michael J. de la Merced, *As A.I.G.'s Losses Grow, Its Survival Options Shrink*, N.Y. TIMES, Feb. 25, 2009, at B5.

32. Walsh & de la Merced, *supra* note 31.

33. *Id.* See Joe Nocera, *Propping Up A House of Cards*, N.Y. TIMES, Feb. 28, 2009, at BU1, for a capsule lesson on the AIG drama.

Let's make things a little more complicated. In 1997, a team at JPMorgan Chase & Co. ("JPMorgan") developed a new kind of financial instrument which combined CDOs and credit default swaps.[34] CDOs were underlain by real mortgages given by individual corporate lenders to lenders, and credit default swaps were essentially insurance policies taken out by lenders. However, this new financial instrument called a synthetic collateralized default obligation, or synthetic CDO, derived its value not from concrete instruments such as mortgages, but from contracts linked to those mortgages, hence the term "derivatives."[35] The fact that they were derived from the contract brought rise to the use of the term "derivatives."[36] The word "synthetic" should have been a clue to investors to throw up a red flag. However, synthetic CDOs generated outsized returns which resulted in more and more investors purchasing them. Many did not actually know what they were buying. The complexity of these instruments is mind boggling, but suffice it to say, when the values of real mortgages began to fall because of rising defaults and foreclosure rates, the value of synthetic investments began to drop even faster.[37] The investment banks that created, promoted, and sold these investments began to suffer staggering losses, thus eating into their capital.[38] To protect the banking system, something had to be done. The investment bank Bear Stearns Companies Inc. failed to raise enough capital and had to be rescued by JPMorgan and the federal taxpayer for less than the value of its headquarters building.[39] The Treasury allowed another investment bank, Lehman Brothers Holdings, Inc., to go into bankruptcy,[40] an event which some experts believe only made

34. Gretchen Morgenson, *How the Thundering Herd Faltered and Fell*, N.Y. TIMES, Nov. 9, 2008, at BU1.

35. *Id.*

36. *Id.*

37. *Id.*

38. *See, e.g.*, *id.* (describing such a situation).

39. *See, e.g.*, Landon Thomas, Jr., *JPMorgan and Fed Move to Bail Out Bear Stearns*, N.Y. TIMES, Mar. 14, 2008, at BU1.

40. See, for example, Ben White & Michael M. Grynbaum, *The Street After Lehman Brothers*, N.Y. TIMES, Sept. 16, 2008, at C1, for a blow-by-blow, minute-by-minute description of the collapse of Lehman Brothers.

things worse for the world economy.[41] Merrill Lynch & Co., Inc. rushed into the saving arms of Bank of America.[42] When the air which securitization pumped into the real estate bubble finally led to the bubble's bursting, securitization, like animals in the wild, had eaten its young. Alan S. Blinder, Professor of Economics and Public Affairs at Princeton University asked rhetorically: "[D]oes anyone doubt that the financial turmoil would have been less severe if derivatives trading had acquired a zookeeper a decade ago?"[43]

Securitization had a more nefarious effect closer to home for those who purchased the mortgages. Every securitization starts with a single mortgage. When the borrower defaults and fails to make a payment due upon that mortgage, the usual remedy for the lender to realize its secured interest is foreclosure. To be successful in a foreclosure action, indeed even to make it past the courthouse door, the lender must prove to the court that it owns the mortgage. As noted above, securitization involves the slicing, dicing, and re-packaging of mortgages. Most states have recording statutes which require that a mortgage must be assigned of record when its ownership changes.[44] Within the foreclosure bar and the foreclosure defense bar, it is no secret that one of the effects of the packaging, securitization, and sale of mortgages is that the assignment chain and actual documentation of mortgage ownership have failed to keep up. Ironically, the pooling and packaging of mortgages—the securitization process—which enabled lenders to make even more mortgages and greater profits, has made it more difficult for those lenders to foreclose when the mortgages go bad.[45] The process also makes it more

41. Eric Dash, et al., *5 days of Pressure, Fear and Ultimately, Failure*, N.Y. TIMES, Sept. 16, 2008.

42. *See, e.g.*, Louise Story & Julie Creswell, *Love Was Blind*, N.Y. TIMES, Feb. 8, 2009, at BU1 (detailing the unhappy marriage between Merrill Lynch and Bank of America).

43. Alan S. Blinder, *Six Blunders En Route to a Crisis*, N.Y. TIMES, Jan. 25, 2009, at BU7.

44. *See, e.g.*, FLA. STAT. ANN. § 701.02 (West 2009); KAN. STAT. ANN. § 58-2223 (2008); N.Y. REAL PROP. LAW § 291 (McKinney 2009). *See also* JAMES KARP & ELLIOT KLAYMAN, REAL ESTATE LAW (5th ed. 2003); DAVID A. SCHMUDDE, A PRACTICAL GUIDE TO MORTGAGES AND LIENS (2004).

45. Gretchen Morgenson, *How One Borrower Beat the Foreclosure Machine*, N.Y. TIMES, July 27, 2008, at BU1.

difficult for borrowers to modify their mortgages in a bid to ward off foreclosure—a difficulty which even President Obama has said "makes no sense."[46] It is well known that original mortgage documents are routinely lost somewhere between the initial lender, the loan servicer, and the purchaser of the CDO that includes the mortgage (or a part of it). As a result, it is often anyone's guess as to who actually owns or has possession of the original mortgage. When the issue at hand may result in someone losing their home, the courts have not been willing to accept "anyone's guess" as the appropriate legal standard.[47]

The problem of lost loan documentation leading to a lender (or loan servicer) losing the standing to foreclose upon a mortgage very recently caught more of the national media's attention. In her article for the *New York Times*, Gretchen Morgenson noted that "bookkeeping," the proper assignment of pooled mortgages and the recording of those assignments in the public record, was not a priority of many big banks.[48] "Bookkeeping is such a bore, especially when there are billions to be made shoveling loans into trusts like coal into the Titanic's boilers. You can imagine the thought process: Assigning notes takes time and costs money, why bother? Who's going to ask for proof of ownership of these notes anyhow?"[49] Ms. Morgenson wrote:

> No one knows how many loans went into securitization trusts with defective documentation. But as messes go, this one has, ahem, potential. According to Inside Mortgage Finance, some eight million nonprime mortgages were put into securities pools in 2005 and 2006 and sold to investors. The value of these loans was $797 billion in 2005 and $815 billion in 2006.[50]

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46. Edmund L. Andrews, *Obama Plan on Housing Said to Push on Lenders*, N.Y. TIMES, Feb. 17, 2009, at B1.

47. Morgenson, *supra* note 11.

48. *Id.*

49. *Id.*

50. *Id.*

As reported by Ms. Morgenson, bankruptcy judges throughout the country have started to deny motions to permit foreclosure where the lender cannot prove ownership of the mortgage.[51] R. Glen Ayers, a former bankruptcy judge in Texas, and an expert in the area, says that for lenders, "[i]t's a huge problem . . . . It's going to be expensive, I don't know how expensive, ultimately to the bondholders."[52] Of course, the possibility that courts may deny foreclosure to lenders can only decrease the value of the CDOs and CMOs based upon those mortgages that the lenders are holding as assets in their vaults. Translated, because of bad documentation, the major banks will experience even greater losses and will need even more capital to survive—capital that, to date, only taxpayers have the wherewithal to provide.[53] And the nightmares of both the bankers and the taxpayers, who apparently may have to pay the bill, have begun.

Beginning in Ohio, and quickly spreading to New York, many courts have either delayed or tossed out foreclosure actions where the plaintiff-lender has been unable to show public record ownership of the subject mortgage.[54] The case of Mamie Ruth Palmer, a seventy-four year old former housekeeper living in Atlanta, made the popular press. In 2002, Ms. Palmer filed for bankruptcy to protect her home from foreclosure. The note securing the loan was assigned to the Bank of New York in September 2002; two months after the bank had begun its foreclosure action. Ms. Palmer's attorney argued that since the bank did not own the note at the time it started its foreclosure action, it did not have standing to foreclose. Rather than risk an adverse ruling, the bank settled with Ms. Palmer by reducing the balance of her mortgage from

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51. *Id.*

52. *Id.*

53. *See* Tyler Cowen, *Three Rocky Roads To a Bank Rescue*, N.Y. TIMES, Mar. 1, 2009, at BU5 (summarizing the capital problems which the banks and taxpayers are facing).

54. *See, e.g.*, In re Foreclosure Cases, No. 07CV2282, 2007 WL 3232430 (N.D. Ohio Oct. 31, 2007) (dismissing several foreclosure actions where owners failed to follow the recording requirements of Ohio law). *See also* Morgenson, *supra* note 11 (discussing court decisions enforcing the mortgage recording requirement).

$100,000 to $59,000.[55]

Suzanne Garcia and I have written on the subject of standing under New York law.[56] Without repeating here the case summaries discussed elsewhere, it should be noted that in cases decided since the publication of our respective articles, the courts have held that lenders who succeed to ownership of a mortgage by assignment that is recorded after the lender initiated a foreclosure action (a retroactive assignment) lack standing to foreclose.[57] One court has asked a lender to explain why it purchased a non-performing loan.[58] Securitization begets confusion even within the same lender. While the lender's right hand was negotiating a settlement with the borrower, the lender's left hand was busy conducting a foreclosure sale. The court found the bank counsel's conduct in bringing a motion for default judgment to have been "unconscionable, dishonorable and unprofessional."[59] How would you like to be in that counsel's shoes the next time he appears before that judge?

Securitization was undoubtedly a major contributor to the air that expanded the real estate bubble over the last few years. When the bubble burst, securitization having run amok was one of the major causes of the bubble's sudden and abrupt destruction. It will take years to fully understand and recover from the impact that securitization had on the bubble and, as we shall soon see, also upon the world economy.

IV. Globalization

Here, "globalization" refers to the spread of debt, which is

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55. Morgenson, *supra* note 45.

56. Suzanne M. Garcia, *A New Perspective on Foreclosure in Title*, N.Y. L.J., Aug. 25, 2008, at S4. *See also* Marvin N. Bagwell, *Judges Take Notice of Subprime Mortgage Crisis*, N.Y. REAL EST. L. REP., Apr. 2008, at 1; Marvin N. Bagwell, *Home Equity Theft Prevention Act*, N.Y. L.J., Apr. 9, 2008, at 5.

