



The Option One Bill¹ Would Roll Back Protections and Allow Abusive Lending Practices to Continue

BACKGROUND

Option One, a major subprime lender owned by H&R Block, and some other subprime lenders have been pushing for a “compromise bill” with consumer advocates on federal mortgage lending legislation. Unfortunately, this “compromise” would be devastating for homeowners and undercuts nearly a decade of progress in preventing predatory lending.

- The Option One bill would **wipe out strong state laws** that prevent predatory lending and save homeowners millions of dollars every year.
- The Option One bill would even **weaken some aspects of current federal law**.
- The Option One bill **is significantly weaker than North Carolina’s state anti-predatory lending law** and laws in many other states.
- **The true “North Carolina Plus” model is found in the Miller-Watt-Frank bill, which already has more than 60 co-sponsors.** The Miller-Watt-Frank bill takes the best practices from proven, effective state predatory lending laws, while allowing states to protect their citizens from the constantly changing landscape of abusive lending practices.

CONCERNS WITH THE OPTION ONE BILL

The Option One bill would fail to cover egregious lending abuses. Because of serious loopholes in defining which loans are covered (i.e., “high-cost” loans), protections would apply to very few subprime home loans.

- For example, under the bill, a \$100,000 mortgage could have a \$5000 origination fee, a \$3000 prepayment penalty, and a \$2000 kickback to the broker (\$10,000 in fees; 10% of the loan amount), and still not receive any of the high-cost loan protections.
- If the same mortgage came from a broker and did not include a prepayment penalty, the kickback to the broker could be unlimited, and the loan would still not receive protection.
- Both of these loans would receive protections under Miller-Watt-Frank, the North Carolina law, and laws in many other states.

The Option One bill fails to protect against well-known abuses that strip hard-earned wealth from homeowners.

- **Prepayment Penalties:** While North Carolina bans prepayment penalties on all home loans under \$150,000, the Option One bill would let lenders charge prepayment penalties for the first 36 months of the loan. Prepayment penalties trap borrowers in subprime loans—their cost makes it too expensive to refinance into lower-cost loan or forces the borrower to sacrifice significant equity in order to move into a lower-cost home loan.

¹ Draft of the bill is dated 3/22/2006.

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- **Yield Spread Premiums and Flipping:** Unlike the Miller-Watt-Frank proposal, the bill disregards lender kickbacks to brokers for steering borrowers into expensive loans and fails to take meaningful steps to reduce abusive loan refinances.
- **Steering:** The bill includes an ineffective provision on steering. Because its definition of “high-cost” has so many exclusions, provisions that purport to address steering and other abuses will almost never apply.

The Option One bill weakens enforcement and remedies against predatory lending.

- While most subprime lenders have announced that they will not use mandatory arbitration clauses on any home loans, this bill prohibits mandatory arbitration only on the few loans that would be considered high-cost. This is a step back from current industry best practices. Miller-Watt-Frank bill would codify the existing industry best practice by prohibiting mandatory arbitration on all home loans.
- The bill severely limits borrower remedies by diluting current federal law on liability once a loan is sold to investors – as are most subprime loans -- and weakening enforcement provisions in current federal law. The result: Homeowners will essentially be barred from protecting their homes from predatory lenders.

The Option One bill includes sweeping preemption of state laws.

- Rather than permitting states to supplement federal protections, the bill would eliminate existing state protections and prohibit states from addressing future mortgage lending abuses. Freezing the law will only invite new abusive lending practices. Given the difficulty of changing federal law (the last predatory lending legislation passed in 1994), a preemptive federal law would represent a great victory for unscrupulous lenders who prey upon homeowners.
- The bill also preempts state law for fly-by-night mortgage brokers and mortgage companies that are unregulated and unsupervised at the federal level. This preemption ties the hands of the states to set standards and curb abuses by actors who are regulated by the states. This flies in the face of common sense and would prevent action by the authorities closest to their communities who can most effectively enforce the law.