Subcommittee on Financial Institutions and Consumer Credit
Subcommittee on Housing and Community Opportunity
Joint Hearing Entitled "Legislative Solutions to Abusive Mortgage Lending Practices"

May 24, 2005

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Chairman Bachus and Chairman Ney, Ranking Member Sanders, and Ranking Member Waters, thank you for the opportunity to testify today on legislative solutions to address abusive mortgage lending practices.

I am the CEO of Self-Help Credit Union and the Center for Responsible Lending (CRL). Self-Help is a community development lender that creates ownership opportunities for low-income and minority families through homeownership and small business financing. Because we lend to people in underserved communities, such as minorities and immigrants, during the past 25 years we have learned a great deal about the subprime market where people with less than perfect credit borrow. Self-Help has provided more than $3.9 billion in financing to almost 45,000 homeowners, small business owners and nonprofits across the nation.

Unfortunately, we also have witnessed first-hand the harm done to borrowers when lenders are irresponsible and unethical. While we and many other community development organizations are focused on helping borrowers build wealth through homeownership, some unscrupulous lenders are siphoning that wealth away.

As the subprime mortgage market has boomed, climbing from $35 billion to $530 billion in the decade through last year, so too have abusive loans, which are concentrated in this market. This explosive market growth has occurred at a time when many states have passed stronger laws against predatory mortgage lending. Appendix A includes more details about the remarkable growth of the subprime market, including the high growth of subprime mortgage lending in states with anti-predatory lending laws. This fact sheet illustrates very clearly that is possible for subprime lenders to prosper while also complying with lending laws implemented on a state level.

In response to the increase in abusive lending practices, Self-Help formed an affiliate, the Center for Responsible Lending (CRL). CRL is a nonprofit, nonpartisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. Both Self-Help and CRL are based in Durham, North Carolina, a state where some of the nation’s largest lenders have headquarters.

During the next five years, approximately 15 million homebuyers and homeowners will receive loans in the subprime mortgage market. The policies you are considering today will determine whether these loans help the working class and minority borrowers who use the subprime mortgage market to improve their economic status or whether they get pushed farther behind. Today, as you listen to different perspectives and consider the best policies to address predatory mortgage lending, I hope you will keep in mind this undisputed fact: Subprime mortgage loans go into foreclosure 10 times more often than mortgages in the prime market.

In our view, any new policies on predatory mortgage lending should be considered in light of these fundamental questions:

- Will homeownership continue to be a way to build wealth, or will it become an opportunity for unscrupulous lenders to steal owners' hard-earned equity?

- Will subprime lending encourage sustainable homeownership, or will we see families and entire communities destroyed through foreclosures?

- Will such policies perpetuate huge disparities in wealth between white Americans and people of color, or will they ensure that homeownership continues to be a wealth-building opportunity for <u>all</u> Americans?

- Will such policies turn back progress by reauthorizing predatory lending practices that have been formally banned in best practices announcements by most major lenders and explicitly outlawed by some states?

In my testimony, I'd like to emphasize the following three points:

1. **Predatory mortgage lending remains a very real threat to citizens who already struggle economically.**

   - Abusive lending practices cause significant numbers of foreclosures, and

   - They have a disparate impact on our most vulnerable citizens, such as the elderly and people in communities of color.

2. **The states have developed and refined workable solutions to predatory mortgage lending that reduce abusive loans and allow <u>responsible</u> subprime credit to remain affordable and abundant.**

   - In North Carolina, which has the longest experience with a state anti-predatory lending law, the subprime mortgage market has experienced similar growth as neighboring states. North Carolina borrowers in the subprime market are enjoying similar access to credit at a similar cost, with only one significant difference: They are not subjected to costly prepayment penalties and other abusive terms.

3. **A federal law, no matter how carefully crafted, will never be adequate to address predatory lending in all parts of the country. However, an effective**

bill would contain comprehensive and meaningful protections, such as a definition of "high-cost loan" that captures all major loan fees.

- The proposed Ney-Kanjorski bill (H.R. 1295) fails to provide meaningful protections against predatory lending. It replaces effective state protections with a weak federal standard, excludes many typical predatory loans from protections, and is significantly weaker than best practices approved by most major subprime lenders.

- The proposed Miller-Watt bill (H.R. 1182), based on the proven success of the North Carolina law, offers strong consumer protections while supporting a healthy subprime mortgage market.