57. *See* Washington Mut. Bank v. Patterson, N.Y. L.J., Jan. 7, 2009, at 29 (N.Y. Sup. Ct. Dec. 15, 2008); New Century Mortgage Corp. v. Durden, N.Y. L.J., Feb. 11, 2009, at 27 (N.Y. Sup. Ct. Feb. 2, 2009).

58. Deutsche Bank Nat'l Trust Co. v. Campbell, N.Y. L.J., Dec. 24, 2008, at 27 (N.Y. Sup. Ct. Dec. 16, 2008).

59. Deutsche Bank Nat'l Trust Co. v. Miele, N.Y. L.J., Sept. 22, 2008, at 19 (N.Y. Sup. Ct. Sept. 5, 2008).

created in the United States, across international borders. A home mortgage secured by real estate located in Fort Myers, Florida could end up on the books of a bank based in Oslo, Norway. In reality, the Oslo bank purchases the CMO or CDO that contains the Fort Myers mortgage as one of the thousands therein, and records the security as an asset on its books. Viewed this way, it is easy to see that globalization and securitization go hand in hand. For example, just look at the case headings cited in footnotes 57 and 58, *supra*.[60] Like the proverbial chicken and the egg, it is difficult to tell which came first. However, it is very clear that if it were not for the globalization of finance (and by finance, I mean borrowing and lending), the American mortgage "contagion" that spread around the world would have been contained within our very own borders. Globalization therefore contributed to the air that inflated the real estate bubble. The story is one of supply and demand.

Let us start with an American household.

To cure the tech crash of 2000, the Federal Reserve Bank, under the leadership of Alan Greenspan, kept American interest rates relatively low. This, in turn, made money very cheap. At the same time, thanks to the securitization pioneered by Wall Street, the mortgage lending business transformed from a local business to one with access to international funding. More money meant that more and more people had the opportunity to borrow. The fact that Fannie Mae and Freddie Mac were on a mission, spreading homeownership as much as possible, added nourishment to the contagion. When you add the perception that the value of American housing had never declined, the atmosphere becomes even headier. Sure of ever-increasing home values, Americans started to view their homes as ATM machines. As home prices go up, more equity is created, which people can borrow against—and they do so. Households then use their cashed-out equity to buy things, especially plasma televisions and other toys made in China and other low wage countries, for both children and adults. Americans have also bought big SUV's which use oil—lots of oil—imported from places like Saudi

60. *See supra* notes 57 & 58 and accompanying text.

Arabia, Russia and Venezuela. To pay for these things, we send our dollars there. To keep the dollars coming, these countries buy our debt, issued by the Treasury Department as well as Fannie and Freddie. The money from this debt is then re-circulated back into our economy so that we can buy more toys. The increase in the supply of money leads to an increase in the demand of goods. To maintain demand, and to keep their economies growing, foreign nations continued to supply funding to the American economy so that Americans could buy more of their goods.[61] It was as if Sir Elton John's *Circle of Life* had left the *Lion King* behind on the Broadway stage and headed for the international economy, which indeed, is exactly what happened.

For their part, the banks did two major things: (1) they securitized the mortgages that American households had used for the cash to buy goods and invest in more property because real estate prices were only going up, and (2) they sold those securities to banks and institutions throughout the world. Hence, the globalization of American homeowner borrowing resulted. Those who bought these securities wanted greater returns, so the bankers and the mortgage lenders who supplied them invented ways to increase the return. Thus, subprime mortgages and adjustable rate mortgages were born. And to further increase the supply of mortgages, lenders created their progeny: "no-docs," (no income verification loans); so-called "ninja loans" (no income, no job, no assets); "exploding loans" (loans where the interest rate adjusted rapidly and surprisingly upwards) and liar's loans (no nothing).[62] It is no wonder that *Time* magazine named Angelo Mozilo, the founder of Countrywide Financial (now Bank of America Home Loans), one of the major subprime purveyors, as the number one person to blame for the economic meltdown.[63] So returns went up for investors, and, after seeing the outsized returns, more investors wanted in. To increase their returns, many investors

61. *See* Neall Ferguson, *Reasons to Worry*, N.Y. TIMES, June 11, 2006, § 6 (Magazine), at 46.

62. *See* Jack Rosenthal, *On Language, No Docs*, N.Y. TIMES, Aug. 17, 2008, § MM (Magazine), at 18 (providing a glossary of subprime mortgage terms).

63. Gibbs, *supra* note 4, at 21.

resorted to borrowing money to leverage their investments.

> They made $100 million bets with only $1 million of their own money and $99 million in debt. If the value of the investment rose to just $101 million, the investors would double their money.
> . . .
> If that $100 million investment . . . were to lose just $1 million of its value, the investor who put up only $1 million would lose everything.[64]

Professor Blinder regards permitting sky-high leveraging, such as in the aforementioned example, as one of the six blunders made by regulators that contributed to the current financial crisis,[65] but more on this later. Securities based upon mortgages made in the United States found their way into the investment coffers of banks, pension funds, municipalities, and governments throughout the world. Then the contagion hit. Many commentators believe that the seminal event was the Treasury's decision to let Lehman Brothers fail and enter bankruptcy.[66] This forced the holder of mortgage-backed securities to see exactly what they had purchased. To their horror, they discovered that their formerly valuable CMO and CDO asset holdings were based upon subprime mortgages or worse. As noted above in the section on securitization, the rating agencies' ratings were meaningless and the insurance provided by AIG was suspect since AIG only had billions in capital to pay trillions of dollars in possible claims.[67] The giant Swiss bank, UBS, thought to be one of the most conservative and careful investors in the world, found itself holding $80 billion in U.S. mortgage-backed securities on which it, by late 2007, had suffered a $37 billion loss with an additional $30 billion waiting to be recognized. Its shareholders lost one half of the value of their stock and its chairman lost his job.[68]

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64. David Leonhardt, *Can't Grasp Credit Crisis? Join the Club*, N.Y. TIMES, Mar. 19, 2008, at A1.

65. Blinder, *supra* note 43.

66. *Id.*

67. *See* discussion *supra* Part III.

68. Nelson D. Schwartz, *The Mortgage Bust Goes Global*, N.Y. TIMES,

The contagion continues to spread.[69] Governments, including those based in London, Berlin, Dublin, Amsterdam, and Brussels, have had to seize major banks and lenders.[70] Essentially, the governments had to seize or pump funds into banks because the losses that the banks experienced from their bad investments in American mortgage-back securities wiped out their capital. The banks became the walking dead—"zombies"—unable to lend or borrow.[71] Without access to credit, neither consumers nor businesses can obtain funds to buy goods or to expand. The Troubled Asset Recovery Program ("TARP"), initiated by the Bush Administration in September 2008, was meant to replenish the banks' capital so that they would start lending again. It is obvious from the daily headlines that TARP did not work.[72] Currently, both nationally and worldwide, we are experiencing no growth or actual falling economies. That is, by definition, a financial crisis. And it all started with home mortgages, the payment on which people could not make. But as we have seen, and will continue to see throughout this Article, the fault does not necessarily lie with the borrowers. As *Time* magazine's list of twenty-five indicates,[73] there is enough blame to go around.[74]

The bursting of the real estate bubble in the United States meant that the consumers' ATMs had run dry. With no cash to spend, the demand for goods by consumers in the United States plummeted. As a result of the lack of demand for goods in America's recessionary economy, China estimates that 20 million of its 130 million migrant workers are now unemployed.[75] According to the United Nations, 50 million people throughout the world could lose their jobs by the end of

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Apr. 6, 2008, at B1.

69. Mark Landler, *The U.S. Financial Crisis Is Spreading to Europe*, N.Y. TIMES, Sept. 30, 2008, at C1.

70. *Id.*

71. Paul Krugman, *Banking on the Brink*, N.Y. TIMES, Feb. 22, 2009, at A27.

72. *See, e.g.*, Gretchen Morgenson, *Bailout Needs Some Strings Attached to Limit Pay*, N.Y. TIMES, Feb. 7, 2009, at BU1.

73. Gibbs, *supra* note 4, at 21.

74. *See* Bagwell, *supra* note 2, at 3.

75. Keith Bradsher, *China's Unemployment Swells as Exports Falter*, N.Y. TIMES, Feb. 6, 2009, at B4.

2009 because of the recession that began in the United States.[76] Both Russia and China, two nations that invested heavily in American debt, have blamed the United States for their financial crisis.[77] These accusations could have been meant as propaganda to play for the audiences at home, but the Chinese and Russian people are beginning to suffer. The American economic crisis has affected Russian used car dealers in specific ways.[78] Dealers in Vladivostok, a city on Russia's eastern frontier, rose up in protests against the government's imposition of tariffs against foreign cars.[79] Russia raised tariffs to protect its foreign currency reserves, which are being drained by (1) a fall in the demand for oil; and (2) a run on the ruble, which was caused by its own hard times that the Kremlin believes were brought on by the American financial crisis.[80] The feared people's protest that poses the biggest threat to the Putin regime may be attributed to the international financial crisis, brought on by the bursting of the American real estate bubble.

The global economic instability brought on by the American recession, which in turn finds its roots in the bursting of our real estate bubble, poses the top threat to our own national security, even outpacing terrorism, according to Dennis C. Blair, the American Director of National Intelligence.[81] In testimony before Congress, Mr. Blair stated that "[t]he crisis . . . [that] started in the United States . . . has [already] increased questioning of U.S. stewardship of the global economy."[82] Not only was the globalization of American mortgage debt a part of the air that inflated the real estate

76. Nelson D. Schwartz, *Unemployment Surges Around the World, Threatening Stability*, N.Y. TIMES, Feb. 15, 2009, at A1.

77. Carter Dougherty & Katrin Bennhold, *Russia and China Blame Capitalist*, N.Y. TIMES, Jan. 28, 2009, at A21.

78. Clifford J. Levy, *Rash of Tariff Protests in Vladivostok Has the Kremlin on the Defensive*, N.Y. TIMES, Feb. 16, 2009, at A6.

79. *Id.*

80. *Id.*

81. Mark Mazzetti, *Global Economic Crisis Poses Top Threat to U.S., Spy Chief Warns*, N.Y. TIMES, Feb. 13, 2009, at A14.

