



Testimony of John Taylor

**President and CEO, National Community
Reinvestment Coalition**

**Before the House Financial Services
Committee**

**Testimony also on behalf of
National Consumer Law Center
Rainbow/PUSH**

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Introduction

Good afternoon, Chairman Frank and Ranking Minority Member Bachus. My name is John Taylor and I am the President and CEO of the National Community Reinvestment Coalition (NCRC). I am honored to be testifying on behalf of the 600 community nonprofit member organizations of NCRC that are dedicated to increasing access to credit and capital for minority and working class communities.¹

I am also honored to be testifying on behalf of the low income clients of the National Consumer Law Center, Inc. ("NCLC") and Rainbow-PUSH. Both Rainbow-PUSH² and NCLC³ have been in the forefront of struggle for consumer protection and civil rights for decades.

¹ The **National Community Reinvestment Coalition** is an association of more than 600 community-based institutions that promote access to basic banking services, including credit and savings, to create and sustain affordable housing, job development and vibrant communities for America's working families. Our members include community development corporations, local and state government agencies, faith-based institutions, community organizing and civil rights groups, minority and women-owned business associations and social service providers from across the nation. Their work serves primarily low- and moderate-income people and minorities. NCRC pursues its work through a variety of partnerships and programs. Our National Homeownership Sustainability Fund leverages the expertise of a national network of mortgage finance advisors. They work with servicers and lenders, on behalf of homeowners, to keep working families from losing their homes to foreclosure. NCRC's National Training Academy provides training and technical assistance on topics such as understanding how to use CRA, fair housing and foreclosure prevention. Our Economic Justice Campaign sites pilot innovative community partnerships to enhance the delivery of financial, technical, and social services to individual consumers, homeowners, and small business. NCRC's work is enhanced by two financial services advisory councils consisting of the nation's largest banks and mortgage finance companies. Quarterly roundtables examine issues involving responsible financial services-related policies, regulations, and legislation, as well as innovative products, services and best practices.

² The **Rainbow PUSH Coalition** is a progressive organization dedicated to protecting, defending and expanding civil rights, to improve economic and educational opportunity for all. The organization is headquartered at 930 E. 50th St. in Chicago. For more information about the Rainbow PUSH Coalition, please visit the organization's website, www.rainbowpush.org,

³ The **National Consumer Law Center, Inc. (NCLC)** is a non-profit Massachusetts Corporation, founded in 1969, specializing in low-income consumer issues, with an emphasis on consumer credit. On a daily basis, NCLC provides legal and technical consulting and assistance on consumer law issues to legal services, government, and private attorneys representing low-income consumers across the country. NCLC publishes a series of sixteen practice treatises and annual supplements on consumer credit laws, including Truth In Lending, (5th ed. 2003) and Cost of Credit: Regulation, Preemption, and Industry Abuses (3d ed. 2005) and Repossessions (6th ed. 2005) and Foreclosures (1st ed. 2005), as well as bimonthly newsletters on a range of topics related to consumer credit issues and low-income consumers. NCLC attorneys have written and advocated extensively on all aspects of consumer law affecting low income people, conducted training for thousands of legal services and private attorneys on the law and litigation strategies to deal predatory lending and other consumer law problems, and provided extensive oral and written testimony to numerous Congressional committees on these topics. NCLC's attorneys have been closely involved with the enactment of all the federal laws affecting consumer credit since the 1970s, and regularly provide extensive comments to the federal agencies on the regulations under these laws.

Over the last several months, NCRC has testified a number of times, warning that the nation stood on the edge of a mortgage tsunami. When we testified in the spring, we heard the regulatory agencies tell us that the “contagion” would not spread beyond the subprime market. As spring turned into summer, it was clear that the “contagion” had spread broadly throughout the housing market. The industry has flooded the market with exotic mortgage lending such as payment-only Adjustable Rate Mortgages (ARMs), and “hybrid” 2/28 and 3/27 ARMs. These exotic and/or high-cost mortgages overwhelm borrowers when interest rates shoot up after an introductory time period. The sum total of the problematic lending is that up to 2 million mortgages may end up in foreclosure this year and in 2008, costing about \$300 billion dollars. Meanwhile, the bailout of Wall Street has started - the Treasury Secretary met with large banks and convinced them to create a \$80 billion fund that will buy mortgage backed-securities in the hopes of stabilizing the housing market.

Yet, while the bailout of large financial firms has commenced, who will look out for the millions of families that will lose their homes and their only or primary source of wealth? Mr. Chairman, your bill is a sign of determined leadership to ensure that Americans will be protected against predatory lending. Your bill is comprehensive and your bill makes difficult choices, but in a few critical places, these choices need to be reversed. As we applaud your leadership, we also hope that you will strengthen certain key elements of your bill to prevent any institution from profiting from investments in unscrupulous mortgage lending practices.