- Federal preemption of state anti-predatory lending laws would be misguided, as any federal standards should supplement, not replace, existing state efforts.

1. The Threat of Predatory Lending

Abusive mortgage lending almost always occurs in the subprime market – home loans for people with impaired or limited credit histories. To account for less-than-perfect credit, responsible subprime lenders charge somewhat higher interest rates to compensate for the increased risk associated with these loans. Subprime home loans are typically packaged immediately and sold to investors in the secondary market, which in turn provides subprime lenders with a source of capital with which to make additional loans.

The subprime market is largely a market for refinance loans: approximately three-quarters of subprime originations in 2001 and 2002 were refinances.[1] Unfortunately, the combination of tremendous growth in subprime lending, the lack of standards for this rapidly growing industry, and subprime borrowers' frequent lack of financial sophistication has created an environment ripe for abuse.

In 2001, CRL estimated that predatory mortgage lending practices cost homeowners $9.1 billion each year. This figure likely underestimates today's cost, because the subprime market has expanded significantly. According to SMR Research, subprime mortgages are now the fastest growing sector of consumer finance.[2] Between 2003 and 2004, subprime mortgage volume increased from $332 billion up to $530 billion, while the issuance of subprime securities rose from $202 billion to $401 billion.[3] In 1994, by contrast, subprime lenders securitized just $10 billion worth of home equity loans.[4]

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[1] SMR Research Corp., Analysis of 2001 and 2002 Home Mortgage Disclosure Act data.
[2] SMR Research Corp., *Subprime Mortgage Loans 2005*, at http://www.smrresearch.com/sml2005.html.
[3] *The 2005 Mortgage Market Statistical Annuals*, Volume 1 – The Primary Market and Volume 2 – The Secondary Market, Inside Mortgage Finance Publications, Inc. (2005).
[4] Cathy Lesser Mansfield, *The Road to Subprime 'HEL' was Paved with Good Congressional Intentions: Usury Deregulation and the Subprime Home Equity Market*, S.C. Law Review, v51, n3, 473–587 (2000).

As a result of the growth of subprime lending, the pressing issue today is not availability of credit in America's communities. Rather, the debate has shifted to the terms on which credit is offered.

A. Predatory lending abuses have created a crisis for American families.
A typical borrower in the subprime mortgage market is "house-rich," but "cash-poor." Many are senior citizens on fixed, limited incomes. Others are families who struggle daily to maintain a tentative grasp on the lower rungs of the middle class. They are hard-working people with little wealth but with big dreams of a better future.

At Self-Help, we have witnessed the tragic consequences of predatory lending. Many of the most egregious cases involve senior citizens who were persuaded to refinance their home multiple times in a practice called "flipping." All too often, these citizens end up losing homes they had previously owned free and clear. In Iowa, the state Attorney General is aware of at least three instances in which predatory mortgage lending was a major contributing factor to suicides.

For most families, the equity owned in their home represents their greatest source of savings. When they lose that equity through an abusive refinance loan, they often lose their best chance to send children to college, start small businesses, weather crises such as unanticipated medical expenses, and enjoy some measure of security in old age. Even worse, because predatory lending can lead to increased foreclosures across a neighborhood, abuses can systematically destroy entire communities.

For quick reference, we provide an abbreviated description of common abuses in the subprime mortgage market:

> <u>Excessive fees</u>: Points and fees are costs not directly reflected in interest rates. Because these costs can be financed as part of the loan, the borrower does not pay in cash, and the real costs of the loan are easy to disguise or downplay. On predatory loans, fees totaling more than 5 percent of the loan amount are common.
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> <u>Abusive prepayment penalties</u>: These penalties for early pay-off can harm borrowers in the subprime market by draining equity or trapping them in expensive loans. The cost of a penalty – often six months' interest -- may force a borrower to remain in an unnecessarily high-cost loan. In the prime market, only about two percent of home loans carry prepayment penalties, while up to 80 percent of subprime mortgages come with a prepayment penalty.[5]

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[5] See Standard & Poor's, *NIMS Analysis: Valuing Prepayment Penalty Fee Income*, at http://www.standardandpoors.com (January 3, 2001); see also Standard & Poor's, *Legal Criteria Reaffirmed for the Securitization of Prepayment Penalties*, at http: //www.standardandpoors.com (May 29, 2002); *Prepayment penalties prove their merit for subprime and 'A' market lenders*, at http://www.standardandpoors.com (January 3, 2001); see also *Freddie offers a new A-, prepay-penalty program*, Mortgage Marketplace, at 1-2 (May 24, 1999); see also Joshua Brockman, *Fannie revamps prepayment-penalty bonds*, American Banker at 16 (July 20, 1999).