82. S. SELECT COMM. ON INTELLIGENCE, 111TH CONG., ANNUAL THREAT ASSESSMENT OF THE INTELLIGENCE COMMUNITY 3 (Feb. 12, 2009) (statement for the record of Admiral Dennis C. Blair), *available at* http://www.dni.gov/testimonies/20090212_testimony.pdf.

bubble, it was also part and parcel of what ultimately caused the bubble to burst. That which American borrowers and lenders, as well as international investors, spread throughout the world may return to exact no small measure of restitution and, dare I say, retribution.

V. Speculation

"Speculation" is defined as the "engagement in business transactions involving considerable risk but offering the chance of large gains, [especially] trading in commodities, stocks, etc., in the hope of profit from changes in the market price."[83] Every financial bubble involves some form of speculation—that is, taking great risks in the hope of obtaining great profits. I have already discussed some forms of speculation in this Article. For example, homeowners who engaged in seriatim borrowing against the equity in their homes were speculating that the values of their homes would continue to rise. The banks that used leveraging, that is, the use of borrowed money to magnify gains, such as the hypothetical investor discussed earlier who borrowed $100 million to increase the profit on their $1 million investment, are speculators.[84]

No discussion of financial speculation can begin without taking note of the tulip mania that gripped Holland in the seventeenth century. Mark Frankel, in his review of Mike Dash's 1999 book, *Tulipomania: The Story of the World's Most Coveted Flower & The Extraordinary Passions It Aroused*, tells the story.[85] Tulips had been prized since the mid-1550s for their extraordinary beauty, purity and sharpness of colors, and extravagant presentation.[86] The fact that it took seven years to grow a tulip from seed to bulb only added to its allure.[87] By the beginning of the seventeenth century, Holland was at the peak

83. Dictionary.com, http://dictionary.reference.com/browse/speculation (last visited Sept. 6, 2009).

84. *See* Thomas L. Friedman, Op-Ed., *All Fall Down*, N.Y. TIMES, Nov. 26, 2008, at A33 (providing a biting critique of speculation by a lender).

85. Mark Frankel, *When the Tulip Bubble Burst*, BUSINESSWEEK, Apr. 24, 2000, *available at* http://www.businessweek.com/2000/00_17/b3678084.htm.

86. *See* MIKE DASH, TULIPOMANIA 27-35 (1999).

87. *Id.* at 56.

of its power, with the merchants in Amsterdam making 400% profits on their East Indies trading.[88] These wealthy Dutch displayed their riches by building grand estates surrounded by elaborate flower gardens that featured rare and exquisite tulips.[89] In 1624, a man in Amsterdam who owned the only twelve bulbs of a midnight blue tulip topped by a band of pure white and accented by crimson flares was offered as high as 3,000 guilders for one bulb.[90] By comparison, Rembrandt received only half that amount when he painted his masterpiece, the *Night Watch*.[91] Prices rose steadily throughout the 1630s and speculators entered the marketplace. In the winter of 1636-37, one rare tulip bulb that was about to split in two was sold at auction for 5,200 guilders.[92] Some bulbs were changing hands in the marketplace ten times a day.[93] Then came the crash. All it took was one buyer in Haarlem who refused to pay for a bulb that he had purchased at auction.[94] Panic struck, and within days, the marketplace had all but vanished. Bulbs, which had routinely commanded 5,000 guilders days before, began to trade for fifty guilders.[95] Great fortunes evaporated overnight.[96]

The tulip mania story is so evocative because every financial bubble since has followed the same course. I could substitute railroad stocks for tulips and end up with a similar description of the mid-nineteenth century collapse in the market for railroad securities; substitute stocks, and I could describe what happened in 1929; substitute shares in "dot.com" companies, and we end up with the dot.com bust of the late 1990s. Today, we read the story of the real estate bubble, and "McMansions" and "flipping" come to mind. Scholars can point out differences among the financial speculations involved in each bubble's bursting, but because human nature has remained virtually unchanged over the centuries, the

88. *Id.* at 71.
89. *Id.* at 78-79.
90. *Id.* at 82.
91. *Id.* at x.
92. *Id.* at 152.
93. *Id.* at 156.
94. *Id.* at 162-63.
95. *Id.* at 165.
96. Frankel, *supra* note 85.

framework remains the same.

More recently, in 2007, the marketplace for commercial real estate was at its highest. Sam Zell, a billionaire real estate investor based in Chicago sold 573 commercial properties located throughout the United States to the Blackstone Group for $39 billion.[97] Blackstone "immediately flipped hundreds of those building [to sixteen different groups] for $27 billion."[98] It was promoted as the deal of the century, and unfortunately for all involved, it may have been. Charles V. Bagli of the *New York Times* wrote that,

> [t]oday, the wreckage of those purchases is strewn across the country, from Southern California to Austin, Texas, to Chicago to New York. Many of the [sixteen] companies that bought [Sam Zell's properties] are now stuck with punishing debt, properties whose values are plummeting and millions of feet of office space they cannot fill.[99]

Mr. Bagli then goes on at length describing how the "deal of the century" destroyed almost every company who invested at the top of the market.[100] One of the buyers was the legendary New York real estate mogul Harry Macklowe, who purchased seven buildings from Blackstone.[101] Macklowe and his family put down only $50 million of their personal fortune and leveraged it into $7 billion in short term, high-interest debt in order to finance the acquisitions.[102] Within two years, because of the bursting real estate bubble, Macklowe was forced to turn over several of the buildings to his lenders.[103] The lenders then turned around and sold those buildings for 25% less than what

97. Charles V. Bagli, *Sam Zell's Empire, Underwater in a Big Way*, N.Y. TIMES, Feb. 9, 2009, at B1.

98. *Id.*

99. *Id.*

100. *Id.*

101. *Id.*

102. *Id.*

103. *Id.*

Macklowe had originally paid for them.[104] Both the "leveragee" and the "leveragor" lost spectacularly. In order to avoid personal bankruptcy and other defaults, Macklowe was also forced to sell the family's crown jewel, the GM Building, which it had acquired in 2003.[105] Macklowe, a well-known and admired risk-taker, had speculated and lost.

Speculation by consumers added to the real estate bubble. Hannah Fairfield of the *New York Times* wrote, "overbuilding in regions of Florida, California and other states with housing bubbles lured overeager residents to become speculators, buying up many homes with the expectation that their value would rise."[106] Florida has been the national poster child for consumer speculation. In Lehigh Acres, a suburb of Fort Myers, "from 2004 to the end of 2006, developers completed 13,183 units . . . , nearly doubling the total stock of 15,216 that existed in 2000."[107] As a result, housing prices doubled and then tripled.[108] "Sometimes houses would sell three or four times in a few months, and no one would move in . . . ."[109] Speculation and the "flipping" that accompanies it were rampant. Then, in 2007, it all went away—the bubble had burst.[110] Perhaps George Packer, in his article, *The Ponzi State: Florida's Foreclosure Disaster*, offered the best description of the real estate speculative fever that gripped Florida and its aftermath.[111]

In his article, Mr. Packer takes the reader on a journey along State Road 54 in Pasco County, Florida—a road running

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104. *Id.*

105. Charles V. Bagli, *Macklowes Sell G.M. Building for $2.9 Billion*, N.Y. TIMES, May 25, 2008, at A27.

106. Hannah Fairfield, *In the Shadow of Foreclosures*, N.Y. TIMES, Apr. 6, 2008, at N4, *available at* http://www.nytimes.com/2008/04/06/business/06metricstext.html. The chart accompanying the article that illustrates subprime mortgages as a percentage of all mortgages is especially edifying.

107. Damien Cave, *Florida's Crossroads of Foreclosure and Despair*, N.Y. TIMES, Feb. 8, 2009, at A1.

108. *Id.*

109. *Id.* (quoting Bob Elliot).

110. *Id.*

111. George Packer, *The Ponzi State: Florida's Foreclosure Disaster*, NEW YORKER, Feb. 9 & 16, 2009, at 81.

forty-five minutes northeast of Tampa.[112] In 1950, twenty thousand people lived in Pasco County. By 2008, the county's population had grown to half a million residents.[113] Over the past few years, around one thousand people a day moved to Florida.[114] This population growth fueled a real estate boom that was "bigger and gaudier than anything the state had ever seen."[115] Flat and desolate fields became housing developments of "look-alike two-story beige and yellow houses" that sold for two to three hundred thousand dollars.[116] The homes in turn led to "shopping malls and mega-churches," but by 2007, it was all over.[117] The developments had become "ghost subdivisions," full of houses in which no one lived because the growth was all a mirage—fueled by the perception of future growth.[118] In the words of Gary Mormino, a professor of history at the University of South Florida, "Florida, in some ways, resembles a modern Ponzi scheme. Everything is fine for me if a thousand newcomers come tomorrow. The problem is, except for a few road bumps—'73, '90, and they were really minor—no one knew what would happen if they stopped coming."[119] In a description that is destined to become classic, Mr. Packer notes that "[by] 2005, the housing market in Florida was hotter than it had ever been, and frenzy spread across all levels of society."[120] Many of the migrant farm workers from the area were able to find jobs in the construction industry, working as roofers and drywall hangers.[121]

> Nearly everyone you met around Tampa had a Realtor's license or a broker's license or was a title agent. Alex Sink, the state's chief financial officer, and a Democrat, said, "When the yardman comes and says he's not going to mow

112. *Id.*
113. *Id.*
114. *Id.*
115. *Id.*
116. *Id.*
117. *Id.*
118. *Id.*
119. *Id.* at 83 (internal quotations omitted).
120. *Id.* at 84.
121. *Id.*

> your yard anymore because he's going to become a mortgage broker, that is a sure sign that something is wrong."[122]

The process of flipping houses and condominiums became an amateur pursuit for those in the middle-class.[123] "People who drew modest salaries at their jobs not only owned a house, but bought other houses as speculators, the way average Americans elsewhere dabble in day trading."[124] It was destined not to end well.

