Blackbox Greenleaf: Lender Behavior Under Uncertain Collateral Enforcement

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Background

- Paper uses Maine Supreme Court ruling in “Bank of America vs. Greenleaf" on July 3, 2014
  - Court ruled that Mortgage Electronic Registration Systems (MERS) did not have the ability to assign mortgage contracts
  - This meant that when mortgage contracts had been sold to another creditor, MERS did not have the ability to make the assignment
  - Therefore if a mortgage was in default, before beginning foreclosures, the current creditor needed to get a letter from the originator asking them to officially assign the mortgage
- Shocks the enforcement of collateral for Maine lenders
  - **Assumptions:**
    - Lenders geographically far from shock would not know about the ruling
    - Thus exposure to Maine MERS mortgages would increase salience of shock to lenders
    - Banks who have more exposure to Maine MERS loans, have a higher uncertainty about how courts will enforce foreclosure

Treatment

- Treatment defined as fraction of Maine MERS originations relative to all their other New England (NE) (non-Maine) originations.
- Exposure measure

$$BankTreatment = \frac{MERSMaineLoanVolume_b}{NewEnglandLoanVolume_b}$$

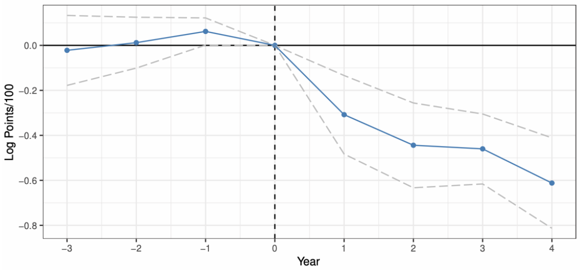
$$TractTreatment = \frac{MERSMaineLoanVolume_b}{NewEnglandLoanVolume_b} \times \frac{LendingVolumeInTract_b}{TotalLendingVolumeinTract}$$

Paper Results

$$Y_{c,b,t} = \alpha + X'_{c,b,t}\gamma + \delta D_b \times Post_t + \epsilon_{c,b,t}$$

- Finds that originations fall following the regulation
- Result driven by portfolio loans because that is where banks really care about foreclosure

Figure 4. Difference-in-Differences Estimates: Log(Portfolio Loan Volume)

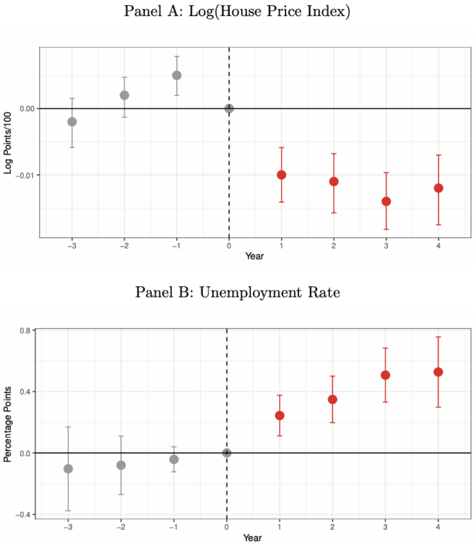


Paper Results

$$Y_{c,b,t} = \alpha + X'_{c,b,t}\gamma + \sum_{s=-3}^{4} \delta_s D_b \times \{t = s\} + \epsilon_{c,b,t}$$

- Home prices fall
- Unemployment rises

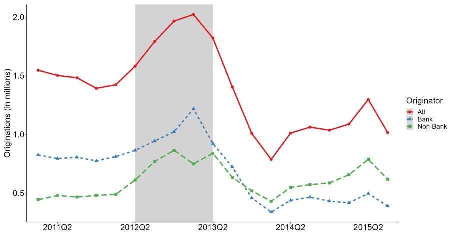
Figure 8. Difference-in-Differences Estimates: Real Effects