Kickbacks to brokers: When brokers deliver a loan with an inflated interest rate (i.e., higher than the rate acceptable to the lender), the lender often pays a “yield spread premium” – a kickback for a costly loan.

Loan “flipping”: A lender “flips” a borrower by refinancing a loan to generate fee income without providing any net tangible benefit to the borrower.

Mandatory arbitration clauses: Lenders frequently include mandatory arbitration clauses in a home loan to prevent borrowers from seeking legal remedies in a court of law if they have been wronged. These clauses also insulate unfair and deceptive practices from fair and public review.

These abuses become very real to families who fall victim to them. The story of Ira Cheatham, a 73-year-old retired veteran of the Korean War, provides just one example of the real life impact of predatory lending. He and his wife had lived in a predominantly minority neighborhood of Portland Oregon for 21 years. By 2002, they had nearly paid off their mortgage.

Then in December of 2001, the Cheathams received a live check in the mail from Wells Fargo Financial for a little over $1,000. Ira had just retired, and the couple’s retirement income had ended up being lower than they had expected, so they cashed the check, and in the process took out a very high interest loan.

Within a week or two after cashing the check, Ira and Hazel got a call from Wells Fargo, urging the elderly couple to consolidate this loan, along with all their credit card debt into a single mortgage. According to Mr. Cheatham, he had excellent credit and Wells Fargo promised that the couple would receive an interest rate between five and six percent, which would reduce their monthly mortgage payments. Based upon these promises, the couple agreed to refinance their mortgage.

When the loan papers were presented the Cheathams, the loan actually contained an interest rate of 9.9 percent and an annual percentage rate of 11.8 percent. Moreover, the Cheatham’s loan contained 10 "discount points" ($15,289) that were financed into the loan, inflating the loan amount and stripping away the Cheatham’s equity. Under the new loan, the Cheatham’s monthly mortgage payments increased to $1,655, amounting to roughly 57 percent of the Cheatham’s monthly income.

The Cheatham’s problems were magnified because this predatory loan contained a substantial prepayment penalty. The couple was required to either remain locked in a high-interest mortgage or pay a large prepayment penalty. Eventually, the Cheathams decided to refinance their mortgage with another lender to obtain the five percent interest rate for which they qualified and which they had been promised. However, the couple was required to pay a prepayment penalty of approximately $7,500 to Wells Fargo in order to escape their predatory loan.

This is only one example of far too many abusive transactions that come to our attention. Again, I want to emphasize that the federal policies you are considering today will determine whether such lending practices continue, or whether families will actually benefit from the credit they receive.

B. The High Rate of Foreclosures in the Subprime Market

Because predatory lenders are known to target certain neighborhoods, the odds are good that one victim of predatory lending lives down the street or around the corner from another. In this way, whole communities are affected, especially when foreclosures become rampant. For instance, according to the Mortgage Bankers Association, at the end of the fourth quarter of 2004, 10.45% of subprime loans in Ohio were in foreclosure, the highest rate in the country.

<u>Research is establishing a strong connection between abusive subprime mortgages and home foreclosures</u>. For example, evidence from the Woodstock Institute in Chicago shows that recent increases in foreclosures have been fueled in large part by increases in subprime home lending in the last half of the 1990s. In addition to finding subprime lending "the dominant driver" of increases in foreclosures, the authors note that the impact of foreclosures is most keenly felt in "modest-income neighborhoods where foreclosures more often lead to abandonment and blight" and that those costs are "borne by entire communities, not just by the lender or borrower."[6] According to the study, from 1995 to 2002, foreclosure starts in the Chicago area grew 238 percent.[7]

More recently, the connection between predatory lending terms, prepayment penalties and foreclosures was confirmed by a study conducted by the Center for Community Capitalism at the University of North Carolina at Chapel Hill. The study found that the inclusion of prepayment penalties and balloon payments[8] in refinanced subprime mortgages dramatically increase the risk of foreclosure, even after controlling for credit scores, loan terms, interest rates, and economic factors. Specifically, after examining a large, nationwide sample of subprime loans, the UNC study found:

- Fully 20 percent of 30-year subprime refinance loans originated in 1998, 1999, and 2000 had entered foreclosure by the end of 2003.
- Refinance loans with extended prepayment penalties (three years or more) and balloon payments are much more likely to foreclose – by 20 percent and 50 percent, respectively – than refinance loans without such features. This is true after controlling for other relevant variables such as FICO scores, LTV, etc.