Packer goes on in his article to discuss the "downward spiral" of the Florida market, noting:

> When, at the Florida's market's dizzying mid-decade height, speculators lost confidence, the faith that kept the state aloft gave way and the economy plummeted like a Looney Tunes character who, suspended in midair, suddenly looks down. Property values did what the lender and borrowers somehow never imagined was possible: they started to decline. Today, the average unit in Fort Myers and Cape Coral is selling for just a hundred and fifty-eight thousand dollars, less than half of what it sold for at the height.[125]

The *Wall Street Journal* reported that "two years ago, the Lee County court system [which covers Fort Myers and Coral Grove] had about 1,900 foreclosure cases on the books. That number swelled to 24,000 by the beginning of [2009]."[126] The average time that it takes a judge to dispose of a case? Fifteen seconds.[127]

Speculation, if dabbled in here and there, is not bad. Its

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122. *Id.*
123. *Id.*
124. *Id.*
125. *Id.* at 88.
126. Michael Corkery, *A Florida Court's "Rocket Docket" Blast Through Foreclosure Cases*, WALL ST. J., Feb. 18, 2009, at A1.
127. *Id.*

use is driven by the desire to make a profit, a concept that is at the core of capitalism. However, it is when speculation runs amok, and people or institutions begin to speculate with other people's money, that society has a big problem—a problem that usually results in financial ruin for those who come late into the game or at the height of the market. Of course, as both Mr. Packer and the *Wall Street Journal* observe, not all people who are being foreclosed out of their homes are speculators.[128] Most are innocent people who have suffered a misfortune, such as a job loss, medical ailment, or some other personal setback that has deprived them of their income and thus, the ability to meet their monthly mortgage payments. The true speculators, especially the scoundrels, are long gone, and they took their profits with them. Whether the bubble surrounds tulips, railroad bonds, stock certificates, dot.com companies, or real estate, speculation inflates the bubble, and then it bursts. Unlike Wile E. Coyote, Sylvester the Cat, or Daffy Duck, the person holding the Acme anvil might not survive the fall.

VI. Regulation

About a century ago, Mark Twain commented that money is not the root of all evil, but rather, "the lack of money is the root of all evil."[129] In the case of our current financial crisis, experts agree that it was not regulation, but the lack thereof that permitted securitization, speculation, and the side effects of globalization to create the circumstances leading to today's financial crises. The real estate bubble—more properly, the bursting of the bubble—is the parent of the crisis. In this context, the lack of regulation enabled the progeny—the financial crisis—to come into being.

As discussed earlier in this Article, *Time* magazine recently listed the twenty-five people to blame for the financial meltdown.[130] Of the twenty-five people who made the list, almost one-quarter were in a position to regulate the financial marketplace. A review of those six individuals places the

128. *Id.*; Packer, *supra* note 111.
129. THE WIT AND WISDOM OF MARK TWAIN (Paul Negri ed., 1999).
130. Gibbs, *supra* note 4, at 20.

apparent fruits of deregulation into historical context. Number two on the list, former Senator Phil Gramm, was Chairman of the Senate Banking Committee from 1995 through 2000.[131] Gramm was an "outspoken champion of financial deregulation. He played a leading role in . . . the 1999 repeal of the Glass-Steagall Act,[132] which separated commercial banks from Wall Street [investment banks]."[133] This led to the creation of major financial institutions such as Citicorp, which, in trying to be all things to all lenders and borrowers, accrued huge losses and then had to be bailed out by the Treasury Department.[134] Gramm is also responsible for a provision in the 2000 Commodity Futures Act[135] that exempted derivatives-like credit default swaps from regulation.[136] Senator Gramm takes issue with his having any blame for the financial crisis.[137] In his Op-Ed piece for the *Wall Street Journal*, he blames the "politicization" of mortgage lenders as exemplified by the Community Reinvestment Act,[138] which "led regulators to foster looser underwriting and encouraged the making of more and more marginal loans;" and the 1992 Housing Bill which "set quotas or 'targets' that Fannie and Freddie were to achieve in meeting the housing needs of low and moderate income Americans" as the "primary cause of this crisis."[139] However, months earlier, in the Op-Ed pages of that very same newspaper, Thomas Frank published an article predicting that conservatives would blame Freddie Mac and Fannie Mae for

131. *Id.*

132. Banking Act of 1933 (Glass-Steagall), ch. 89, 48 Stat. 162, *repealed by* Gramm-Leach-Bliley, Pub. L. No. 106-102, 113 Stat. 1338 (1999) (codified in scattered sections of 12 and 15 U.S.C.).

133. Gibbs, *supra* note 4, at 20 (internal footnote added).

134. *See, e.g.*, David Enrich et al., *U.S. Agrees to Rescue Struggling Citigroup*, WALL ST. J., Nov. 24, 2008, at A1 ("The federal government agreed Sunday night to rescue Citigroup Inc. by helping to absorb potentially hundreds of billions of dollars in losses on toxic assets on its balance sheet . . . .").

135. Commodities Futures Modernization Act, Pub. L. No. 106-554, § 1(a)(5), 114 Stat. 2763 (2000).

136. Gibbs, *supra* note 4, at 20.

137. Phil Gramm, Op-Ed., *Deregulation and the Financial Panic*, WALL ST. J., Feb. 20, 2009, at A17.

138. Community Reinvestment Act of 1977, Pub. L. No. 95-128, 91 Stat. 1111 (codified as amended at 12 U.S.C. §§ 2901-2908 (2006)).

139. Gramm, *supra* note 137.

causing the crisis because they, for "political reasons," were required to buy bad mortgages taken out by people who could not pay.[140] Instead, Frank, quoting Bill Black, a professor of economics and law at the University of Missouri-Kansas City, assigns the blame to "four entities that under conservative economic theory should have exercised effective market discipline—the appraisers, the originators of the mortgages, the rating agencies, and the investment banking firms that packaged the subprime mortgage-backed securities."[141]

Bill Clinton is number thirteen on *Time*'s list.[142] As President, he signed both the repeal of Glass-Steagall and the 2000 Commodity Futures Act into law.[143] Clinton also loosened housing lending rules which had the perverse, unintended side effect of creating subprime mortgages.[144] Number fourteen, George W. Bush, "embraced deregulation and allowed federal oversight agencies to ease off of banks and mortgage brokers."[145] Number four, Christopher Cox, head of the Securities and Exchange Commission ("SEC"), oversaw the massive leveraging by banks and failed to rein in the risks undertaken by investment banks such as Bear Stearns, Lehman Brothers, and Merrill Lynch.[146] *Time* believes that Cox deserves so much of the blame, that in a subsequent edition, it devoted an entire column to his failures, noting that he was a "crucial voice [that] was missing;" "absent;" a "no show;" and "asleep on the job"—and that was just in the article's first three paragraphs.[147] Number two on the list is Alan Greenspan, who as head of the Federal Reserve, permitted low interest rates to persist for far too long, and whose "long-standing disdain for regulation underpinned the mortgage crisis."[148] Greenspan also admitted to Congress "that

140. Thomas Frank, Op-Ed., *The Tilting Yard: The GOP Blames the Victim*, WALL ST. J., Oct. 1, 2008, at A23.

141. *Id.*

142. Gibbs, *supra* note 4.

143. *Id.*

144. *Id.*

145. *Id.*

146. *Id.*

147. Adam Zagorin & Michael Weisskoff, *Inside the Breakdown at the SEC*, TIME, Mar. 9, 2009, at 34.

148. Gibbs, *supra* note 4, at 20; *see also* Floyd Norris, *Failing Upward at*

he made a mistake in presuming that financial firms would regulate themselves."[149] Finally, former Treasury Secretary Hank Paulson appears as number five on the list because he responded "too late in battling the crisis."[150]

It should be noted that *Time*'s list also includes the former head of one federal governmental institution, which it turns out should have been regulated much more tightly. Franklin Raines, number nine on *Time*'s list, became the head of Fannie Mae in 1999.[151] Fannie Mae and Freddie Mac, its smaller brother, are federally chartered financial institutions, charged with providing liquidity to the housing marketplace by purchasing mortgages from lenders.[152] In effect, Fannie Mae and Freddie Mac are dominant purchasers, and thereby lenders, in the secondary marketplace. After staggering losses, the Federal Government seized both entities in September 2008.[153] Franklin Raines left Fannie Mae in 2004 as the result of an accounting scandal, just as it was making massive investments in subprime mortgages and securities, both of which went south.[154] Congressional hearings on the failure of both Fannie Mae and Freddie Mac disclosed that they had spent over $175 million in lobbying fees over ten years precisely to avoid greater regulation.[155] In 2008, Fannie Mae had a loss of $58.7 billion, an amount that "exceed[ed] its net income for the preceding 17 years."[156] Both Fannie Mae and Freddie Mac are expected to "gush [red ink] in even larger quantities" because of mortgage defaults and losses in the

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the Fed, N.Y. TIMES, Feb. 27, 2009, at B1 (providing an in-depth criticism of Alan Greenspan and the Federal Reserve's failures which led to the current financial crisis).

149. Gibbs, *supra* note 4, at 20 (internal quotations omitted).

150. *Id.*

151. *Id.*

152. *See* Stephen Labaton & Edmund L. Andrews, *In Rescue to Stabilize Lending, U.S. Takes Over Mortgage Finance Titans*, N.Y. TIMES, Sept. 7, 2008, at A1 (discussing the Bush administration's bailout of Fannie Mae and Freddie Mac).

153. *Id.*

154. Gibbs, *supra* note 4, at 20.

155. Lynnley Browning, *Ex-Officer Faults Mortgage Giants for "Orgy" of Nonprime Loans*, N.Y. TIMES, Dec. 10, 2008, at B3.

156. James R. Hagerty & Damian Paletta, *Red Ink Clouds Role of Fannie, Freddie*, WALL ST. J., Feb. 27, 2009, at A2.

value of their derivative contracts.[157] As for Congress, there is a saying about those who live in glass houses that comes to mind.

