

ISSUE ALERT

**A Multi-Billion Dollar Bailout for Those at Fault:
Corporate Homebuilders, the Housing Crash
and the Mortgage Crisis**

UPDATE



Laborers'
International
Union of
North America

LIUNA!

A Multi-Billion Dollar Bailout for Those at Fault: Corporate Homebuilders, the Housing Crash and the Mortgage Crisis

THE HOUSING MARKET CRASH and meltdown of the mortgage industry has cost more than 200,000 construction workers their jobs, put 3 million American families in danger of foreclosure and gutted the value of what was the financial security net for most working men and women: their homes.

As Congress and others consider policy proposals—including the Foreclosure Prevention Act—to remedy this crisis which has pushed the nation toward recession, lawmakers are being lobbied by corporate homebuilders. Among the remedies corporate homebuilders have sought is a three-year extension of the net operating loss (NOL) carry back for 2006 and 2007, which would allow homebuilders to claim losses on their taxes as far back as 2003. Current revisions to their proposal have trimmed the carry back to four years.

The half-million members of LIUNA—on the forefront of the construction industry, a powerhouse of 10 million workers who produce 5 percent of the U.S. economic output—believe this must be rejected for three significant reasons.

- The carry back proposal will potentially further decimate the housing market and home values across America.
- Corporate homebuilders are seeking a handout for a crisis they recklessly helped create.
- The remedy corporate homebuilders propose won't help those who need it most—homeowners and residential construction workers.

A Multi-Billion Taxpayer Bailout Will Do More Harm Than Good

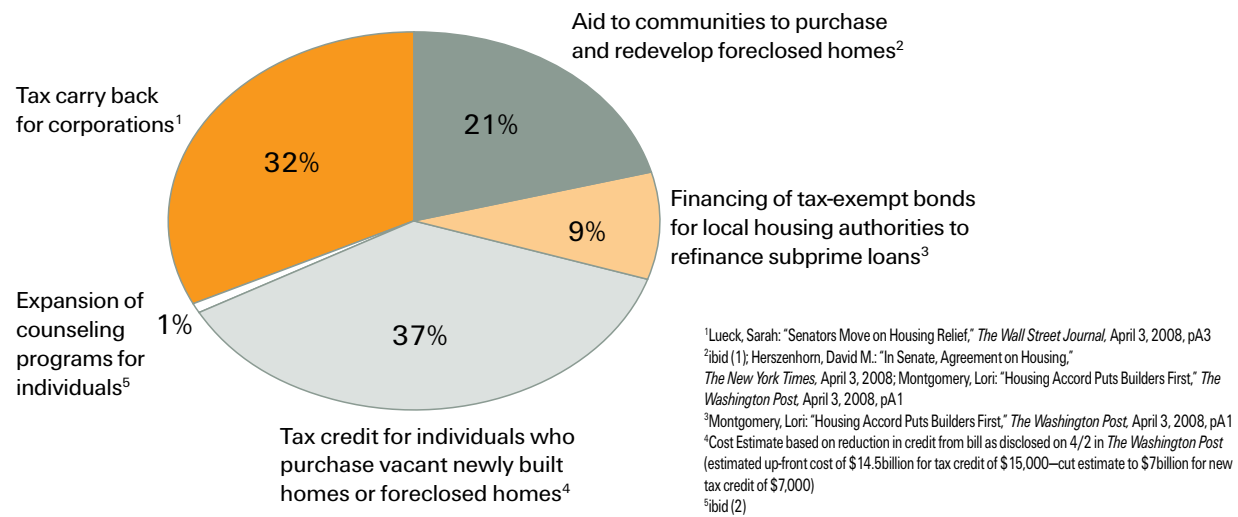
The Joint Tax Committee has estimated the total cost of the carry back would decrease U.S. government revenues by \$15 billion in 2008 alone.¹ Current estimates, based on a revised bill in Congress, estimate the first year cost at \$6 billion. In fact, the true cost is unclear—Joint Tax Committee estimates are based on the state of the economy, and the committee has increased its cost estimate by more than \$1

billion alone in a matter of months. In addition, the committee bases total costs on projections and assumptions which they decline to release to the public.