This study represents the first of its kind to establish that abusive loan terms are directly related to foreclosure.

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[6] Immergluck and Smith, Risky Business -- An Econometric Analysis of the Relationship Between Subprime Lending and Neighborhood Foreclosures, Woodstock Institute, March 2004.
[7] See Immergluck and Smith, note 5.
[8] A "balloon payment" is a large, lump-sum payment that is due at the end of a series of smaller periodic payments. Such payments may essentially force vulnerable borrowers to accept high-cost refinances or lose their home.

While we might expect some elevation of default rates in the subprime market, the statistics documenting Self-Help's experience with lending to borrowers with blemished credit and low incomes (including our loss rate of no more than 0.5 percent per year) suggest that foreclosures in the subprime market cannot be explained solely by borrower behavior. Rather, we must recognize that abusive lending pushes borrowers past their limits and imposes extensive costs in our communities.

C. The Disproportionate Impact of Predatory Lending

Because subprime loans go disproportionately to minority borrowers, predatory mortgage lending has a particularly harsh impact on people of color. The effect is that predatory lending perpetuates the wealth gap between whites and people of color, which is well established and growing. According to a recent report by the Pew Hispanic Center, in 2002 African Americans and Latinos had a median net worth of $5,998 and $7,932, respectively, compared to white Americans' median net worth of $88,651.[9] In other words, white families' median net worth is about 11 times greater than Latinos' and nearly 15 times greater than the median net worth held by African Americans, up from a ten to one disparity as reflected in the 1990 census.

Among African American and Latino homeowners, the median family in each group held 88 percent of its total wealth in the form of home equity. These figures illustrate that home equity is a critical factor in determining economic progress among these populations.

These facts are relevant to this discussion because predatory lending puts that wealth at risk-- African-Americans and Latinos are overrepresented in the subprime mortgage market and have borne the brunt of abusive practices. According to a 2004 study published by ACORN, African-Americans were 3.6 times as likely as whites to receive a home purchase loan from a subprime lender and 4.1 times as likely as whites to receive a refinance loan from a subprime lender in 2002.[10] In 2002, for both home purchase and refinance loans, Latinos were 2.5 times as likely as whites to receive a loan from a subprime lender.

Most recently, CRL research also showed that abusive subprime prepayment penalties occur disproportionately in zip codes areas with a higher concentration of minority residents. After controlling for income and other relevant factors, we found that borrowers in minority communities have a significantly greater chance of receiving a prepayment penalty.[11] Studies such as these contribute to growing evidence that predatory lending imposes proportionately higher economic burdens on the most vulnerable communities.

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[9] Rahesh Kochhar, *The Wealth of Hispanic Households 1996 – 2002*, Pew Hispanic Center (October 2004).
[10] *Separate and Unequal 2004: Predatory Lending in America*, ACORN, ACORN Housing Corp., ACORN Fair Housing (February 2004).
[11] Debbie Gruenstein Bocian and Richard Zhai, *Borrowers in Higher Minority Areas More Likely to Receive Prepayment Penalties on Subprime Loans*, Center for Responsible Lending (January 2005).

Predatory lenders are known to steer borrowers into subprime mortgages, even when the borrowers could qualify for a mainstream loan. Studies show that between 30 and 50 percent of borrowers with subprime mortgages could have qualified for loans with better terms.[12] This point is further illustrated by joint U.S. Department of Housing and Urban Development - Treasury Department research showing that borrowers in upper-income African-American neighborhoods were twice as likely as homeowners in low-income white neighborhoods to refinance with a subprime loan.[13]

2. State Laws are Working

Since the federal Home Ownership and Equity Protection Act (HOEPA) passed in 1994, the problem of abusive lending has grown worse. Unscrupulous lenders quickly found ways to circumvent the law. This situation illustrates how difficult it is for a federal law to remain current and maintain effectiveness against the creative practices of predatory lenders in different parts of the country.