Another regulator's failure to regulate recently came to light. In July 2008, the Treasury seized IndyMac Federal Bank, FSB ("IndyMac") in the third largest bank failure ever recorded.[158] At the time of its failure, IndyMac had $32 billion in assets and $19 billion in deposits.[159] IndyMac had pursued an overly aggressive growth strategy that included failing to verify borrowers' incomes and relying on expensive deposits to fund its operations.[160] The Treasury Department's inspector general said that the Office of Thrift Supervision ("OTS"), which was charged with regulating IndyMac, "did not take aggressive action to stop those practices from continuing to proliferate."[161] OTS recognized the red flags which had come up, but, at the time, did nothing to address them.[162]

Economists from the left, the middle and the right agree that regulators, particularly Alan Greenspan and the Federal Reserve, share the blame for the real estate bubble.[163] The *New York Times* quotes Gerald P. O'Driscoll, Jr., of the libertarian Cato Institute, as saying "[the Federal Reserve] allowed these absolutely insane bubbles to happen."[164] Charles W. Calomiris of the conservative American Enterprise Institute said, "[w]e do need some regulation-smarter regulation."[165] As noted previously, Alan S. Blinder of Princeton University has written that the people in power made six errors which, had they avoided, would have evaded the financial crisis.[166] Those

157. *Id.*

158. Louise Story, *Regulators Seize Mortgage Lender*, N.Y. TIMES, July 12, 2008, at C5.

159. Reuters, *Indy Mac Files for Bankruptcy Protection*, N.Y. TIMES, Aug. 2, 2008, *available at* http://www.nytimes.com/2008/08/02/business/02lender.html.

160. Michael R. Crittenden, *Regulators Missed Woes at Indy Mac*, WALL ST. J., Feb. 27, 2009, at A2.

161. *Id.*

162. *Id.*

163. Abha Bhattarai, *Economists Plumb the Depths of the Downturn*, N.Y. TIMES, Aug. 6, 2008, at C3.

164. *Id.*

165. *Id.*

166. Blinder, *supra* note 43.

errors have permitted "wild derivatives," "sky-high leverage," "a subprime surge," "fiddling on foreclosures," "letting Lehman go," and the "TARP's detour."[167] Robert J. Shiller, a professor of economics and finance at Yale University, noting that "Alan Greenspan . . . acknowledged in a Congressional hearing . . . that he had made an 'error' in assuming that the markets would properly regulate themselves, and . . . that he had no idea a financial disaster was in the making," wrote that "lots of people were worried about the housing boom[, but]. . . the Fed did not take them very seriously."[168]

The experts do not spare the SEC either. Michael Lewis, the author of *Liar's Poker*,[169] and David Einhorn, co-author of *Fooling Some of the People All of the Time*,[170] in discussing the rating agencies, wrote that "[o]ver the last 20 years American financial institutions have taken on more and more risk, with the blessing of regulators . . . ."[171] Further, although the SEC was "[c]reated to protect investors from financial predators, the commission has evolved into a mechanism for protecting financial predators with political clout from investigation."[172] Although the *New York Times* headline says it all—*S.E.C. Chief Pursues Reversal of Years of Lax Enforcement*[173]—I will quote some of the article anyway. The author stated:

> Investor groups had been frozen out by an agency dominated by commissioners describing themselves as proponents of free-market principles, who made it more difficult for the professional staff to bring cases. Senior jobs lay vacant for many months. Many problems at the largest investment houses had gone undetected,

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167. *Id.*

168. Robert J. Shiller, *Challenging the Crowd In Whispers, Not Shouts*, N.Y. TIMES, Nov. 2, 2008, at BU5.

169. LEWIS, *supra* note 3.

170. DAVID EINHORN & JOEL GREENBLATT, FOOLING SOME OF THE PEOPLE ALL OF THE TIME (2008).

171. Michael Lewis & David Einhorn, *The End of the Financial World As We Know It*, N.Y. TIMES, Jan. 4, 2009, at WK9.

172. *Id.*

173. Stephen Labaton, *S.E.C. Chief Pursues Reversal of Years of Lax Enforcement*, N.Y. TIMES, Feb. 23, 2009, at B1.

> and tell tale signs or possible fraud at Bernard L. Madoff Securities and at the Stanford Group, which was accused last week of being involved in an $8 billion investor fraud, were ignored.[174]

No discussion of the lack of regulation would be complete without acknowledging the failure of regulators to curtail one of the most pernicious financial inventions that contributed to millions of Americans losing their homes—the subprime mortgage. "Subprime" is a catchall term which describes suspiciously cheap mortgages peddled to the elderly, first-time homebuyers, and to those who were unwilling or unable to read the small print. Adjustable-rate mortgages ("ARMs")—the aforementioned liars loans, ninja loans, and no-doc loans—fall within the subprime category. Almost all subprime mortgages contain an ARM feature. The mortgages generally carry a low teaser interest rate for an initial period. That rate normally resets or "explodes" within six months to two years to a much higher interest rate, which effectively captures the interest and profit lost by the lender during the initial period. Often, when the interest rate resets, the monthly mortgage payment can increase by up to 50%.[175] This can be catastrophic for the borrowers whose incomes are generally stretched to meet the initial teaser rate payments.[176] When subprime mortgages are bundled, or packaged, together, and then sliced and diced into tranches and securitized, they often become "toxic waste," with death coming to all who invest in them.[177] In the words of Jack Rosenthal, the *New York Times* columnist, subprime mortgages "reflect the deceit, cynicism and scandalous exploitation that are taking the homes of many thousands, perhaps millions of families."[178]

Why would people buy into a subprime mortgage? Often, they are not told that the mortgage is subprime and carries an adjustable rate. Then, when they find out, the borrowers are

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174. *Id.*

175. Niall Ferguson, *Reasons to Worry*, N.Y. TIMES, June 11, 2006, § 6 (Magazine), at 46.

176. *Id.*

177. Rosenthal, *supra* note 62.

178. *Id.*

also told that they can refinance into a lower rate mortgage when the loan resets. Of course, if the borrower is a speculator, then she assumes that the property secured by the mortgage will be sold, and the mortgage paid off, before its interest rate resets. Further, mortgage brokers, who originate 50% of all mortgages, have an economic incentive to promote subprime mortgages. Lenders often pay the mortgage brokers a fee, called a yield service premium ("YSP") for placing a borrower into a subprime mortgage. YSPs are present in fully 90% of all subprime mortgages, implying that brokers needlessly pushed their clients into subprime mortgages for the YSP.[179] Subprime mortgages were not limited to the poor, elderly, or financially untutored. A study conducted by the Department of Housing and Urban Development shows that one-in-nine middle class families and one-in-fourteen upper middle class families who refinanced their mortgages were placed in a subprime loan.[180]

The problem for the economy and for many homeowners is that when the interest rates on their subprime mortgages reset, they could no longer afford their homes. As a result, they either abandoned their homes or lost them through foreclosure. George Packer's trip along State Route 54 near Tampa, Florida, and his visits to the "ghost subdivisions" along the route, vividly illustrates the problem.[181] Manny Fernandez wrote an investigative report for the *New York Times* detailing what occurred in a four block area in Jamaica, Queens County, which had the highest foreclosure rate in New York State.[182] Since 2004, thirty-nine homes in just that four block area went into foreclosure.[183] In the past five years, in southeast Queens, 226 foreclosures have been filed.[184] In 2005 alone, 69% of the homes purchased in the area were purchased with subprime mortgages.[185] The foreclosures basically turned what had been an evolving middle-class neighborhood into a depressed area

179. Elizabeth Warren, *Making Credit Safer: The Case for Regulation*, HARV. MAG., May-June 2008, at 36.

180. *Id.*

181. Packer, *supra* note 111.

182. Manny Fernandez, *Door to Door, Foreclosure Knocks Here*, N.Y. TIMES, Oct. 19, 2008, at A33.

183. *Id.*

184. *Id.*

185. *Id.*

with renewed drug activity, gangs, over-grown lots, and abandoned or vandalized homes. In short, people just disappeared.[186]

For the regulators, the shame is that they knew that the subprime debacle was coming well in advance, but they did nothing to curtail its detonation. The real estate bubble is generally thought to have burst in the late summer or fall of 2007. In June 2006, Niall Ferguson noted:

> Since March 2004, there has been a 59 per cent increase in one-year adjustable rate mortgages. But that just means that they have become more expensive for new borrowers. The key question is: When do existing A.R.M.'s reset? The answer: Soon. According to calculations published by Barron's in February, over the next two years the monthly payments on about $600 billion of mortgages taken out by borrowers in the so-called subprime market (those with checkered or nonexistent credit histories) will increase by as much as 50 per cent. This is because many A.R.M.'s have two-year teaser periods to entice borrowers. After that, the meaning of adjustable becomes painfully apparent.[187]

We were warned.

Now, we are being warned that the subprime loans given by lenders to borrowers with good credit, Alt-A loans, are about to go bust as well. Fannie Mae and Freddie Mac have long claimed that Alt-A loans were not subprime mortgages, but a subset of "A" mortgages.[188] However, in emails disclosed at a congressional hearing, it became apparent that staffers at both Fannie Mae and Freddie Mac had warned their senior executives about risk factors associated with acquiring Alt-A mortgages.[189] Despite these warnings, both agencies increased

186. *Id.*
187. Ferguson, *supra* note 175, at 50.
188. Browning, *supra* note 155.
189. *Id.*

their purchases in an "orgy of junk mortgage development."[190] Congress was not amused.[191]

On the horizon is an increase in the number of defaults on another type of mortgage: payment-option mortgages. Like subprime mortgages, payment-option mortgages are given with an adjustable rate. They typically carry a low introductory rate and give borrowers multiple payment options that may not cover the interest due, a practice known as negative amortization.[192] When the interest rate is recast, borrowers can see their monthly payment increase by up to 60%. However, unlike subprime mortgages, payment-option mortgages were offered only to borrowers with the best credit.[193] Therefore, it came as a surprise when FirstFed Financial Corp., a major California option mortgage issuer who was thought to have pared back on risky lending, reported a loss of $70 million in the first quarter of 2008.[194] Forty percent of its borrowers had become at least thirty days delinquent after their option mortgages were recast.[195] This was viewed as a bad sign, and could be an indication of the next mortgage debacle.[196]

In summation, it is appropriate to quote Professor Elizabeth Warren of Harvard Law School, who in her article, *Making Credit Safer: The Case for Regulation*, wrote that due to governmental regulation, "[i]t is impossible [in the United States] to buy a toaster that has a one-in-five chance of bursting into flames and burning down your house," but "innovation in financial products has produced incomprehensible terms and sharp practices that have left families at the mercy of those who write the contracts."[197] It should be noted that Professor Warren, who is the head of the Congressional Oversight Panel evaluating the effectiveness of

190. *Id.*

191. *Id.*

192. Ruth Simon, *FirstFed Grapples With Payment–Option Mortgages; Loans Could Be Next Nightmare for Banking Sector*, WALL ST. J., Aug. 6, 2008, at A3.