Our challenge is to sustain safe and sound credit in communities. We need to eradicate the abusive lending that drains wealth. At the same time, we need to bolster safe and sound lending that builds wealth by creating affordable and sustainable homeownership for hard-working families. Your anti-predatory bill contains key elements that will curb abusive lending, so long as you ensure that it is fully enforceable against all players in the marketplace. While a strong anti-predatory bill will ensure that lending protects equity, enacting the CRA Modernization Bill of 2007 will promote safe and sound lending by applying CRA to a broad array of non-bank financial institutions. We need to apply CRA to mainstream credit unions, independent mortgage companies, insurance companies and securities firms. NCRC’s Chief Operating Officer, James Carr, is testifying today before the Subcommittee on Domestic Policy of the Committee on Oversight and Government Reform, asserting that CRA as applied to banks needs to be strengthened and that CRA needs to be applied to non-bank financial institutions.

Research demonstrates that anti-predatory lending legislation reduces abusive lending while CRA increases safe and sound lending. Professor Michael Stegman and his colleagues at the University of North Carolina concluded that while the North Carolina

anti-predatory law did not restrict overall access to credit, it did decrease loans with abusive features such as loans with prepayment penalties beyond three years.⁴ In addition, a study by Bostic, Engel, et al. concluded that state anti-predatory laws do not reduce overall credit flows. In fact, broader coverage (more high-cost loans covered), stronger enforcement, more liberal private rights of action, and stronger assignee liability are associated with higher levels of subprime originations. The authors hypothesize that consumers feel more confident receiving subprime loans in states with broader coverage.⁵ The beneficial impacts of anti-predatory law are coupled with CRA; Federal Reserve economists and Harvard University document that CRA has increased lending to minority and low- and moderate-income borrowers and communities.⁶

NCRC, NCLC, Rainbow-PUSH, and NCRC's 600 member organizations look forward to working with you to enact a strong anti-predatory lending bill and a CRA Modernization bill to stomp out abusive lending and to sustain access to credit for underserved communities during these precarious times of the mortgage meltdown.

Summary of Recommendations

Your bill has the earmarks of landmark legislation designed to address the mortgage crisis this country is facing. We applaud your leadership and urge Congress to expeditiously pass a comprehensive anti-predatory bill.

Our testimony responds to the major provisions of each Title of the The Mortgage Reform and Anti-Predatory Lending Act of 2007 and also responds to the Escrow, Appraisal, and Mortgage Servicing Improvements Act of 2007. We have three major recommendations that include:

No Preemption of State Law: We are extremely pleased that you have resisted the tremendous efforts to convince you to preempt state law with this bill. The dual goals of a federal bill addressing abusive mortgages should be, first – to change the dynamics in the mortgage marketplace and create incentives for sustainable home lending, and second – to improve and expand the consumer protections for homeowners.

⁴ Roberto G. Quercia, Michael A. Stegman, and Walter R. Davis, *The Impact of North Carolina's Anti-Predatory Lending Law: A Descriptive Assessment*, the Center for Community Capitalism, University of North Carolina at Chapel Hill, June 25, 2003.

⁵ Raphael W. Bostic, Kathleen C. Engel, Patricia A. McCoy, Anthony Pennington-Cross, Susan M. Wachter, *State and Local Anti-Predatory Laws: The Effect of Legal Enforcement Mechanisms*, August 7, 2007, via <http://ssrn.com/abstract=1005423>.

⁶ The Joint Center for Housing Studies at Harvard University, *The 25th Anniversary of the Community Reinvestment Act: Access to Capitol in an Evolving Financial Services System*, March 2002; Robert Litan, Nicolas Retsinas, Eric Belsky and Susan White Haag, *The Community Reinvestment Act After Financial Modernization: A Baseline Report*, produced for the United States Department of the Treasury, April 2000; *The Performance and Profitability of CRA-Related Lending*, Report by the Board of Governors of the Federal Reserve System, July 17, 2000; Raphael Bostic and Breck Robinson, *Do CRA Agreements Influence Lending Patterns?* July 2002, available via bostic@usc.edu.

Currently state laws are unable to change the incentives in the mortgage marketplace on a national level. However, state laws are still extremely useful and effective – in many states – in providing relief to homeowners. State statutory and common law claims have been very effective tools to obtain redress for individual homeowners and protecting them from foreclosure. Preservation of these state law protections is an absolutely essential factor in our support of any federal legislation.

