

The battle over whether local governments should have the right to seize and restructure troubled mortgages is moving to Capitol Hill.

Rep. John Campbell (R., Calif.) is set to introduce legislation on Thursday that would aim to put a stake in the heart of the movement to let cities take over severely underwater loans.

Mr. Campbell's

bill, "Defending American Taxpayers from Abusive Government Takings Act," would use government-controlled mortgage finance giants Fannie Mae and Freddie Mac, as well as the Federal Housing Administration and the Veterans Administration, to block the concept.

The eminent domain proposal impacts "private label" loans that aren't government-guaranteed and were mainly made before the housing bust. But the legislation aims to stop the practice by barring government-linked entities from buying or guaranteeing loans in counties where a local government has used eminent domain to seize a mortgage loan.

Since the vast majority of home loans come through one of these entities, the legislation would essentially stop the eminent domain idea in its tracks, **Mr. Campbell** says.

The proposal "**is banana republic-type stuff**" that would chill investment in the mortgage market, **Mr. Campbell** said. "**The whole basis of commerce in the United States is that you make transactions, you make contracts under the law and that you can count on those laws as the contracts go forward...Here you're basically going to void them.**"

Since the eminent domain concept started gaining attention over the summer, the mortgage industry has been aggressively trying to derail it. The Securities Industry and Financial Markets Association, or Sifma, has proposed prohibiting loans originated in areas using eminent domain from a key part of the mortgage-backed securities market. And the Federal Housing Finance Agency, which oversees mortgage giants Fannie Mae and Freddie Mac, has said it may take action against the idea.

California Lt. Gov. Gavin Newsom has weighed in, alleging in a letter sent this week to Attorney

General Eric Holder that mortgage investors “may be colluding to restrain trade and to redline communities in California” by conspiring to restrain lending in areas that act on the eminent domain proposal.

The eminent-domain concept is being advanced by San Francisco-based venture-capital firm Mortgage Resolution Partners. It has hired investment banks Evercore Partners EVR 0.00% and Westwood Capital to raise funds from investors. And supporters of the measure have also been working behind the scenes, meeting with potential allies on Capitol Hill in recent weeks.

“I’d find it hard to believe that Congress would support blatantly retaliatory measures against cities and counties that are exercising their statutory powers under the constitutions of their states,” said Daniel Alpert, managing partner of Westwood Capital. “This is a states’ rights issue if there ever was one.”