193. *Id.*

194. *Id.*

195. *Id.*

196. *Id.*

197. Warren, *supra* note 179, at 34.

the TARP payments to banks, has come under criticism from conservatives for her views about debtor responsibility for the financial crisis.[198]

The evidence is in. From across the spectrum, it would be very hard indeed to find someone who does not concur that the lack of appropriate governmental regulation added to the air within an expanding real estate bubble. The question now is whether they have learned enough from the mistakes of the past to lead us into a new age of American capitalism where *all* are protected from the most harmful, solely short-term, and purely self-interested, aspects of the free marketplace. After all, even Alan Greenspan has conceded that the marketplace does a pretty poor job of regulating itself.[199] After a twenty-year vacation, it is time for regulators to return to work.

VII. Consumerism

As Walt Kelly famously pointed out: "We have met the enemy and he is us."[200]

We have already discussed how consumerism—the obsession to buy more and bigger things, from toys to electronics to vacation homes—through the use of the home equity ATM machine, contributed to the creation of the real estate bubble and its eventual bursting.[201] The Darwinian question subject to debate is which came first: consumerism, the propensity to buy things on credit, or the bubble? Jackson Lears, the author of *Something for Nothing, Luck in America*, says that the answer is the former—debt-financed consumerism came first.[202] In his article, *The American Way of Debt: We Moralize About It. Then We Borrow*, Lear discussed the history of consumer debt in America.[203] Noting that "Americans are awash in red ink, consumer indebtedness is

198. Susan Schmidt, *Policing TARP Proves Tricky*, WALL ST. J., Feb. 20, 2009, at A4.

199. *See supra* note 149 and accompanying text.

200. WALT KELLY, POGO: WE HAVE MET THE ENEMY AND HE IS US (1987).

201. *See supra* Part IV.

202. *See* Jackson Lears, *The American Way of Debt: We Moralize About It. Then We Borrow*, N.Y. TIMES, June 11, 2006 (Magazine), at 13.

203. *Id.*

soaring, the savings rate is down to zero and people are filing for bankruptcy at record rates," he said:

> [t]he equation of debt and decline assumes that once upon a time Americans lived within their means and saved for what they bought. This is fantasy: there never was a golden age of thrift. Debt has always played an important role in Americans' lives - not merely as a means of instant gratification but also as a strategy for survival and tool for economic advance.[204]

Therefore, it should come as no surprise that American consumers were number five on *Time* magazine's list of the twenty-five people to blame for the financial crisis.[205] We were charged with living beyond our means through borrowing.[206] *Time* noted that "[h]ousehold debt in the U.S. . . . zoomed to more than 130% of income in 2007, up from 60% in 1982."[207]

The operative image of the American consumer over the last five years or so has been one of a family borrowing against the rising equity in its home, in effect turning its home into an ATM machine to purchase more and more. The examples are legion. George Packer introduces us to Jennifer and Ron Formosa.[208] She worked as a bank clerk and he worked in construction. Using a $110,000 mortgage, they built a three family home in Cape Coral, Florida.[209] "[T]hey refinanced with Washington Mutual [and] took out an equity line" in order to pay their bills.[210] The value of their house rose to $280,000.[211] They continued to borrow and used the proceeds to put in a patio, pay off the cars, and to buy a boat; and then there were the vacations, cruises, going to Orlando, taking the kids to

204. *Id.*
205. *See* Gibbs, *supra* note 4, at 22.
206. *Id.*
207. *Id.*
208. Packer, *supra* note 111, at 86.
209. *Id.*
210. *Id.* at 88.
211. *Id.*

Disney—just being Americans.[212] Then, Ron lost his job when the construction industry imploded in Florida.[213] The loss of their home came next.[214] The Formosa family thus became one of the 24,000 families on the foreclosure docket in Lee County that year.[215]

Even when families act conservatively, they can be trapped in their homes when the rock of their debt meets the hard place of their home's decreasing value. The *Wall Street Journal* recently focused on the effects of the collapse of real estate prices in Maricopa, Arizona.[216] Maricopa, which is located near Phoenix, grew from a population of 1,400 a decade ago to 37,000 in 2008.[217] The Campbell's were a typical family who moved into the area in 2005 when Mr. Campbell accepted a job transfer from San Diego to Phoenix.[218] "They scraped together a $50,000 down payment to buy a new four-bedroom home in Maricopa, for $250,000."[219] Today, because of overbuilding caused by easy money in the past, Ms. Campbell believes the house is worth half as much, and that may even be optimistic.[220] The developer who built the Campbell's' home is offering similar homes in the same subdivision "from $69.9K."[221] Zillow.com says that 75% of the homeowners in the area owe more on their mortgages than their homes are worth.[222] Those individuals, like the Campbell's, are trapped in their homes and cannot move unless they are willing to take a substantial loss. Yet, with a 20% down payment, they did nothing wrong.

In June 2006, before the real estate bubble burst in 2007, the *New York Times* devoted an entire Sunday magazine to American debt. Future historians, in their attempt to

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212. *Id.*
213. *Id.* at 210.
214. *Id.* at 92.
215. *See* Corkery, *supra* note 126.
216. James R. Hagerty, *After The Boom: In Maricopa, Ariz., a Paradise Found and Lost*, WALL ST. J., Feb. 24, 2009, at A12.
217. *Id.*
218. *Id.*
219. *Id.*
220. *Id.*
221. *Id.*
222. *Id.*

understand how the current recession got started, will most certainly be reading this prescient edition of the *New York Times* for clues. For our purposes, two quotes will be sufficient. Niall Ferguson, a professor of history at Harvard wrote:

> In the past five years alone, the value of U.S. home-mortgage debt has increased by nearly $3 trillion. Not all of that borrowing went to pay for real estate, the traditional function of mortgages. In 2004, net mortgage borrowing not used for the purchase of new homes amounted to nearly $600 billion. The International Monetary Fund estimates that this kind of equity extraction has risen from less than 2 percent of household disposable income in the year 2000 to more than 9 percent in the third quarter of last year.[223]

Additionally, Jackson Lears explained:

> The upward spiral of earning and spending survived until the 1970's, when the midcentury ideal of corporate citizenship evaporated in the harsher climate of renewed international competition. Fearing foreign rivals, American business ended its implicit social contract with unions by seeking cheap labor in overseas markets. During the 1980's, while real income continued to stagnate for most Americans, the ascendancy of Ronald Reagan gave government sanction to unprecedented consumer spending. Reagan's rhetorical refusal of limits combined with the deregulation of the lending industry to detach dreams of luxury from previous constraints. As money worship mounted, job security disappeared and inequalities widened, pundits spoke of a new Gilded Age. By the 1990's, bloated icons of affluence proliferated: the gargantuan pseudo-military vehicle, the 10,000-

223. Ferguson, *supra* note 175, at 48.

> square foot hacienda. A bigger standard package of household goods demanded deeper debt and accelerated the pace of the consumer treadmill. No one wanted to look like a "loser."[224]

Even former Senator Phil Gramm, deflecting the blame for the financial crisis from himself to everyone else, wrote in an Op-Ed piece for the *Wall Street Journal*:

> The Fed's sharp, prolonged reduction in interest rates stimulated a housing market that was already booming - triggering six years of double-digit increases in housing prices during a period when the general inflation rate was low. Buyers bought houses they couldn't afford, believing they could refinance in the future and benefit from the ongoing appreciation. Lenders assumed that even if everything else went wrong, properties could still be sold for more than they cost and the loans could be repaid. This mentality permeated the market from the originator to the holder of securitized mortgages, from the rating agency to the financial regulator.[225]

Then, in the fall of 2007, shortly after the beginning of the credit crisis in May 2007, the real estate bubble burst and consumers stopped buying. Soon thereafter, major retailers such as Linens 'n Things, Sharper Image, Mervyn's, Circuit City, Steve & Barry's, Fortunoff's, and many others began to file for Chapter 11 under the Bankruptcy Code.[226] "The 5,233 new commercial bankruptcy filings in May [2008] also

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224. Lears, *supra* note 202, at 15.

225. Gramm, *supra* note 137.

226. *See, e.g.*, *Retailers and Bankruptcy*, DEAL.COM, June 2, 2009, http://www.thedeal.com/newsweekly/dealwatch/retailers-and-bankruptcy.php (discussing "some of The Deal's retail bankruptcy coverage and [analyzing] what might be in store for some not yet bankrupt but possibly teetering [retailers]").

represented a 46% increase from May 2007 . . . ."[227] On the consumer side, the *New York Times* reported that:

> [b]y the end of 2008, slightly more than 9 percent of all mortgages in the United States were either delinquent or in foreclosure, according to the Mortgage Bankers Association. The number of loans in foreclosure hit a new record of 2.3 million last year, more than double the volume in 2006, and industry analysts estimate that it will hit at least 3 million in 2009 in the absence of a government rescue.[228]

By February 2009, the financial uncertainty had driven consumer spending off the proverbial cliff. The malaise and lack of spending even reached the style pages of the newspapers. Restaurant and store openings, which only last season were lavish affairs, were suddenly becoming less spectacular, even when owners tried to make them fabulous. Club kids, the harbingers of new styles, are beginning to lose cachet to—you may gasp here—Barbie.[229] In the face of the grim economy, Kenny Kenny, club kid and style maven, admitted that "[t]he only way you can possibly make it through, darling, is to face reality . . . . Fabulousness only goes so far."[230]

Fashion Week in New York, universally known for its celebrity sightings, over-the-top displays, and excess, was "invaded instead by a palpable grimness this year."[231] "[S]ome were taken aback by just how somber the mood hanging over the crowds at Fashion Week was; several of the most devoted fashionistas said that even they were thrown into a bit of an existential crisis."[232] A Wall Street hedge fund manager who

227. Jacqueline Palank, *Bankruptcies Rise Sharply on Credit Woes*, WALL ST. J., June 4, 2008, at B6B.

228. Andrews, *supra* note 46.

229. Guy Trebay, *There's Trouble in the Tweets*, N.Y. TIMES, Feb. 19, 2009, at E1.

230. *Id.*

231. Cara Buckley, *In the Tents, Most Faces Feature Model Pout*, N.Y. TIMES, Feb. 21, 2009, at A16.

232. *Id.*

was a guest at one of the shows epitomized it all. At the end of the show, he pulled his Blackberry from his cashmere coat pocket, which by the way was missing a button, checked the stock market and groaned: "I'm watching the whole thing melting down."[233]