In response to local surges in predatory lending activities, many states have passed predatory lending laws to supplement federal protections. North Carolina was a pioneer in this area, passing the first anti-predatory law of its kind in 1999.[14] Since then, that law has become a model for other states, while subprime mortgage lending in North Carolina has received a great deal of scrutiny. CRL estimates show that the new law saved consumers at least $100 million per year by preventing predatory loan terms that would have been expected to occur in the law's absence.[15]

More recently, the Fannie Mae Foundation published research by the University of North Carolina based on an examination of North Carolina's market before and after the anti-predatory law was implemented in 1999 and 2000. UNC found a decline in subprime refinance loans with predatory terms, and an increase in purchase subprime loans.[16] Specifically, the study noted a 72 percent drop in subprime prepayment penalties with terms of three years or longer along with a 43 percent increase in subprime home purchase loans. <u>In other words, under the North Carolina law, borrowers in the subprime</u>

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[12] Fannie Mae has estimated that 30-50% of subprime borrowers could have qualified for a loan with better terms. Freddie Mac estimates that 10–35% of subprime borrowers could have qualified, and cites a poll of 50 subprime lenders who estimate that half could have qualified for prime loans. *Id.* (*citing* Freddie Mac Special Report on Automated Underwriting (Sept. 1996) at http://www.freddiemac.com/corporate/reports/moseley/chap5.htm; *see also Half of Subprime Loans Categorized as'A' Quality*, Inside B&C Lending (June 10, 1996).

[13] Task Force on Predatory Lending, U.S. Department of Housing and Urban Development and U.S. Department of Treasury, *Curbing Predatory Home Mortgage Lending* at 48 (June 2000).

[14] It is worth noting that the bill passed with support from a strong coalition of bankers, credit unions, mortgage brokers, mortgage bankers, consumer advocates, the NAACP, AARP, and other community organizations.

[15] Keith Ernst, John Farris, Eric Stein, *North Carolina's Subprime Home Loan Market After Predatory Lending Reform,* Center for Responsible Lending (2002).

[16] Roberto G. Quercia, Michael A. Stegman, and Walter R. Davis, *Assessing the Impact of North Carolina's Predatory Lending Law*, Housing Policy Debate, Vol. 15, Issue 3, Fannie Mae Foundation (2004).

market were buying homes in record numbers while being subjected to significantly less predatory lending in the refinance market.

A. The Performance of North Carolina's Subprime Market

The lending industry continues to claim that state anti-predatory lending laws have stunted the subprime lending market and hindered access to credit. That seems highly questionable in light of the continued explosive growth of the subprime market. Nevertheless, to address issues raised by industry, CRL has updated its analysis of the performance of the subprime market in North Carolina and other key states.

Using data from the Loan Performance database,[17] CRL examined the performance of the subprime market in North Carolina as compared to neighboring states. CRL also analyzed data from other states with strong anti-predatory lending laws (New Jersey and New Mexico) versus states with weaker laws (Florida, Ohio and Pennsylvania). The latter three states were selected because they take a less comprehensive approach to predatory lending, including in the way they define a "high-cost loan."

The data show that predatory lending is down in North Carolina, but the subprime mortgage market has continued to flourish. Subprime lending in the state has experienced similar growth to neighboring states, and borrowers are receiving the same types of subprime mortgages at better prices. In fact, borrowers participating in North Carolina's subprime market are almost indistinguishable from borrowers in other states, with one exception: North Carolina subprime borrowers are rarely subjected to large prepayment penalties.

North Carolina versus Neighboring States

1. Flow of Credit

As shown in Appendix B, subprime refinance lending has grown considerably in North Carolina since the state's law became fully effective in 2000. For subprime refinances, North Carolina's growth slightly exceeded other neighboring states except Virginia, which experienced growth far ahead of the country overall. For subprime purchase loans, again North Carolina's performance was second among these states, showing a cumulative increase of 366 percent growth during the period between 1998 and 2003.

2. Cost of Credit

When Self-Help helped champion North Carolina's anti-predatory lending law in 1999, we pushed for provisions that would encourage lenders to limit fees and instead reflect credit risk through the interest rate on the loan. When the cost of credit is reflected in rate rather than fees, understanding the real cost of the loan and comparing loan options is much easier for homeowners. Further, while fees are gone forever once they are stripped from home equity, a homeowner who is in a loan with a rate that is too high can refinance. In response to provisions in the North Carolina law that discouraged high fees,

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[17] For more information describing the Loan Performance database, see Quercia and Stegman, note 15.

we anticipated a possible increase in interest rates, perhaps ranging from one-half to one percent.