The lending industry has thrived in a regime in which HOEPA has served as a floor while allowing for stronger state anti-predatory law that is consistent with HOEPA. It is critical to preserve this regime. Since lending markets differ across states, state governments need the flexibility to respond to their changing and unique situations.

Assignee Liability: The bill needs one significant area of improvement however: all of those who make or fund or service predatory mortgages must be fully accountable for the abusive loans. Without that full accountability, most of the other excellent provisions of your bill will not effectuate the change you intend – and which is so vital to America’s homeowners – on the mortgage market.

All players involved in the mortgage loan must be part of the solution – just as they are now part of the problem. The industry and the secondary market all argue strenuously against assignee liability of any sort, saying that credit will dry up if the investors have to assume the costs for predatory loans. Yet the research and the evidence, elaborated on below, suggests that assignee liability provides critical consumer protections without restricting meaningful access to credit.

Full assignee liability is critical for two reasons. First, it ensures that the homeowners who are harmed by the violations in the law have full redress against the holders of their loans so that they may obtain the protections of the law. Second, it ensures that market incentives exist from the originators to the investors, for mortgage loans to be made which are sustainable for homeowners and communities. Without the pressure of potential liability, there is little cost to the investor when funding profitable, yet illegal loans. This is the dynamic which must be changed.

Ability to Repay: An ability to repay provision must be rigorous, require institutions to take into account the maximum possible interest rates on adjustable rate loans, include taxes and insurance in assessing borrower ability to repay, and consider all debts. The ability to repay provision must require documentation of income. Stated-income and low-documentation loans have been a major contributor to the foreclosure crisis since abusive lenders have been extending limited documentation loans to borrowers that clearly could not afford them. Limited documentation loans were not used because borrower income information was not available, but was used as a means to commit fraud. Your bill provides a robust ability to repay provision, which should be retained. However, it is applicable in too limited a context. We ask that it be further strengthened by adding residual income into the analysis; otherwise, low-income borrowers may meet

required debt-to-income ratios while lacking sufficient actual dollars to cover basic needs.

Provisions of the Frank-Miller-Watt Bill

Our comments respond to the bill's provisions by Title. We offer the following comments and suggestions:

Title I (Mortgage Origination)

Federal Duty of Care: A federal duty of care imposed on all mortgage originators is an important component of an anti-predatory lending bill. A requirement to act with reasonable care and good faith prohibits outright fraud and placing a borrower in a clearly inappropriate loan. A duty of care requires that loan officers of depository institutions and brokers act as responsible professionals.

While a duty of care is desirable, we would have preferred a fiduciary duty imposed on mortgage originators. Financial penalties for breaching a fiduciary duty must be swift and severe enough to discourage irresponsible and fraudulent lending. Currently, abusive brokers engage in predatory lending because they can sell loans to secondary market investors and thereby escape financial penalties associated with predatory lending. Recent industry research documents that 43% of brokers using low documentation loans stated in a survey that borrowers could not qualify for loans under standard debt-to-income ratios. This survey result suggests that the brokers were not using reasonable care; instead they were placing borrowers in loans that confronted borrowers with too much debt. Using low documentation loans inappropriately appears to be a widespread industry practice, which must be stopped by a stringent federal care of duty standard. We hope that a fiduciary standard can be attached to the federal care of duty.

Anti-Steering: Steering borrowers qualified for a lower cost loans into high cost loans is a pervasive industry practice that robs borrowers of hard-earned equity. We applaud the Frank-Miller-Watt bill for prohibiting steering. Further, we strongly support the provision that prevents mortgage originators from receiving compensation, including yield spread premiums that vary with the terms and Annual Percentage Rate (APR) of the mortgage. Inducing brokers and loan officers to make higher interest rate loans by offering them extra compensation has contributed significantly to steering and price discrimination.

Your prohibition is essential. However, your remedy is overly limited. The remedy for steering a borrower into an overly expensive, inappropriate loan, must include at the least the homeowner's actual damages resulting from the steering. Further, the bill should clarify that any cap on damages included does not limit damages resulting from other claims relating from the same behavior.

When a borrower is steered towards a loan with an APR two or three percentage points higher than the loan for which he or she qualifies, the borrower will pay tens of thousands or hundreds of thousand dollars more in mortgage costs due to the discrimination. This represents a substantial loss of wealth, which could have been used to send a child to college or start a small business. When several residents of a minority or working class neighborhood suffer price discrimination, the neighborhood loses millions of dollars that could have been reinvested in neighborhood businesses and other institutions to build wealth.