Even the purveyors of luxury goods, who many thought would withstand the crisis, began to experience financial pain and even started to lay off workers. Some in the industry were beginning to wonder whether a prolonged slump in consumer spending could result in an eternal backlash against conspicuous consumption.[234] Maybe we should all begin to worry. Given the fact that the economy depends upon consumer spending for growth, the words of the Formosa's, who we met earlier, should give us some pause: "I'll save my money instead of spend it . . . . I don't think I'll ever want to buy a house again."[235]

As former Senator Gramm conceded, consumer spending based on consumer borrowing was a significant factor in creating the real estate bubble.[236] It would be ironic if the slide in spending—the basis of the American marketplace—caused by the bursting of the real estate bubble, had the perverse effect of endangering the very core of American capitalism. Given our societal history of debt, perhaps we need not worry. However, the Japanese experience offers a caveat. From the 1990s through about 2000, the Japanese went through such a severe economic malaise that the period was dubbed "The Lost Decade."[237] "Stunted wages and depressed stock prices . . . turn[ed] [the] once free-spending [Japanese] consumer into" a careful and constant saver.[238] Even after their economy recovered, fueled in part by an export boom to the United States and China, many Japanese have continued to save.[239] Their unwillingness to spend produced a significant drag on

233. *Id.*

234. *Sellers Confront Lapse of Luxury*, WALL ST. J., Feb. 20, 2009, at C10.

235. Packer, *supra* note 111.

236. Gramm, *supra* note 137.

237. Hiroko Tabuchi, *When Consumers Cut Back: An Object Lesson From Japan*, N.Y. TIMES, Feb. 22, 2009, at A1.

238. *Id.*

239. *Id.*

the Japanese economy. Rampant consumption is frowned upon and many people now want to live the simple life. As a result, the Japanese economy is in "free-fall because it cannot rely on domestic consumption to pick up the slack."[240] Japanese consumers felt compelled to save more in case they lost their jobs, thus creating a vicious deflationary cycle.[241] Could the same happen here in the United States?

Consumer spending, fueled by an unprecedented increase in the value of American homes and the belief that home prices would never go down, certainly contributed to the perpetuation of the real estate bubble. When the bubble burst, and home prices actually started to go down, credit dried up. Consumers stopped spending, businesses dependent on that spending began to go under, and consumers began to spend even less. More businesses, therefore, went out of business, more consumers lost their livelihoods—you see where this is going. The tea leaves are not good. In the fourth quarter of 2008, the American "gross domestic product fell at an annualized rate of 6.2 percent, the steepest decline since the 1982 recession . . ."[242] The University of Michigan reported, "an index of consumer confidence fell for the first time in three months, to 56.3, from 61.2 in January [2009]."[243] After years of unbridled consumption, American consumers are petrified. We cannot put this recession behind us until we start to spend again. This is the irony of ironies. Consumer spending based upon consumer borrowing helped to create the real estate bubble, the bursting of which led to our current financial recession. Now, to restart the economy, consumers have to start spending and borrowing again, but, as discussed above, lenders, because of losses resulting from profligate lending during the boom years, do not currently have the capital to lend.[244] "Vicious" may be the entirely proper word to describe the economic cycle in which we now find ourselves.

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240. *Id.* ("In the last three months of 2008, Japan's economy shrank at an annualized rate of 12.7 percent.").

241. *See id.*

242. Catherine Rampell, *G.D.P. Revision Suggests Long, Steeper Downturn*, N.Y. TIMES, Feb. 28, 2009, at B3.

243. *Id.*

244. *See* discussion *supra* Part IV.

I began this section with a quote from Jackson Lears: "Debt has always played an important role in Americans' lives – not merely as a means of instant gratification but also as a strategy for survival and a tool for economic advance."[245] And, for the sake of the global economy, I think we all should hope that Mr. Lears is correct.

VIII. Mortgage Fraud

Professor Elizabeth Warren quoted experts as estimating that "fraud and deception stripped $9.1 billion in equity from homeowners, particularly from elderly and working-class families, even before the subprime crisis got into full swing."[246] "[L]enders [were expected] to incur about $2.5 billion in losses as a result of mortgage fraud in 2008."[247] The Mortgage Asset Research Institute ("MARI"), in its Quarterly Fraud Report, dated December 2, 2008, reported that during the second quarter of 2008, the number of incidents of fraud and verified misrepresentations submitted by mortgage industry participants increased by 45% over the same period in 2007.[248] According to MARI, the FBI investigates mortgage fraud in two distinct areas: "fraud for profit" and "fraud for property."[249] Fraud for property covers individuals who misstate their income or assets in order to qualify for a mortgage.[250] Fraud for profit involves industry insiders, such as appraisers, brokers, title personnel, and lenders, who conspire to obtain mortgages.[251] Committing fraud for housing is an illegal action, which is perpetrated solely by borrowers.[252] Fully 80%

245. Lears, *supra* note 202, at 13.

246. Warren, *supra* note 179, at 37.

247. Bob Tedeschi, *The Widening Web of Fraud*, N.Y. TIMES, Apr. 6, 2008, at RE10 (citing a report produced by the financial consultant firm TowerGroup, Needham, Mass.).

248. MORTGAGE ASSET RESEARCH INST., MARI QUARTERLY FRAUD REPORT 2 (2008) [hereinafter MARI 2008 REPORT], *available at* http://www.marisolutions.com/pdfs/mba/mortgage-fraud-report-2008Q2.pdf.

249. MARI, Understanding Mortgage Fraud, http://www.marisolutions.com/mortgage-fraud.asp (last visited Sept. 27, 2009).

250. *Id.*

251. *Id.*

252. *See id.*

of all reported fraud losses involve collaboration or collusion by industry insiders, basically fraud for profit.[253] The types of fraud for profit include equity skimming, property flipping, and mortgage-related identity theft.[254]

Equity skimming, or as it is better known in New York, home equity theft (also known as "deed theft" or "foreclosure rescue"), starts with a homeowner, usually elderly, who is facing, or is in, foreclosure.[255] The mortgage, which is in foreclosure, is usually in an amount that is only a small fraction of the value of the property. A third party "investor" approaches the homeowner in foreclosure and offers to save the homeowner from foreclosure. To do this, the investor requires that the homeowner, sometimes with disclosure, but more often without, convey the mortgaged property to the investor. The investor promises to return the property to the homeowner once that person meets an easy payment plan. Of course, the homeowner in foreclosure can never meet the terms of the plan. Often, the homeowner never realizes, or is never told, that he or she has conveyed the property to the investor. Using the deed, the investor obtains a new mortgage based upon the real or inflated value of the property. The new mortgage goes into foreclosure often without the knowledge of the original homeowner, who the investor, only months before, "rescued" from foreclosure.

Over the past few years, such home equity thefts from the elderly became epidemic in areas of New York City that were experiencing gentrification and rapid increasing property valuations. Recently, the *Wall Street Journal* reported on the case of Daphne and William Webb, an elderly couple in Montclair, New Jersey, who found themselves the victims of a "foreclosure rescue" scheme.[256] After suffering a heart attack, Mrs. Webb left her job.[257] The couple soon fell behind on their

253. Fed. Bureau of Investigation, Operation Quick Flip Stats, http://www.fbi.gov/page2/dec05/chartsandgraphs.pdf (last visited Sept. 27, 2009).

254. MARI 2008 REPORT, *supra* note 248.

255. Philip Shiskin, *When 'Rescue' Means Eviction*, WALL ST. J., Feb. 26, 2009, at D1.

256. *Id.*

257. *Id.*

mortgage and their lender started a foreclosure action.[258] Two investors, Ronald Losner and Alyssa Azran, came to the Webb's rescue with a sale-leaseback offer.[259] The Webb's sold their home to Ms. Azan for $820,000 in March 2006, but they received no cash from the sale.[260] They signed a $2,600 a month lease which provided that they could buy their house back for $45,000 after paying rent for eighteen months.[261] Already, the math does not add up. Ms. Azran obtained a $533,000 mortgage from Credit Suisse, even though she had allegedly admitted on her loan application to not having a job and only having $100 in assets.[262] Ms. Azran fell behind on her mortgage payments (surprise) and Wells Fargo, the loan servicer for Credit Suisse, commenced a foreclosure action against Azran.[263] The Webb's have brought an action against Losner, Azran, and Credit Suisse for fraud, claiming that they did not understand the documents that they were asked to sign.[264] They assert that Losner, a disbarred attorney, and Azran cheated them out of $400,000 in equity that they had in their home.[265]

A New Jersey court has stayed the foreclosure action and the Webb's are paying their rent into an escrow account.[266] Undoubtedly, an investment bank packaged Ms. Azran's now non-performing mortgage into a CDO or CMO that is probably underwater itself. If one multiplies this mortgage by those taken out by thousands of other homeowners whose stories are like those of the Webb's or the Formosa's, we can see how mortgage-backed securities became so toxic. The underlying mortgages are either not being paid, or their values have decreased because of decreasing demand for the houses that have been pledged as security for the loans.

In order to prevent the type of home equity theft that the Webb's alleged happened to them, the New York State

258. *Id.*
259. *Id.*
260. *Id.*
261. *Id.*
262. *Id.*
263. *Id.*
264. *Id.*
265. *Id.*
266. *Id.*

Legislature adopted, and the Governor signed, the Home Equity Theft Prevention Act, which took effect on February 1, 2007.[267] Under the Act, a person deprived of their home equity had two years to rescind the transaction that led to the loss of their equity.[268] In addition, the Act imposed substantial criminal and civil penalties upon participants in an equity skimming transaction.[269] The Act imposes much of the burden of determining which schemes came under its purview to title underwriters, who would have to bear the cost of claims.[270] Because suspect transactions became uninsurable, home equity theft, after February 1, 2007, no longer took up space on the front pages. Also, much of the public and law enforcement's attention turned to the problems caused by subprime lending.[271]

According to MARI, Florida had the most reported incidents of mortgage fraud in the second quarter of 2008.[272] George Packer gives an example of the second type of fraud, property flipping, in his article, *The Ponzi State*:

> Karen Johnson-Crowther, another real estate agent in Fort Myers, showed me the sales history of a property in an upscale gated community which she had recently bought at a foreclosure auction. Building had begun in 2005. On December 29, 2005, the house sold for $399,600. On December 30, 2005, it sold for $589,000. On June 25, 2008, it was foreclosed on. Johnson-

267. Home Equity Theft Prevention Act, 2006 N.Y. Sess. Laws ch. 308 (McKinney). The Act, codified as Chapter 308 of the Laws of 2006, amended paragraphs (e), (f) and (g) of, and added a new paragraph (h) to, Section 595-a of the Banking Law, added new Section 265(a) to the Real Property Law and added Section 1303 to the Real Property Actions and Proceedings Law.