However, as shown in Appendix C, the expected increase did not occur, and North Carolina's anti-predatory lending law has not adversely affected the cost of credit. Interest rates in North Carolina remain virtually indistinguishable from those of neighboring states. The same holds true for APR, based on that portion of the subprime market's Home Mortgage Disclosure Act data we have received to date. This shows that North Carolina borrowers are neither paying higher interest rates nor higher fees, and in fact suggests that borrowers were paying unnecessary fees before the law went into effect.

At the same time, borrowers in North Carolina receive loans without abusive terms. In 2003, only one percent of North Carolina borrowers had prepayment penalties of 36 months or longer on their subprime refinance loan. That figure stands in sharp contrast to states without strong laws. For example, in Tennessee, 58 percent of borrowers with refinances in the subprime market received prepayment penalties of 36 months or longer.

3. Borrowers Served by the Subprime Market

Even if credit flows had remained constant and interest rate and fees level or below those of neighboring states, we would still have cause for concern if the North Carolina market seemed to be underserving those with the fewest credit alternatives—borrowers with weaker credit, less income, or African-American and Latino borrowers that have historically had difficulty accessing credit. We are pleased to report that none of these concerns emerge from the data. For example, as shown in Appendix D, by two primary measures of creditworthiness—credit score (FICO) and loan-to-value ratio (LTV), the results for borrowers in North Carolina's subprime market are very similar to those in neighboring states.

4. Strong v. Weaker State laws

Similar results occurred in our comparison of strong and weaker state laws. Again, growth in the subprime market has been robust in states with strong laws. New Jersey, for example, continues to experience similar or lower interest rates compared to other states. In fact, interest rates and APR remain relatively constant among the states in the analysis. And again, while approximately 11 percent of subprime refinance loans in New Jersey and New Mexico had prepayment penalties of 36 months or longer in 2003, Ohio, Pennsylvania, and Florida each showed that 55 percent of their refinance loans included such prepayment penalties.

These positive results have been acknowledged by the lending industry. For example, last August a very favorable article appeared in National Mortgage News. In the article, Donald Fader, president of North Carolina Association of Mortgage Professionals, noted that the industry has continued to prosper under North Carolina's law. Mr. Fader is quoted as saying, "The membership in our organization has grown and there has been a high volume of business in the state."[18] In another instance, an analysis by a leading industry trade journal, *Inside B&C Lending*, found that top North Carolina subprime lenders "continue to offer a full array of products for borrowers in North Carolina – with little or no variation in rate" compared to other states.[19]

In addition, a Morgan Stanley & Co. survey of 280 subprime branch managers and brokers found that tougher predatory lending laws have not reduced subprime residential lending volumes. In fact, branch managers thought that changed practices in response to state laws like North Carolina's are having neutral to positive impact on volume because they make customers feel more comfortable and "lower points and less onerous prepayment penalties make the economic terms more attractive."[20]

More recent comments by state officials suggest other state laws are having similar effects. The New Jersey Department of Banking recently stated:

> Based on our experience to date, we are pleased to report that we believe that the [New Jersey anti-predatory lending] law is fulfilling its twin goals: curbing abusive practices while also ensuring that responsible forms of credit continue to be made available to all New Jerseyans. This is reflected in the fact that consumer complaints about predatory practices are down, the number of entities seeking to become licensed lenders continues to rise, and all segments of the market remain stable. We note, for example, that according to *Inside B&C Lending,* New Jersey had the eighth highest volume in subprime mortgage lending at the end of the first quarter in 2004, showing an increase of 19% from the previous year.[21]

Attorney General Patricia Madrid recently said about New Mexico's state law, "In New Mexico, nearly a year and a half after the HLPA went into effect, my office is not aware of any New Mexicans who have been unable to obtain a home loan as a result of the law's protections."

3. The Characteristics of a Meaningful and Effective Federal Bill

Recently, two bills have been introduced in the House of Representatives to replace HOEPA and which purport to provide stronger protections for consumers against predatory lending. As Congress considers these bills, we urge members to carefully scrutinize the benefits touted by sponsors and to consider each bill in light of the practical realities of predatory mortgage lending. At a minimum, CRL believes that any meaningful bill would accomplish these goals:

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[18] Jennifer Harmon, *Looking Back at the North Carolina Law's Effects*, National Mortgage News, vol. 28, no. 45 (August 9, 2004).

