

The current epidemic of subprime foreclosures is severe and widespread. The primary victims are hard-working families who, instead of gaining the benefits of homeownership, are struggling to keep their home. However, in spite of these realities, certain myths persist:

***Myth: Adopting new laws and regulations to stop abusive lending practices will end up restricting credit and hurting the very people subprime loans are intended to help.***

**Fact:** Bad lending practices, not good underwriting practices, restrict credit. The credit crunch is a consequence of the lack of adequate regulation and the reckless lending that followed. If subprime lenders had been subject to reasonable rules—the kind of rules that responsible mortgage lenders have always followed—we wouldn't have the problems we're seeing today. Sound laws bolster market health by restoring public confidence and promoting sustainable homeownership.

***Myth: The subprime market is correcting itself, weeding out the bad players, and penalizing those who engage in unfair, deceptive practices.***

**Fact:** Market forces are not correcting the situation. The truth is, the subprime mortgage market as currently structured doesn't have adequate incentives to change its practices. As long as the subprime market continues running without adequate rules, brokers and lenders will continue to make any type of loan that Wall Street will buy. In fact, a recent market analysis by an investment management firm noted, "We find little difference between the salient risk characteristics of subprime loans originated in 2007 and 2006,<sup>1</sup> and advertisements for dangerous loan products still abound. See, for example, <http://redtape.msnbc.com/2007/09/type-goes-here.html#posts>

***Myth: Unemployment and other economic problems are the main reason borrowers are becoming delinquent and facing foreclosure in record numbers, not abusive loan terms.***

**Fact:** Data shows that the severity of the current foreclosure problem is due to abusive loan terms, not simply economic forces. The 2nd Quarter National Delinquency Survey, recently released by the Mortgage Bankers Association (MBA), shows that foreclosures on all types of loans have increased, but, as expected, that the increase in foreclosures in the subprime market is most severe. New foreclosures on subprime adjustable-rate loans in the second quarter 2007 are 90% higher than the same time last year, compared with a 23% increase on prime fixed-rate loans. While local economic conditions do matter, subprime loans typically include features, such as prepayment penalties, that are well known to increase the rate of foreclosure.

***Myth: Clear disclosures on loan documents would solve the problems in the subprime market.***

**Fact:** It is a fallacy that borrowers consciously choose and accept the loan terms they get. Most terms on a standard mortgage contract are buried in pre-printed loan documents and are dictated by the lender, not negotiated by consumers. What's more, by the time buyers see the disclosures, they likely have nowhere else to live but the new home.

As former Mortgage Bankers Association president, Rob Couch, explained, “Consumers rarely use these forms and disclosures to compare prices or identify the terms of the transaction because, quite simply, they cannot understand what they read nor what they sign. In addition, the mandated forms lack reliable cost figures, a fact that impedes prospective borrowers from ascertaining true total cost.”

Brokers and lenders are already required to provide a mortgage borrower with a “good faith estimate” (GFE) of closing costs that supposedly must bear a reasonable resemblance to actual charges. Yet there no liability if the GFE is inaccurate or incomplete, or even not provided at all. Recent efforts by the U.S. Department of Housing and Urban Development to strengthen GFE disclosure accuracy were defeated by industry trade groups.

More disclosures as part of an already confusing and paper-heavy mortgage settlement process will not correct the problem.

***Myth: Predatory lending legislation with stronger lending rules will make it harder for homeowners in trouble to refinance, which will lead to additional foreclosures.***

**Fact:** Homeowners in trouble will not be better off if they refinance into new unaffordable and abusive loans. If lenders can continue to make the same loans that caused the problem to begin with, another unaffordable refinance will simply compound the problem. The truth is, most homeowners who refinance are likely to lose even more equity – or go even further under water – due to refinancing fees and costs, especially if there’s no requirement that the loan provide a net benefit to the borrower.

***Myth: Imposing “subjective” legal standards (such as reasonableness or appropriateness) on mortgage originators will negatively impact credit.***

**Fact:** The mortgage lending industry has a long history of operating under broad underwriting and regulatory standards that require the exercise of good judgment and common sense. Anti-predatory lending laws typically include a combination of bright-line rules and flexible standards. While bright lines are useful for setting parameters where certain lending practices are unacceptable, in some cases, these more rigid rules can be either overbroad or too limited in addressing lending abuses. Flexible standards are less likely to become obsolete as industry practices and products adapt and change.

***Myth: A federal standard that permits the states to pass stronger lending protections would be prohibitively expensive for the industry and stunt market growth.***

**Fact:** The subprime market grew and flourished—increasing from \$35 billion in 1994 to \$640 billion in 2006—during a period when more than 30 states passed predatory lending laws. Furthermore, lenders have been able to reduce the costs of compliance dramatically by using automated compliance systems. According to a 2005 report by the Center on Responsible Lending, compliance adds only about \$1 to the cost of making each mortgage loan. Since many other lending related issues are regulated at the state level, including contract law, foreclosure rules and processes, and broker licensing, a national standard for a federal predatory lending law would not change the need to adhere to individual state laws.

***Myth: Advocates say that they want to increase homeownership, especially among minority borrowers, yet this bill will prevent lending to the very communities that they say they're trying to help.***

**Fact:** Placing people into loans they cannot afford helps no one. We value homeownership because it creates an opportunity for accumulating wealth and stabilizing neighborhoods. As the current foreclosure crisis starkly demonstrates, reckless lending practices ultimately drain the wealth of both families and communities. While it is crucial that anyone who is qualified to buy a home can do so regardless of their race or the location of the home, no one has an interest in increasing the number of people who buy homes that they cannot afford. In fact, a foreclosure typically delays re-entry into homeownership by a decade or more.

By ensuring that families have the ability to pay their mortgages, this bill will create more homeowners, not just more homebuyers. Moreover, by preventing mortgage loan originators from steering minorities into more expensive loans than those for which they qualify based on objective underwriting criteria, this bill will make homeownership more affordable for minority homebuyers, not less.

***Myth: Consumers deserve a full range of choices of mortgage loan products.***

**Fact:** The risky loans sold in recent years were not responding to borrower demand; rather, they were created to maximize short-term industry profits, and they were aggressively push-marketed to consumers. As Alan Greenspan recently told Newsweek, "The big demand was not so much on the part of the borrowers as it was on the part of the suppliers who were giving loans which really most people couldn't afford."<sup>ii</sup>

In a civil society, government has no higher duty than to promote the general welfare of its citizens. As a nation, we provide legal safeguards for a wide variety of products and trade practices to ensure safety and fairness. Given that a home purchase is typically the largest and most important investment of a person's life and is, for the vast majority of Americans, the primary repository of the family's wealth, it would be foolish if we did not provide equally effective safeguards for mortgage-related products and practices.

***Myth: Most people facing foreclosure are investors or speculators who were trying to make a quick buck by "flipping" homes in a rising real estate market and have been caught in the downturn.***

**Fact:** Most foreclosures—88 percent—are suffered by families living in their primary residence. While it's always been true that the rate of foreclosures on investor-owned properties is higher than on primary residences, actual foreclosures are overwhelmingly dominated by families who live in their homes.

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<sup>i</sup> FBR Capital Markets, note 14 at p. 2.

<sup>ii</sup> From "The Oracle Reveals All," Newsweek, pp. 32, 33 (Sept. 24, 2007).