What is clear is that the handout to homebuilders will cost billions of dollars and makes up a third to a half of the cost of the Foreclosure Prevention Act. One study estimates the cost to taxpayers of a three-year extension at \$33 billion, of which a third—\$10.8 billion—would go to the 15 largest, and among the most profitable, homebuilders in the country.²

Nor would this raid on the Treasury help the taxpayers who would foot the bill. In fact, in a recent report on options for economic stimulus, the Congressional Budget Office gave the proposal to extend the loss carry back period its lowest cost effectiveness rating out of three possible ratings, coupled with the highest rating of uncertainty about the policy’s effects.³ The CBO noted the carry backs are “unlikely to generate substantial changes in investment in the short run.”⁴ So while it’s unlikely to create new business investment, it would surely enrich after-tax income for big builders, which can already claim refunds on two years’ worth of taxes. Under current law, for example, Lennar, the second-largest builder in the country, is now expecting a tax refund of \$800 million this year.⁵

Fig. 1: Senate Housing Bill Disclosed Costs, Total Estimated Cost of Bill: \$18.8 Billion



Not only would this proposal from the nation’s largest homebuilders force American taxpayers to reward reckless behavior, it would potentially further lower the values of working families’ homes by giving builders an incentive to dump their existing inventory because they can recoup losses through a tax refund. According to research by Wachovia, the bailout provision would not generate a positive cash flow for many builders without the rapid sales of land at decreased values.⁶ While this might increase corporate builder profits, it would drive home prices down further in areas hardest hit by the current crisis.

Fig. 2: Estimated Tax Payer Bailout for Top Corporate Homebuilders⁷

Corporate Homebuilder	Estimated Tax Bailout
D.R. Horton	\$1,368,800,000
Pulte Homes	\$1,034,800,000
Centex	\$1,002,800,000
KB Home	\$ 695,900,000
Toll Brothers	\$689,700,000
Lennar Corp.	\$531,700,000
Hovnanian Enterprises	\$465,600,000
The Ryland Group	\$434,800,000
MDC/Richmond American	\$416,000,000
Standard Pacific	\$193,200,000
Meritage Homes	\$148,300,000

In fact, the nation's fourth largest builder has said it has done exactly that, selling 8,500 homes at 30 percent of book value of \$161 million. The expected tax refund for Centex's land fire-sale is \$294 million.⁸

Giant Homebuilders Helped Create the Housing Crash and Mortgage Crisis

Corporate homebuilders hope America sees them as passive Main Street victims of the current crisis. They and their lobbyists do not want the story told of their role in helping to create the mortgage and housing crisis and the current slide toward recession.

The corporate homebuilding industry in America contributed to the crisis in several ways.

By taking advantage of a lax—and in many cases, fraudulent—mortgage environment, the actions and business practices of major homebuilders helped to create the mortgage crisis and continuing wave of foreclosures. In order to control the buying process, most large homebuilders have their own mortgage subsidiaries to which they steer the majority of homebuyers. Homebuilders originated tens of thousands of mortgages each year in essentially every major market.

The builders' mortgage companies also pushed predatory and risky mortgage products, such as those with negative amortization, loans requiring only stated income, or piggy-back loans with high-cost second mortgages, all in order to lure homebuyers into qualifying for houses which were sold at what are now clearly inflated prices. For example, 40 percent of the mortgages originated in 2006 by Richmond American's subsidiary, HomeAmerican Mortgage, were interest-only ARMs.⁹

An analysis of data provided by the Home Mortgage Disclosure Act (HMDA) shows that homebuilders increasingly sold high-cost mortgages and first and second mortgage combinations (80/20 loans) with high-cost second mortgages.¹⁰

From 2005 to 2006, homebuilder-originated subprime loans increased significantly faster than prime loans. For instance, the number of subprime loans originated by homebuilder giants Lennar and Pulte more than doubled from 2005 to 2006, while their prime mortgage originations remained the same or decreased.

Fig 3: Increase in Subprime Loans

Lender	2006 Prime Loans	2005 Prime Loans	% Increase in Prime Loans	2006 Subprime Loans	2005 Subprime Loans	% Increase in Subprime Loans
DHI Mortgage (DR Horton)	38,632	34,339	12.50%	10,644	6,651	60.04%
HomeAmerican (Richmond American)	9,809	9,465	3.63%	2,233	746	199.33%
KB/Countrywide (KB Home)	15,500	5,309	230.57%	5,934	1,175	405.02%
Pulte	27,784	27,539	1.00%	3,212	2,016	59.33%
Shea	4,370	4,059	7.66%	510	253	101.58%
Universal American (Lennar)	20,368	21,843	-6.75%	5,978	2,321	157.56%

The HMDA analysis also showed high-cost loans increased as a share of total loans in 2006 over 2005.