Main Comment 1

- Why would new originations be affected?
    - Banks can rewrite MERS sentence
- **Concern:** Bank lending volume decreased significantly for the largest banks post Basel III, other regulatory changes were also passed in 2014
    - Large banks were under the most regulatory pressure such as GSIBs, SIFIs, and other large banks
    - New capital requirements made it costly to take up balance sheet space
    - Portfolio loans take up more balance sheet space than securitized loans
    - DOJ law suits made non-agency loans costly

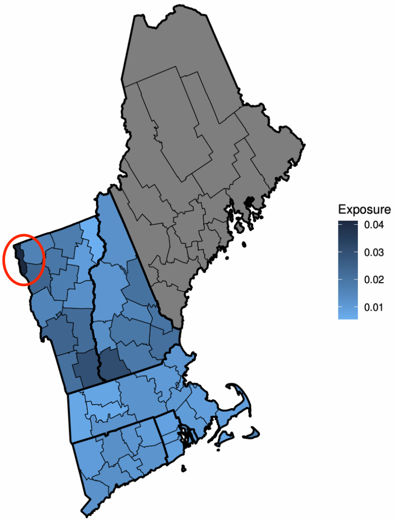
Originations Post Basel III



Main Comment 1

- Note if a bank has a high exposure to Maine and is fairly concentrated in NE (only one bank lends in an area), it will have a high tract treatment
    - If a bank is highly exposed to bank regulation, would create the effects that the author observes in terms of lending volume and home prices

Figure 2. Exposure to Greenleaf judgment Across New England



Comment 2

- Assumes banks care about Maine courts' decisions on foreclosure.
  - This is correlated with current treatment, which is higher ***Maine MERS lending***.
  - However, current treatment is exposure to securitized loans. It is being used as a proxy for salience but if the assumption is that Maine lenders care about Maine courts, the lenders should care about all Maine loans.
  - Treatment is putting higher weight on banks that do more securitizing. These are going to be the larger banks. The shock should affect any bank that originates in Maine, even if it does not do much securitizing.
  - Conversely, the current treatment measure – shares of Maine MERS loans – also applies to non-banks, non-banks securitized MERS loans and therefore have exposure to the shock, however their originations have been increasing over this time period.

- Run robustness test with treatment as volume of ***Maine lending***
- Control for bank capital requirements - run regressions by bank tier that is regulated

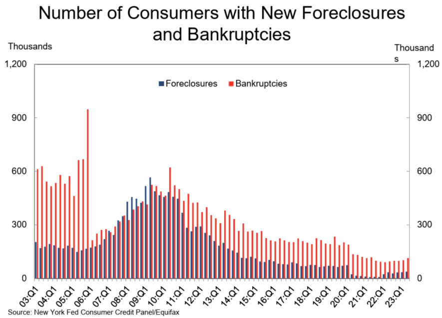
Comment 3

- Is Maine typically borrower friendly in Foreclosure?
- Do banks move away from Maine and toward other states post shock?
- This we would expect to see in securitized loans, as well as portfolio loans.
  - If investors that a state is likely to have a similar ruling, they may offer lower prices for packages of loans in those states, causing banks to move away from them.
  - Hamdi, Jiang, Lewis, Padi, Pal (2023) find that non-bank servicers foreclose most, bank portfolio loans second most, and finally bank GSE loans

Comment 4

- Foreclosures are decreasing over this time period, so it is surprising that ruling caused such a large effect
- Would expect the opposite result on the labor market
  - Paper establishes that credit to small businesses increases
  - Previous work finds that moratorium on foreclosure boosts the labor market by giving borrowers liquidity they need to continue job searching after a negative income event (Padi, Banga, Meng (2023), Pal (2023))

Originations Post Basel III



Comment 5

- Use monthly data - merging with tax and deed and putting the MERS flag on to HMDA data should enable merging on the month
  - Sharpen ability to isolate the timing of the shock
- Get anecdotal evidence that lenders did not know about this shock
  - My prior is that it would send shock waives through the securitization industry because they should all be looking checking their exposure to Maine MERS contracts