268. *Id.*

269. *Id.* § 3. *See also* Michael J. Berey, *Home Equity Theft Prevention Act Took Effect Feb. 1*, N.Y. L.J., Mar. 26, 2007, at 4 (providing a detailed analysis of the Home Equity Theft Prevention Act); Marvin N. Bagwell, *Home Equity Theft Prevention Act: The Title Company's Perspective*, N.Y. L.J., Aug. 13, 2007, at S6 (discussing land title trends).

270. MARI 2008 REPORT, *supra* note 248.

271. Marvin N. Bagwell, *Home Equity Theft Prevention Act: Subprime Crisis May Be Masking Effects of Statute*, N.Y. L.J., Apr. 9, 2008, at 5.

272. MARI 2008 REPORT, *supra* note 248, at 2.

> Crowther bought it in December for $325,000. I said that the one day increase in value must have been some kind of record, and she looked at me pityingly: "No."[273]

Alex Sink, the State Treasurer told Packer point blank, "That's a fraudulent transaction."[274]

Here is another example in Mr. Packer's words:

> Last fall, Michael Van Sickler, of the *St. Petersburg Times*, tracked the real-estate deals of a local tattoo-parlor owner named Sang-Min Kim, also known as Sonny. Starting in 2004, Sonny Kim made ninety sales around Tampa, mostly in poor neighborhoods, on which he cleared four million dollars. Van Sickler found that many of Kim's buyers, who put little or no money down were, untraceable, some had been convicted of drug dealing and other crimes. Kim, who has not been charged with any crimes and could not be reached for this article, closed a third of his deals with a title agent named Howard Gaines, who now faces up to forty-five years in prison on a fraud conviction elsewhere in Florida. According to law enforcement experts, drug dealers often become flippers, in order to launder money. . . .
>
> . . . .
>
> . . . Kim's deals had been financed by Wachovia, Wells Fargo, Bank of America, Lehman Brothers, Fannie Mae and Freddie Mac.[275]

Illinois ranked third in reported incidents of mortgage fraud according to MARI.[276] Susan Chandler of the *Chicago*

273. Packer, *supra* note 111, at 84.
274. *Id.*
275. *Id.* at 84-85.
276. MARI 2008 REPORT, *supra* note 248, at 2.

Tribune wrote a series of investigative articles describing a fraud that—except for a dead body in a red tracksuit—was very similar to the one in Florida, described above.[277] In Illinois, as in Florida, a realtor, mortgage broker, title agent, and straw buyer conspired to steal property from the deceased's mother, who was also deceased.[278] The Chicago case attracted national attention in the real property bar because the title underwriter, Ticor Title, denied the title claim made by the lender, Countrywide, because of Countrywide's gross negligence in funding the loan.[279] Ticor asserted that Countrywide's actions came under the policy's "acts of the insured's" exclusion.[280] The point is made. I will pass on discussing cases from the state that is ranked number two, California. You can just imagine.

The third type of mortgage fraud, identity theft, used to be so simple. Title people of a certain age might remember the first time that a borrower showed up at a mortgage closing with a woman who he claimed was his wife, but who later turned out to be his girlfriend. Then, equal opportunity arrived, and with it, equal opportunity fraud; the wife brought her boyfriend to the closing. What is good for the goose is good for the gander. Title companies reacted by requiring photo identification at the closing. The crooks then began to manufacture fake drivers' licenses. Now, with the aid of computers and "dumpster diving," those intent upon committing fraud will steal a person's entire identity. The victim may not find out that she even purchased the property until she receives a foreclosure notice in the mail. Such claims are ruinous for everyone concerned—from lender to title company to victim.[281] No one profits except the person or persons who perpetuated the fraud.

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277. Susan Chandler, *This House was a Steal*, CHI. TRIB., Feb. 24, 2008, at 1.

278. *Id.*; Susan Chandler, *Title Firm Ready to do Battle*, CHI. TRIB., Aug. 17, 2008, at 1 [hereinafter Chandler, *Battle*].

279. Chandler, *Battle*, *supra* note 278.

280. Complaint for Declaratory Judgment, Ticor Title Ins. Co. v. Countrywide Home Loans, Inc., No. 2008-CH-25938 (Ill. Cir. Ct. filed July 18, 2008), 2008 WL 3991700. *See also* Marvin N. Bagwell, *Obligation Contested: Insurer's Suit Could Have National Implications*, N.Y. L.J., Oct. 8, 2008, at 5; Chandler, *Battle*, *supra* note 278.

281. *See generally* Marvin N. Bagwell, *Identity Theft Fraud Is Alive and Well*, N.Y. L.J., Aug. 8, 2005, at S5.

When identity theft is added to equity skimming or flipping, the damages can be huge. The *New York Times* reported that federal prosecutors recently indicted four individuals who conspired to obtain $10 million in mortgage loans, using persons living in a halfway house and public housing as homebuyers.[282] It appears that flipping, with the aid of appraisers and a bank employee, may have been involved.[283] When the mortgage fraud also involves investors, that is, when people provide a lender with funds to make mortgages, the losses can take years to resolve and ruin lives. It took a decade, but authorities are now holding Wayne Puff in jail for orchestrating a Ponzi scheme on top of a mortgage fraud that may cost New Jersey investors $55 million.[284]

It should be clear from the above discussion on securitization that mortgage lenders deserve part of the blame for the real estate bubble.[285] Including Angelo Mozilo of Countrywide at number one, eleven bankers also appear on *Time* magazine's list: (1) Joe Cassano of AIG at number seven; (2) Dick Fuld of Lehman Brothers at number eleven; (3) Marion and Herb Sandler of World Savings Bank at number twelve; (4) Stan O'Neal of Merrill Lynch at number fifteen; (5) John Devaney, a hedge fund purchaser of option ARMs, at number eighteen; (6) Lew Ranieri of Salomon Brothers, who invented mortgage pooling, at number twenty; (7) Fred Goodwin of the Royal Bank of Scotland at number twenty-two; (8) Sandy Weill of Citigroup at number twenty-three; and (9) Jimmy Cayne of Bear Stearns at number twenty-five.[286]

Not only did these mortgage lenders and buyers create, sell and buy mortgage securities that resulted in devastating losses throughout the financial markets nationwide at the retail level, but their shoddy underwriting permitted fraud to occur. For example, the Ontario Teachers' Pension Plan Board, in a suit filed against Washington Mutual Bank, ("WaMu") (which, in

282. Benjamin Weiser, *4 Indicted in $10 Million Subprime Mortgage Fraud*, N.Y. TIMES, Feb. 20, 2009, at A28.

283. *Id.*

284. Russ Buettner, *First, Investors' Real Estate Boom, and Now a Bust*, N.Y. TIMES, Oct. 19, 2008, at LI8.

285. *See* discussion *supra* Part III.

286. Gibbs, *supra* note 4.

order to prevent its collapse, the Federal Government arranged for it to be taken over by JPMorgan Chase), complained that it was all about the number of loans and not the quality.[287] The employees were instructed to approve loans, "no matter what."[288] "They didn't care if we were giving loans to people that didn't qualify. Instead, it was how many loans did you guys close and fund?"[289] Proper documentation or not, the securitization machine had to be fed.

As noted above, mortgage fraud has numerous permutations. We are probably not aware of all of them, and most certainly, new ones are being perpetuated and invented every day. In answer to the question, "Why do you rob banks?", Willie Sutton is reputed to have responded, "[b]ecause that is where the money is."[290] When it comes to mortgage fraud, the same holds true, except that instead of one, or even a dozen banks being the victim, this time it was an entire global financial system. Although we may never know the amount, there can be no doubt that mortgage fraud was a major contributor to the inflation of the real estate bubble and to its eventual bursting.

IX. Conclusion

People working in the title industry have been greatly affected by the bursting of the real estate bubble. Major underwriters, Commonwealth and Lawyers' Title, now have new corporate owners. Hundreds of title offices have been closed. Many companies, especially on the West Coast, have entered bankruptcy. Hundreds of employees in New York, and thousands across the nation have been laid off. Despite the suffering, many people in the industry question whether we could have done anything to prevent the real estate bubble from being created and from bursting. After all, we attended the closings and saw many transactions where we knew that

287. Gretchen Morgenson, *Was There a Loan It Didn't Like?*, N.Y. TIMES, Nov. 2, 2008, at BU1.

288. *Id.*

289. *Id.*

290. *See* Albin Krebs, *Willie Sutton is Dead at 79*, N.Y. TIMES, Nov. 19, 1980, at A31.

the borrower could not pay the mortgage and had no idea what a subprime, adjustable rate, or negative amortization meant. We often predicted, with some accuracy, that the borrower would default, and that in ninety, maybe 120, days, we would be running a foreclosure search on the same property. Perhaps we could have prevented a closing every now and then, but the purpose of this over-lengthy Article was to show that it would have been akin to one person's putting his or her finger in a dike that surrounded not only Wall Street, but also London, Dublin, Beijing, Tokyo, Taiwan, Paris, Sydney, Rihayd, Dubai, Singapore, Caracas, Mexico City, Toronto—anywhere money was to be made.

Quite frankly, the financial forces arrayed against anyone trying to stop the flood would have made deterrence impossible. Title people need not feel guilty. Nobody can live without air. The forces of securitization, globalization, lack of regulation, speculation, consumerism, and mortgage fraud would have conspired to render any Cassandra voiceless and impotent. The only saving grace is that we have the opportunity to learn from the current crisis so that we do not repeat our borrowing and investment errors. The next time, and there will be a next time, we will not make the same mistake. The next bubble will not involve real estate. After all, no one really speculates obscenely on the price of tulips anymore. Or do they?