Fig 4: Increase in High Cost Loans

Lender	2006 % of Loans that are High Cost	2005 % of Loans that are High Cost	% Change
DHI Mortgage (DR Horton)	21.60%	16.20%	33.33%
HomeAmerican (Richmond American)	18.54%	7.31%	153.63%
KB/Countrywide (KB Home)	27.68%	18.12%	52.76%
Pulte	10.36%	6.82%	51.91%
Shea	10.45%	5.87%	78.02%
Universal American (Lennar)	22.69%	9.61%	136.11%

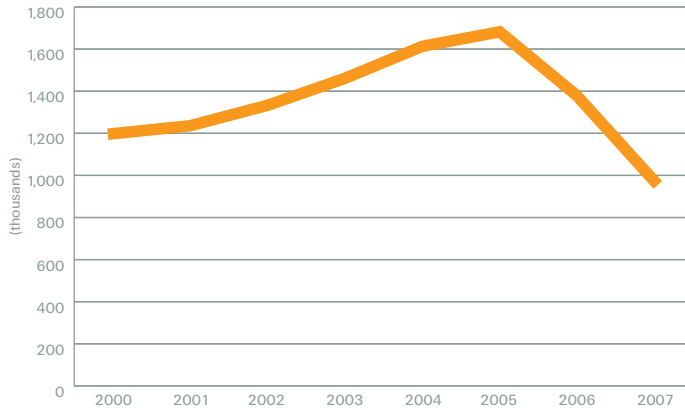
Feeding a Wave of Speculative Investors and Wall Street Expectations

The exponential increase in homebuilders' marketing of subprime and exotic loans enabled sales to continue even after markets were overbuilt, albeit to buyers who were later to become threatened with foreclosure.

The chief lobbying organization for corporate builders, the National Association of Homebuilders, acknowledges that builders continued to flood the market with new construction, even when it became clear that demand for new homes was slowing down.¹¹

Between 2003 and 2006, 6.27 million new single-family homes were built, peaking with 1.68 million homes built in 2005 as homebuilders raced not only to feed consumer demand, but also the demand of speculators who were betting on ever-rising housing costs, and the demands of Wall Street, which rewarded ever-increasing sales and as has now come to light, irresponsible lending. These factors helped create and reinforce an artificial, weak and inflated market. (Fig. 5)¹²

Fig. 5: Single Unit Building Permits 2000-2007¹³



With the nation’s for-sale housing inventory now at almost 5.5 million homes and new homes constituting about 11 percent of that amount, housing starts have decreased 25.2 percent from 2006 and 33.5 percent from 2005. New home sales have decreased by similar percentages during this time.^{14, 15}

Forty percent of the new homes built in the last two years were constructed by the largest corporate builders, with each adding tens of thousands of homes each year. Despite their contribution to the market crash, builders reaped enormous profits. In 2006, the top 10 builders alone made \$16 billion in profits on \$100 billion in revenues. (Fig. 6)

Fig. 6: Top 10 Builders 2006¹⁶

Rank	Company	Total Closings 2006	Total Revenue 2006 (\$ millions)
1	D. R. Horton	53,410	15,016
2	Lennar Corp.	49,568	16,267
3	Pulte Homes	41,487	14,274
4	Centex Corp.	37,539	14,400
5	KB Home	32,124	11,004
6	Hovnanian Enterprises	20,201	7,016
7	Beazer Homes USA	17,500	5,159
8	The Ryland Group	15,392	4,757
9	NVR	15,139	6,134
10	MDC/Richmond American	13,123	4,802

But in doing so, homebuilders ignored real market conditions in order to maximize profits. According to the NAHB, “Economists were starting to say this is a cyclical business and we are going to get into a downturn. But some [builders] were chasing the gold and pursuing the brass ring, and they didn’t heed the market warnings as quickly as they should have.”¹⁷

According to the NAHB, “There were some builders [who] were probably overly aggressive. There’s no question about that.” Many of these builders kept building, kept buying land, and kept pushing their own brand of subprime and exotic mortgage products.