In 2003, NCRC released a path-breaking study, entitled the *Broken Credit System*, documenting price discrimination on a national level.⁷ We found that after controlling for creditworthiness and housing characteristics, the amount of subprime refinance loans increased as the number of minorities and elderly increased in neighborhoods in ten large metropolitan areas. In addition to the NCRC report, two studies conducted by Federal Reserve economists found that subprime lending increases in minority neighborhoods after controlling for creditworthiness and housing market conditions.⁸ The Center for Responsible Lending also used HMDA data with pricing information to reach the same troubling conclusions that racial disparities remain after controlling for creditworthiness.⁹

More recently, NCRC's *Income is No Shield against Racial Differences in Lending* released in July of 2007 found that lending disparities for African-Americans were large and increased significantly as income levels increased. Middle- and upper-income (MUI) African-Americans were twice as likely or more than twice as likely to receive high-cost loans as MUI whites in 167 metropolitan statistical areas (MSAs). In contrast, LMI African-Americans were twice as likely or more than twice as likely to receive high-cost loans as LMI whites in 70 MSAs. Moreover, MUI African-Americans receive a large percentage of high-cost loans. In 159 metropolitan areas, more than 40% of the loans received by MUI African-American were high-cost loans. Hispanics also experienced increasing disparities as income levels increased. NCRC's mystery shopping supports the data analysis and has found that brokers and lending institutions steer qualified minorities to high-cost loans.

Licensing and Registration of Mortgage Originators: Licensing and registration requirements for mortgage originators will ensure that consumers can identify if a originator is a legitimate business and has met state and/or federal standards. The standards that the originators are to meet must be rigorous in that they require a deep knowledge of law and industry underwriting standards. Easily-met educational

⁷ See NCRC's *Broken Credit System* at <http://www.ncrc.org/policy/cra/documents/ncrcdiscrimstudy.pdf>

⁸ Paul S. Calem, Kevin Gillen, and Susan Wachter, *The Neighborhood Distribution of Subprime Mortgage Lending*, October 30, 2002. See also Paul S. Calem, Jonathan E. Hershaff, and Susan M. Wachter, *Neighborhood Patterns of Subprime Lending: Evidence from Disparate Cities*, in Fannie Mae Foundation's Housing Policy Debate, Volume 15, Issue 3, 2004 pp. 603-622.

⁹ Center for Responsible Lending, *Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages*, see <http://www.responsiblelending.org/issues/mortgage/reports/page.jsp?itemID=29371010>

requirements, for example, can provide a veneer of legitimacy to unscrupulous originators that possess only cursory knowledge of lending and are not dedicated to the best interests of the borrower. For licensing and registration of mortgage originators to be truly valuable to consumers, information about complaints against the originators must be publicly available as is -- unfortunately -- not explicitly provided for in your bill.

Remedies: Remedies must be sufficient to make a borrower whole, to fully compensate borrowers, and to expeditiously place borrowers in safe and responsible loans. The remedy in the Frank-Miller-Watt bill addresses originator abuses by establishing rewards equal to up to triple the indirect and direct compensation received by originators. The language should be clarified that the monetary damage is triple, not up to triple, the compensation received. Yet, this proposed reward will fall short in several instances to compensate for the full amount of harm experienced by a borrower and it will be insufficient to finance a new loan that enables a borrower to avoid foreclosure and succeed in homeownership.

Lenders who buy abusive loans from brokers should be clearly responsible for the actual damages stemming from abusive loans. This will ensure that lenders are very careful with whom they do business. As noted above, any remedy in this section also should not impede other remedies currently available.

Title II (Minimum Standards for All Mortgages)

Ability to Pay/Net Tangible Benefits: A strong ability to repay and tangible net benefit requirement is vital for a federal anti-predatory lending law. The ability to repay provision must assure rigorous underwriting for adjustable rate loans and must include a carefully chosen debt-to-income ratio as a threshold for determining affordable loans.

The ability to repay provision must take into account the maximum interest rate that can be charged during the first seven years of the loan, in the case of adjustable mortgage loans. To sustain homeownership, and preserve precious equity, the bill should require the underwriting standards for adjustable rate home loans to be: *At the time a home loan is made, the lender should ensure that the homeowner currently has the capacity to pay all housing related debt based on the maximum possible rate which could apply under the terms of the loan.*

Basing ability to repay on the fully-indexed rate, as in the Frank-Miller-Watt bill and in existing regulatory guidance, runs the risk of basing ability to repay on an artificially low rate when the LIBOR or other commonly used benchmark rates are low. If the House Financial Services Committee desires to use the fully-indexed rate, we urge the Committee to add a margin such as 200 basis points above the fully-indexed rate, which is the underwriting procedure mandated by Rep. Ellison's bill, H.R. 3081.

