



How the National Home Equity Mortgage Association Distorts the Impact of New Jersey's Home Ownership Security Act of 2002

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Get your facts first, and then you can distort them as much as you please. Facts are stubborn, but statistics are more pliable.

Mark Twain

The National Home Equity Mortgage Association report by Professor Richard DeMong of the University of Virginia asserts that the New Jersey mortgage market decreased as a result of the state's anti-predatory lending law, which became effective the last week of November 2003. The Center for Responsible Lending, which has seen such industry-sponsored studies in virtually all states that have attempted to rein in predatory lending, finds that the report's claims do not withstand objective scrutiny.

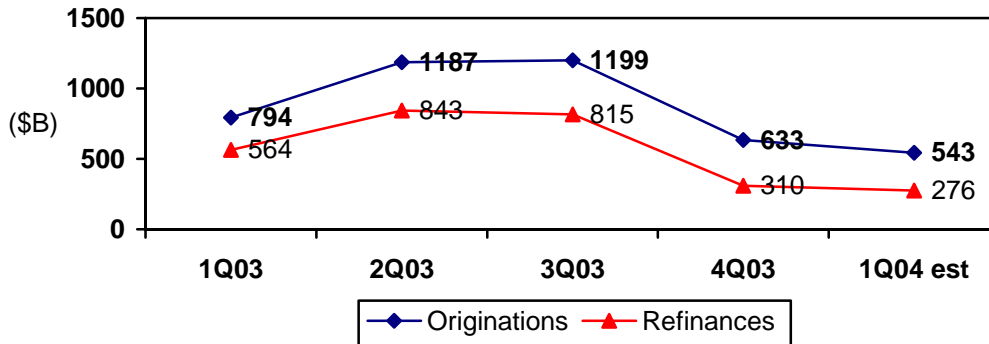
In particular, the NHEMA report ignores the fact that the entire mortgage market declined significantly at the end of 2003, as higher interest rates reduced refinances from record high levels in 2nd and 3rd quarter 2003. The report also evaluated an exceptionally small "slice" of New Jersey's mortgage activity, as reported by only 2% of active NJ lenders, and for only two months following the law's enactment. Further, the report neglects to consider other market developments that most certainly influenced reported results—the two most significant being (1) market disruption caused by confusion about Standard & Poor's policies for rating securities with cash-out refinance and home improvement loans, and (2) extensive lobbying by NHEMA and mortgage brokers (not doubt many survey respondents) to gut the NJ law.

While the NHEMA report drastically overstates the impact of the NJ law on subprime originations, experience in other states with anti-predatory lending laws shows that when loans with abusive terms are eliminated, some decline in subprime originations may occur. However, studies show that this decline does not increase the cost of subprime credit or reduce access to credit for higher-risk borrowers. The laws do, however, save consumers millions of dollars in home equity. In New Jersey, we estimate consumers will save over \$500 million as a result of the NJ Home Ownership Security Act. By anyone's definition, that is true success.

The Center for Responsible Lending has identified the following flaws and omissions in the NHEMA report.

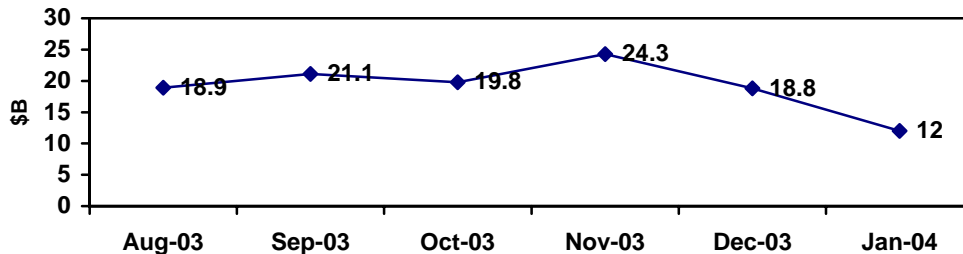
1. The drop in NJ lending cited in the study tracks the drop in production across the entire mortgage market during 4th quarter 2003 and 1st quarter 2004.

US mortgage originations dropped 53% from 3rd to 4th quarter 2003-- and refinances dropped 72%



Source: Mortgage Bankers Association

Subprime volume (securitizations) dropped as well



Source: Inside B&C Lending

2. Standard & Poor's changed its policy on rating securities with cash-out refinances and home improvement loans just before the NJ law went into effect in late November. This caused significant lender confusion until its new policies were properly understood by the market.

Lenders and investors were able to accurately adjust to the law after the NJ Department of Banking and Insurance and the state's Attorney General issued new guidance, but this may have reduced mortgage activity for a limited period.

3. The NHEMA report's methodology is seriously flawed and its conclusions are incomplete and skewed by political considerations.

Less than 2% of New Jersey's 1,500 active licensed mortgage lenders were surveyed, and almost half of the respondents could NOT cite a primary reason for their drop in lending volume.

The NHEMA report incorrectly concludes that differences between loan volumes in New Jersey and Pennsylvania can be uniformly attributed to a lasting effect of the NJ law. Such an assumption is unreliable. In addition to the limitations of comparing NJ to only one other state, the data risks substantial bias in that NJ-based lenders might well have simply shifted focus to loans in nearby Pennsylvania as the market adjusted to the new law—an effect that would at once artificially elevate Pennsylvania lending and depress estimates of NJ home lending.

The study effectively covered two months – December and January – during which NHEMA and mortgage brokers were aggressively lobbying to amend the New Jersey law. There should be little doubt that this context affected responses to survey questions.

The cited lending “decline” also includes previously-subprime borrowers who may have been bumped up into prime mortgages as a result of the NJ law. Since 83% of all subprime borrowers have “A-minus” credit or better, it is reasonable to assume that some percentage of these borrowers are now getting the prime loans they deserve.

According to the NJ Department of Banking and Insurance, applications for mortgage lending licenses in New Jersey have increased dramatically since the law's passage.

4. The report ignores the savings (\$295-563 million) NJ consumers will realize as a result of a reduction in predatory loan terms under the Home Ownership Security Act.

According to the Center for Responsible Lending's 2001 study, the potential savings to NJ consumers from anti-predatory lending legislation was estimated at \$295 million.¹ This is a conservative estimate of today's savings for consumers, since the subprime market grew 191% from 2001 to 2003.² Based on this rate of growth, the total savings to NJ consumers today could be as much as \$563 million.

About the Center for Responsible Lending

The Center for Responsible Lending is dedicated to protecting home ownership and family wealth by working to eliminate abusive financial practices. The CRL is a national nonprofit, nonpartisan research and policy organization that promotes responsible lending practices and access to fair terms of credit for low-wealth families. For additional information, please visit our website at www.responsiblelending.org or call us at **919-313-8500 / 202-349-1850**

¹ Eric Stein, Coalition for Responsible Lending, *Quantifying the Economic Cost of Predatory Lending* (2001), p 18. Available at <http://www.responsiblelending.org/pdfs/Quant10-01.PDF>

² Inside B&C Lending reported subprime origination amounts: 2001- \$173B, 2002- \$213B, 2003-\$332B