Builders also did little to curtail speculative investors. The massive amount of speculative purchasing raised overall housing prices, resulting in greater profits for builders and greater reliance on subprime and riskier mortgages—as well as rising costs for buyers. In major markets like Phoenix, Fort Lauderdale, and Las Vegas, almost one in six houses were purchased by investors. (Fig. 7)¹⁸ From late 2003 to the first part of 2005, speculators drove up Las Vegas new home prices by 40 to 50 percent, and in some communities nearly half of sales went to speculators.¹⁹

Fig. 7: Top 5 Markets in 2005 with the Most Speculative Activity²⁰

Phoenix-Mesa, Arizona	17.10%
Fort Lauderdale, Florida	17.00%
Sacramento, California	16.40%
Las Vegas, Nevada	16.00%
Miami, Florida	15.30%

The result of investors being given free reign would later be that entire communities of homeowners—who played no part in creating the current crisis other than seeking their American Dream—are suffering the consequences. If the bailout provision is passed, struggling homeowners stand to suffer even more as the bailout will encourage the selling off of land by corporate homebuilders at decreased values²¹ which will further depress the home market and may lead to a second wave of damaging speculative investments.

Illegal Behavior?

There are widespread allegations of builders engaging in illegal and unethical practices to market loans, downplaying the risks to lenders, denying traditional fixed-rate loans to buyers who would have qualified for them, and outright selling loans to borrowers who didn’t understand the product, the loan structure or the escalating payments that trapped their homes.

Through 2006 and 2007, HUD reached millions of dollars in settlements with homebuilders over allegations that they engaged in illegal business practices involving captive title reinsurance and that they accepted illegal kickbacks from title insurers in the form of payments in exchange for referrals. These investigations netted most of the big builders, including Richmond American, Beazer, Shea, KB Homes, and Pulte. Each corporation settled for hundreds of thousands of dollars.^{22,23,24}

In other cases involving mortgage wrongdoings, KB Home paid a record \$3.2 million settlement with HUD over allegations that its mortgage unit was responsible for poor underwriting practices such as approving loans to borrowers who were not eligible.²⁵ Beazer Homes said it would restate financials for a three-year period after an internal probe found employees in its mortgage origination unit violated federal lending rules.²⁶ After investigations by the U.S. Attorney and the SEC, Beazer Homes exited the mortgage origination business and announced its intention to pull out of various geographic markets.^{27, 28}

Homeowners, Not Corporate Builders, Need Help

As housing construction has dropped precipitously and foreclosures have skyrocketed, the impact has been tragic.

Millions of families face eviction and loss of their homes. In just 2007, nearly 1.3 million U.S. housing properties were subject to foreclosure activity, a 75-percent increase over 2006. Nevada—a market heavily dominated by corporate homebuilders—had the highest rate, with 3.4 percent of households falling into foreclosure, more than three times the national average and up more than 200 percent from 2006 (see Fig. 8). Florida was second, followed by Michigan, California, Ohio, Georgia, and Arizona.²⁹

Americans not facing foreclosure are seeing the value of their primary investment decimated. Nationally, homeowners have lost a median of about \$20,000 in resale value in just the last year, according to the January 2008 Standard & Poor's/Case-Shiller index.

As expected, in the areas with the highest foreclosure rates, the values of home prices have decreased dramatically. In Las Vegas, prices have dropped 21 percent in the past 20 months, returning to 2004 levels.³⁰ In Maricopa County, Arizona, which saw a six-fold increase in foreclosures over two years ago, housing prices have dropped by double-digit percentages.³¹

According to the Federal Reserve Bank, the rapid decline in home values has helped reduce to below 50 percent the equity Americans have in their homes—the lowest since 1945.