A presumption of an inability to repay when the debt-to-income ratio is above a certain threshold is a reasonable approach that does not preclude finding a loan unaffordable or

abusive if the debt-to-income ratio falls below the threshold rate. A presumption of an inability to repay when the debt-to-income ratio is 50% or higher has been a widely used standard, but NCRC’s experience is that this ratio may be too high. Based on our programmatic experience, a threshold ratio of 45% may be more effective in capturing abusive loans.

NCRC operates a foreclosure prevention program, the National Homeownership Sustainability Fund (NHSF), whose clients have been placed in loans beyond their ability to repay. A sample of 69 NHSF cases included calculations of the monthly housing payment-to-income ratio (front-end ratio) and the monthly total debt-to-income ratio (back-end ratio). The median front-end ratio was 35.4%. The median back-end ratio was about 50% as shown in the graph below. Standard front-end and back-end ratios for prime loans are 28% and 36%, respectively. The considerably higher ratios of the predatory loans in the NHSF sample suggest that the loans were beyond the consumers’ abilities to repay, leading to financial distress and/or bankruptcy and foreclosure.

Since the median ratio was 50% for the consumers seeking assistance from NCRC’s NHSF program, it is likely that a 50% debt-to-income ratio represents a breaking point in terms of making a loan unaffordable. Thus, we ask the Financial Services Committee to consider a slightly lower threshold ratio of 45%.

**HSF Unaffordable
Cases Loans**

Debt-to-income Ratios

	Front-end Ratio	Back-end Ratio
Average	40.77%	50.28%
Median	35.43%	49.78%

The ability to repay provision should be further strengthened by adding residual income into the analysis. It is possible for low-income borrowers to meet required debt-to-income ratios but lack sufficient actual dollars to cover other basic needs including food, transportation, and clothing.

Finally, the bill’s provisions relating to underwriting for negative amortization are important, however the underwriting in the bill should be based upon the full effect of negative amortization and failure to make principle payments.

Net Tangible Benefits: Considering the costs and terms and conditions of the previous and new loan, a refinance loan must offer a net tangible benefit for a borrower. Your bill appropriately stipulates that the costs of refinance loans do not exceed the amount of the new principal. Another important provision for a net tangible benefit standard is that refinance loans must legitimately lower costs for borrowers. The lower interest rate

must be low enough so that the savings achieved from the lower rate pays off the fees associated with the new loan in a specified time period such as four years. If the fees of the new loan are abusive, the fees drain borrower equity and it takes several years for the interest rate reduction to pay for the costs of the new fees.

Safe Harbor for Qualified Mortgages and Limitations on Securitizer Liability: The safe harbors for qualified mortgage loans appear to provide absolute immunity for assignees, and therefore offer no meaningful remedy for homeowners with such loans, even if the loans do in fact violate the substantive provisions of this bill. Complete insulation from liability is much more restrictive than the relatively new state laws modeled on HOEPA. The new state laws generally do not prevent a private right of action for an individual homeowner when a financial institution has met a safe harbor. We reiterate here the need for homeowners to be able to bring affirmative causes of actions against the holders of their loans when the loans have been in violation of federal law.

We do appreciate the additional defenses that you set out for homeowners to use when they are in foreclosure. However, it is counterproductive federal policy to permit vindication of a federal right only when a homeowner is on the brink of losing their family home. Indeed, a solid proportion of the homeowners in distress will continue to pay on completely unaffordable mortgages – out of pride, fear of hurting their credit, or because they believe it is the only moral way of behaving. These homeowners should be able to exercise the consumer protections you are providing in this new law.

It would be an unfortunate message to send to the American public that foreclosure is the only avenue for redress against a mortgage holder who has funded a loan which violates federal law. We hope you will change this message.

The bill also seeks to create and then virtually eliminates liability for the intermediate assignees that structure the loan pools. Intermediate assignees currently can be held liable under Truth in Lending, although more clarification about a consumer's right to know who they are and that they are liable would be helpful. However, the right to cure and exemption from liability eliminate almost any effect of placing the burden on this segment of the industry to redress loans. First, a securitizer can completely escape liability for any abusive loans simply by adopting a policy of buying only qualified mortgages and qualified safe harbor mortgages, executing representations and warranties with regard to such policies, and engaging in some sampling and review of sample loans.¹⁰

Adopting a set of broad policies should not render any entity 100% immune. The result is that homeowners with such loans are 100% without a remedy. Moreover, an entity that buys loans outside the safe harbors will need to cure only the loans for the comparatively few borrowers who have the resources to complain after the fact of their receipt of

¹⁰ This assumes the entity has not already escaped any accountability simply because it is an assignee and therefore can be presumed, without rebuttal, to have complied with the terms of 129B if the loan itself is a qualified mortgage or qualified safe harbor mortgage.

abusive loans. (Any entity working just within the safe harbors, or at least claiming to do so through its policies, will not even need to cure). An entity thus can shield itself simply by opening up a small department to cure the relatively few loans that will come its way, while avoiding any significant institutional changes that would be much more expensive. Essentially, the right to cure will be simply a cost of doing business. Full assignee liability for borrowers with abusive loans is the key to market change.

