

By Margaret Chadbourn

April 30 (Bloomberg) -- The U.S. Senate rejected a measure that would let bankruptcy judges cut mortgage terms to help borrowers avoid foreclosure, a victory for banks and credit unions that said the legislation would increase loan costs.

The proposed "cram-down" amendment to a housing bill was defeated today in a 51-45 vote, with 12 Democrats among the 51 opponents. The measure needed 60 votes to pass over Republican objections. The House passed its version 234-191 on March 5.

"These bankers who brought us into this crisis are literally shunning and stiff-arming the people who are facing foreclosure," said Senator Richard Durbin of Illinois, sponsor of the legislation and the chamber's second-ranking Democrat.

The defeat is a setback for President Barack Obama's administration, which included cram-down in the anti-foreclosure plan aiming to help 9 million homeowners. The mortgage industry has twice succeeded in helping to kill the proposal since Durbin first introduced it in 2007. The senator said today "this is not the last time" he will raise the issue.

Democrats led by Durbin had sought a compromise on the measure with JPMorgan Chase & Co., Wells Fargo & Co., Bank of America Corp., the American Bankers Association and Financial Services Roundtable. The lenders that scuttled the negotiations are "surviving today because of taxpayers' dollars," Durbin said. The three banks he named received \$95 billion in U.S. aid.

"It's clear that part of the mortgage industry was never interested in meeting us halfway, as negotiations went forward, they moved the goalpost back and back," said Senator Charles Schumer, a New York Democrat.

'Greedy, Stubborn'

Banks that refused to negotiate a compromise were "greedy, stubborn and unreasonable," said Senator Sheldon Whitehouse, a Rhode Island Democrat.

Durbin had proposed limiting the size of mortgages eligible for modification by judges, and his proposal would have covered loans issued through Jan. 1 or delinquent for 60 days. A provision in the legislation also would have required borrowers to contact loan servicers 45 days before filing for bankruptcy.

Arizona Republican Senator Jon Kyl, whose state had the second highest rate of foreclosures in the first-quarter report by Irvine, California-based RealtyTrac, said the measure would force mortgage companies to increase interest rates.

"The answer is not to incentivize bankruptcy by making it the means to save one's home," Kyl said.

Higher Rates

The mortgage industry said the provision would lead to higher interest rates on other borrowers, as lenders sought to make up for their losses in court.

“The cram-down measure would have increased the cost of buying a home for all Americans, and that is the exact opposite result that everyone is working towards right now,” said Scott Talbott, senior vice president of government affairs at the Financial Services Roundtable.

A coalition of 12 financial industry groups, in a letter to senators yesterday, said the cram-down bill would destabilize the housing market. The Democratic effort lost support last week after federal credit unions refused to endorse the legislation.

“Simple common sense demands improvement in the bankruptcy process,” said David Sloane, vice president for AARP, the Washington-based advocacy group. There is “no adequate argument” to limit loan modifications in court, Sloane said.

The U.S. economy has lost 5.1 million jobs since December 2007, and unemployment rose to 8.5 percent in March, the highest since 1983. Consumers remain burdened by debt, as foreclosure filings for March totaled 341,180, a record high, according to RealtyTrac.

“The mortgage crisis continues to worsen, and the need for this legislation will only grow,” said Mike Calhoun, president of the Center for Responsible Lending. “Unfortunately, millions of homeowners and all Americans waiting for economic recovery will pay dearly for this delay.”

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