Fig. 8: U.S. Foreclosure Market Statistics by State—2007 Totals³²

Rate Rank	State Name	Total Foreclosure Filings	%Change from 2006–2007	%Change from 2005–2007	Total Properties with Filings in 2007	% Households in foreclosure in 2007
–	United States	2,203,295	74.99	148.83	1,285,873	1.033
37	Alabama	7,903	81.76	83.07	5,572	0.268
28	Alaska	1,650	54.64	17.69	1,332	0.486
8	Arizona	69,970	150.91	160.70	38,568	1.516
26	Arkansas	14,310	26.44	23.58	6,406	0.513
4	California	481,392	237.99	681.95	249,513	1.921
5	Colorado	71,149	29.96	140.12	39,403	1.919
16	Connecticut	23,470	100.05*	111.38*	11,860	0.833
38	Delaware	1,430	225.00*	342.72*	999	0.266
–	D.C.	800	607.96*	393.83*	777	0.28
2	Florida	279,325	123.96	129.25	165,291	2.002
7	Georgia	99,578	31.07	118.43	59,057	1.566
43	Hawaii	1,270	88.71	-60.39	966	0.197
20	Idaho	6,032	140.51*	119.83*	3,640	0.611
9	Illinois	90,782	25.29	94.30	64,310	1.25
10	Indiana	52,930	11.31	73.57	27,980	1.027
33	Iowa	7,404	114.92*	251.90*	4,103	0.314
42	Kansas	4,978	20.85	161.31*	2,434	0.203
35	Kentucky	8,793	23.45	76.96	5,105	0.274
41	Louisiana	7,331	151.58*	90.61	3,968	0.204
48	Maine	N/A	N/A	N/A	286	0.042
17	Maryland	25,109	455.26	388.41	18,879	0.83
19	Mass.	41,487	161.14	751.36	17,737	0.66
3	Michigan	136,205	68.32	282.22	87,210	1.947
25	Minnesota	13,615	127.11*	506.73*	11,557	0.513
45	Mississippi	1,997	91.65	4.55	1,409	0.114
13	Missouri	32,022	80.93	176.74	23,492	0.906
36	Montana	1,378	29.27	52.60	1,150	0.268
30	Nebraska	3,971	30.88	91.84	3,636	0.474
1	Nevada	66,316	215.12	758.68	34,417	3.376
40	New Hampshire	N/A	N/A	N/A	1,238	0.212
14	New Jersey	53,652	34.06	52.75	31,071	0.902
32	New Mexico	3,893	-26.04	-46.55	2,994	0.357
27	New York	57,350	10.19	54.72	38,688	0.493
18	North Carolina	37,426	66.52	135.07	29,101	0.739
46	North Dakota	308	74.01	86.67	250	0.082
6	Ohio	153,196	87.93	207.35	89,979	1.797
23	Oklahoma	13,594	-12.78	0.71	8,256	0.52
22	Oregon	10,746	12.25	56.76	8,461	0.543
34	Pennsylvania	34,089	-11.07	18.98	16,379	0.302
31	Rhode Island	3,241	153.80*	7804.88*	1,838	0.41
39	South Carolina	5,038	-27.56	-33.76	4,247	0.22
50	South Dakota	N/A	N/A	N/A	24	0.007
11	Tennessee	45,834	24.56	65.66	25,914	0.983
12	Texas	149,703	-4.57	9.22	84,469	0.936
15	Utah	9,668	-25.87	-16.19	7,438	0.852
49	Vermont	61	35.56	1.67	29	0.009
24	Virginia	24,199	456.3	728.73	16,307	0.514
21	Washington	23,705	27.95	59.47	15,184	0.573
47	West Virginia	1,135	30.31	10.95	460	0.053
29	Wisconsin	17,503	131.15*	241.79*	12,133	0.486
44	Wyoming	497	21.52	99.60	356	0.151

The Workers Who Build America Are Suffering

Hundreds of thousands of jobs have evaporated in residential construction since peaking in September 2006. Some areas have been hit harder than others. For example, from October 2006 to December 2007 in Arizona, where almost one in 10 jobs is construction related, almost 27,000 construction jobs disappeared.³³

As 2007 ended, the nation had lost 232,000 jobs in all construction sectors as losses began to spill over into non-residential sectors.

Fig. 9: States With Loss of Construction Jobs From January 2007 to January 2008³⁴

Alaska	-800	Minnesota	-4,200
Arizona	-23,600	Missouri	-100
Arkansas	-1,000	Nevada	-8,900
California	-69,300	New Hampshire	-200
Delaware	-600	New Jersey	-3,800
District of Columbia	-100	New Mexico	-700
Florida	-69,000	Ohio	-4,200
Georgia	-600	Oklahoma	-300
Idaho	-1,300	Oregon	-4,800
Illinois	-5,200	Rhode Island	-2,300
Indiana	-3,600	South Carolina	-900
Iowa	-1,400	Vermont	-900
Maine	-400	Virginia	-5,200
Maryland	-900	West Virginia	-3,100
Massachusetts	-3,600	Wisconsin	-6,000
Michigan	-10,600		

Many more jobs have been lost in supporting industries such as real estate, banking and other housing-related fields, and the nation's slide into recession is due largely to the current housing and mortgage crisis.

Instead of taking responsibility for a crisis they helped create, corporate builders are asking every group *not* responsible to bail them out through extensive lobbying for the carry back provisions.

The hundreds of thousands of construction workers already laid off and the additional construction workers facing layoff are not to blame. Over the next two years, 1.8 million more subprime mortgages are scheduled to reset to higher interest rates, throwing another wave of homeowners into foreclosure.³⁵ Neither these homeowners, nor the victims before them, are to blame. U.S. taxpayers, already reeling from impending recession, are not to blame.

Corporate homebuilders profited from the creation of the current crisis. They should not be further rewarded with a multi-billion dollar bailout.

Endnotes

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