The introduction of securitizer liability also introduces a dual scheme for borrowers in default. By necessity, they will continue to try to work with the servicer representing the current holder/investor to find a loan modification or other arrangement in order to stay in the home. At the same time, they will now be forced to seek any other remedy from another party—the securitizer. Additionally, while the bill contemplates the securitizer buying back the loan from the pool, it is not clear the homeowner will be in a position to enforce any such agreement. Pooling and servicing agreements usually include such provisions now, and often they are not followed.

While the section on securitization indicates that rescission is available, the bill as written does not actually provide for such a remedy. Addressing this omission will also allow for the proper remedy in the section providing for a foreclosure defense.

We understand that you are responding to concerns that assignee liability will restrict lending activity. But in addition to the research on anti-predatory law that casts serious doubts on the credit restriction thesis, the best answer these concerns may be to look at previous experience with assignee liability. In particular, we urge you to examine what happened after 1975 when the Federal Trade Commission passed the *Preservation of Consumers Claims and Defenses Rule*.¹¹ That rule applies *full liability* in most circumstances to assignees of loans used to purchase goods and services. The automobile dealers and other sellers of goods, among others, argued that if the rule passed that the cost of credit would increase, credit would be more difficult to obtain, retail merchants would be hurt, financial institutions would stop purchasing consumer loans altogether, and many would be forced out of business altogether.¹² The finance companies and the banks argued that they did not want the responsibility of policing sellers and that sellers would not survive with the additional red tape, many consumers would stop paying on the loans without cause, and that the rule would interfere with free competition.¹³ However, there are no serious indications that the passage of this FTC rule had any significant impact on the availability of or cost of credit. Indeed, it appears that credit availability continued to expand since the passage of this rule.¹⁴

¹¹ 16 C.F.R. § 433, 40 Fed Reg. 53506 (Nov. 18, 1975).

¹² 40 Fed Reg. 53506, 53517 (Nov. 18, 1975).

¹³ *Id* at 53518.

¹⁴ In 1970, the total non-revolving credit in the US was approximately \$124 billion; growth continued steadily through the 1970s and by December 1980, the total non-revolving credit in the US was approximately \$297 billion. This growth continued notwithstanding the announcement and final promulgation of the holder rule. Source: Federal Reserve Statistical Release G.19 1970 through 1980.

It is untrue that if the secondary market were to have full liability the industry would stop making or funding mortgage loans. Consider the massive protections consumers have against unauthorized charges in credit card transactions: the Fair Credit Billing Act promises that creditors will take the hit for all such unauthorized charges.¹⁵ The credit card industry has not suffered from this full liability. Instead, the credit card industry has created a comprehensive system for limiting those losses. That is the same incentive that it is necessary to provide to the mortgage industry.

Defense to Foreclosure: A defense to foreclosure provision is vital. This protection is critical in all cases, but especially in jurisdictions with non-judicial foreclosure procedures, which tend to offer fewer protections to borrowers. We are appreciative of the inclusion of this provision in the bill. As we noted above, the addition of language providing the rescission remedy is essential to effectuate this provision at all.

Additionally, as we explained in the above section, the defense to foreclosure is not sufficient to protect homeowners who have been victims of violations of this new federal law. The secondary market is in the best position to stop predatory loans. If the secondary market has the incentive to insure that the loans it is buying, packaging and selling as investments are not predatory, the secondary market will figure out an efficacious way of accomplishing this.

Renters: As homeowners and investors default on their mortgages, their tenants face eviction risk, and communities face the possibility of speculators buying properties and then renting them out at a higher rate while not adequately investing in their maintenance. This cycle of eviction and disinvestment is very troubling and is appropriate for Congressional review and intervention. NCRC recommends strong protections for tenants who are in homes that are in foreclosure to ensure that they can either maintain their existing housing or have adequate time to relocate to new affordable rental housing stock. Your bill appropriately requires investors of foreclosed properties to assume the commitments in leases with renters and requires vacate notices to provide 90 days for tenants who do not have leases to move out.

Additional Standards and Requirements: We are pleased that the Frank-Miller-Watt bill is prohibiting mandatory arbitration and single premium credit insurance on all mortgages. These practices are inherently abusive and have been abandoned by major players in the financial industry. Banning these practices altogether is the next logical step. Prohibiting onerous prepayment penalties is also a critical protection since onerous prepayment penalties prevent borrowers from refinancing out of abusive loans and trap borrowers in precarious financial situations. We strongly support your provision to prohibit prepayment penalties that are applied within 90 days of introductory interest rates re-setting on ARM loans. Borrowers need sufficient time to refinance without prepayment penalties if they confront significant interest rate increases. If anything, the time period should be extended to 120 days.

¹⁵ 15 U.S.C. § 1666.

Right To Cure: We are quite concerned about the amendments to Truth in Lending Act's (TILA) correction of errors provision. The proposed changes would allow a cure after a borrower provides notification, as long as it is before institution of an action, and for any "unintentional violation." This has the effect of dramatically decreasing the need for responsibility on the part of originators and investors. The "unintentional violation" standard will always be the defense – then potentially requiring consumers to prove that the violation was intentional. This potentially places a level of proof on many individual borrowers which makes the litigation of standard Truth in Lending cases require evidence of a lender's intent. That is a gross increase in the necessary proof for both traditional TILA disclosure claims, as well as the more substantive provisions included in this bill. The effect will be to make all of the protections that much more elusive. Also, by allowing notification from a consumer to be the trigger to correct errors completely eliminates any incentive on the originators or the investors to look for and avoid such errors in the standard course of business. Instead the bill should be creating business incentives for business to establish their own internal safeguards.

Title III (High Cost Mortgages)

The Frank, Miller, and Watt bill would provide additional protections for loans defined as high-cost loans. The bill would define a high-cost loan as a loan with points and fees greater than 5% of the loan amount or an Annual Percentage Rate (APR) that was 8 percentage points greater than Treasury rates of comparable maturities.

For loans with APRs and points and fees greater than these thresholds, the bill would:

- Prohibit the financing of points and fees;
- Prohibit excessive fees for payoff information, modifications or late payments;
- Prohibit practices that increase the risk of foreclosure such as balloon payments and encouraging a borrower to default;
- Require pre-loan counseling

These added protections for high-cost loans are essential. NCRC's NHSF program frequently encounters loans in which borrowers do not suspect that the points and fees are excessive because they are financed into the loan. The excessive fees and points contribute to unaffordable loans. The NHSF program has also experienced usurious fees for payoff information and stiff balloon payments. Pre-loan counseling is essential before a borrower enters into a high-cost loan. Time after time, the NHSF program assists unsuspecting borrowers who trusted the abusive broker and loan officer and did not understand the vast array of confusing terms and conditions associated with high cost loans. The borrowers felt pressured to sign for the loans because they believed they had no alternatives. Loan counselors would provide reassurance to borrowers that they have alternatives.

The Escrow, Appraisal, and Mortgage Servicing Improvements Act of 2007

As well as prohibiting abusive lending, Congress must enact protections against abusive servicing and appraisal practices. While Rep. Kanjorski's Escrow, Appraisal, and Mortgage Servicing Improvement Act of 2007 (H.R. 3837) contains important consumer protections, new protections need to be added and certain provisions need to be enhanced.

The chief additional provision which community and consumer groups hope will be included in any mortgage servicing bill is a requirement for mandatory loss mitigation efforts before foreclosure is initiated.

Requiring reasonable efforts to avoid foreclosure and engage in loss mitigation is one critical consumer protection absent from the Kanjorski bill. NCRC and NCLC recommend that the Financial Services Committee adopt the loss mitigation procedures from Senator Reed's bill, the Homeownership Protection and Enhancement Act of 2007 or S 1386. Senator Reed's bill requires servicers to "reasonably" analyze the borrower's financial situation and to assess the feasibility of measures including forbearance, waiver or modification of loan terms and conditions, acceptance of partial payments and short sales.

Requiring reasonable efforts on the part of servicers is urgently needed since 2 million adjustable rate mortgages will have re-setting interest rates in which the initial rates will climb upward during the rest of 2007 and 2008. Current mediation efforts have been woefully lacking. Recently, Moody's reported that less than 1% of problematic subprime loans have been modified.

H.R. 3837 protects borrowers against sudden and unexpected expenses by requiring escrows for high-cost loans and loans in which borrowers have considerable debt. H.R. 3837 also appropriately requires that loan underwriting consider escrow payments when assessing borrower ability to repay the loan. NCRC's NHSF program demonstrates that a lack of escrows has contributed to delinquencies and foreclosures. Two thirds of the borrowers in a sample of loans in NCRC's NHSF program did not have escrow accounts. A number of borrowers assisted by the NHSF program experienced payment shock when they discovered that they had thousands of additional dollars in taxes and hazard insurance payments that were not covered by the loans.

Kanjorski's bill does advance protections against servicer abuses. The bill requires servicers to make efforts to contact borrowers before placing costly hazard insurance to the loan.

The force placing of property and flood insurance has led to widespread abuses in the servicing industry. Tens of thousands of homeowners are in default, with foreclosure looming, simply because of the questionable practices of force placing of insurance. There are cases where properties were force placed even when the servicer held a fully

paid up escrow account, or when the servicer had in its files multiple documents proving the existence of homeowners' insurance, or even the placement of flood insurance on property sitting on the top of a mountain! Force placing of insurance is a lucrative practice for servicers which has devastatingly serious consequences for homeowners.

The bill's requirement that servicers refrain from placing insurance when a borrower confirms verbally that she or he has hazard insurance is good. Moreover, the bill would prohibit servicers from declaring a loan in default due to a borrower's failure to obtain or pay for hazard insurance. However, as promising as these additional protections are in H.R. 3837, we urge the Financial Services Committee to absolutely ban the force placing of insurance unless the borrower has been denied property insurance for some reason other than non-payment.

A common servicer abuse is not crediting the borrower with making loan payments, often resulting in loan delinquencies. The Kanjorski bill protects against this practice by requiring the prompt crediting of borrower payments. The bill also requires prompt responses to pay-off requests and prompt refunds of escrow amounts on payoff.

Importantly, H.R. 3837 creates an unfair and deceptive practices standard designed to protect consumers from fraudulent appraisals. However, without a private right of action, this protection is quite limited. Industry survey research reports that 90 percent of appraisers believe that they have been pressured to inflate their property valuation estimates. Appraisal fraud has contributed to the mortgage meltdown as lenders stretch to put borrowers into loans for homes with inflated property values. H.R. 3837 would prohibit the intimidation, influencing, or bribing of an appraiser when the appraiser is estimating property values. The bill's unfair and deceptive practices standard would be significantly strengthened, however, if lenders were held liable for fraudulent appraisals, and homeowners had a clear right of action under the bill to sue the appraisers.

Conclusion

Some observers will caution legislative and regulatory restraint, claiming that economic cycles are inevitable and that the market will wring out the worst excesses of abusive lending. While economic cycles occur, the extent of dangerous lending suggests that fundamental market failure is occurring that cannot be corrected by the market itself. Economists assert that market outcomes will be inefficient when economic actors fail to internalize the negative externalities of their actions. In other words, the mortgage meltdown was caused when industry participants did not internalize the harms of their actions because they did not suffer financial penalties commensurate with the harms. Brokers and loan officers did not suffer financially when they issued predatory loans because they sold their loans to the secondary market. Secondary market investors did not suffer financially either because they developed sophisticated means to diversify risk.

In this context, fiduciary duty imposed on originators and assignee liability are critical mechanisms to provide financial incentives for industry actors to refrain from predatory

lending. We therefore urge the House Financial Services Committee to adopt fiduciary duty and full assignee liability.

While asking that the Committee adopt full assignee liability, we applaud Representatives Frank, Miller, and Watt for not preempting state law and for building in a number of vital protections in the bill. Full assignee liability and no preemption of state law would work together to ensure that the robust protections established by the bill can be enforced. The bill's ability to repay provision is a good standard that should be bolstered by adding an analysis of residual income and requiring consideration of the maximum possible rate in the case of ARM loans. Other important provisions of the bill include the anti-steering provision; prohibitions on onerous prepayment penalties, single-premium credit insurance, and mandatory arbitration for all mortgages; prohibitions on financing fees for high-cost mortgages; counseling requirements for high-cost mortgages; and protections for renters residing in foreclosed properties.

We also hope that the House Financial Services Committee attaches H.R. 3837 to the Mortgage Reform and Anti-Predatory Lending Act of 2007. H.R. 3837 requires escrows for high-cost mortgages and mortgages with large debt loads. Importantly, the bill addresses force placed insurance and appraisal fraud; we hope the Committee considers our recommendations for strengthening these provisions.

Homeownership remains the only or primary source of wealth for most Americans. Protecting families and communities from the scourge of predatory lending must be one of the most important priorities of Congress. Predatory lending devastates entire communities, from low-income to middle-class neighborhoods. Abusive lending is now even impacting the global economy. Congress can no longer rely on prodding the regulators and the industry to adopt more guidelines and best practices. A strong national law is needed that will provide comprehensive consumer protections and deter abusive lenders by providing swift financial penalties for predatory lending.