[19] Cite. Also, some erroneously point to an industry-sponsored study (published by the Credit Research Center) as evidence that the North Carolina law decreased access to subprime credit for low-income borrowers. However, the study has been widely criticized. Significantly, the study was based on loans originated between 1997 and June 30, 2000; however, the N.C. law did not take full effect until July 1, 2000.

[20] *Lenders Will Try to Pin Down Effects of NC Mortgage Law*, Inside B&C Lending (March 5, 2001).

[21] *Channel Check: Surprisingly Strong Subprime Growth*, Morgan Stanley - Diversified Financials (August 1, 2002).

1. Adopt a definition of "high-cost loan" that captures all major fees, so that abusive loans are included in the definition.
2. Prohibit practices that are so abusive that they are inappropriate on any home loan, such as loan flipping -- repeated refinances that provide no benefit to borrowers.
3. Provide effective protections for high-cost loans.
4. Ensure that homeowners' rights are effective by providing meaningful remedies and the ability to enforce rights when the loan is sold.
5. Allow flexibility for states to address localized and new abuses.

A. H.R. 1295, sponsored by Representatives Ney and Kanjorski

Unfortunately, the bill introduced by Representatives Robert Ney (R-OH) and Paul Kanjorski (D-PA), entitled "The Responsible Lending Act" (H.R. 1295), would achieve none of the goals of a meaningful and effective federal bill. If implemented, this proposal would fail to protect homebuyers and homeowners against irresponsible lending and, in fact, would allow predatory mortgage lending to proliferate.

Although H.R. 1295 purports to expand consumer protections, it would in fact outlaw a small minority of predatory loans. CRL strenuously objects to H.R. 1295, for the following reasons:

1. The bill fails to take a comprehensive approach to excessive points and fee*s.* The Ney-Kanjorski bill excludes almost all prepayment penalties and appears to exclude yield spread premiums from the calculation of whether a loan has points and fees at a level that triggers the protections in the Act.

- Protections for high-cost loans are only meaningful if all lender and broker compensation is included in the calculation to determine if a loan is a high-cost loan. Otherwise, unscrupulous lenders will evade the bill's scope simply by shifting compensation to these excluded fees.

- Prepayment penalties on subprime loans strip hard-earned home equity, trap borrowers in unaffordable loans, and are tied by statistical research to increased foreclosures. Under the Ney-Kanjorski proposal, penalties for paying off the home loan early are not counted towards whether a borrower has received a "high-cost" loan, except in rare circumstances where a lender refinances its own loan.

- Kickbacks to mortgage brokers, known as yield spread premiums, encourage the steering of borrowers into higher-priced loans than borrowers qualify for, but it appears this form of broker compensation is not treated like other fees in determining whether a borrower has received a "high-cost" loan in the Ney-Kanjorski proposal.

The chart below breaks out the costs to the borrower associated with two hypothetical loans that the Ney-Kanjorski bill would treat as perfectly good mortgages.

	LOAN #1	LOAN #2
Loan Amount	$ 100,000	$ 150,000
Total Points and Fees Paid	$ 24,482	$ 31,723
Points & Fees as % of Loan Amount	24.4%	21.1%
<u>Fee Breakdown</u>		
Origination Fees	$ 4,990	$ 7,485
Broker Fees	$ 4,000	$ 6,000
Discount Points	$ 2,000	$ 3,000
Single Premium Credit Insurance	$ 10,000	$ 10,000
Prepayment Penalties	$ 3,492	$ 5,238
Total Loan Amount if Fees Financed	**$ 124,482**	**$ 181,723**
Original Interest Rate	8.73%	8.73%
APR	11.33%	10.99%
Monthly Payment	$ 977.52	$ 1,427.02
EQUITY LOST AFTER REFINANCE IN 2 YEARS	**$ 24,482**	**$ 31,723**

Total Points and Fees Paid: *This line shows the cost of the loan from the homeowner's perspective. In Loan #1, the points and fees equal almost 25% of the loan amount. However, Loan #1 is not a higher-cost loan under Ney-Kanjorski, because the bill excludes a host of fees from its calculation of whether a loan falls into this special category.*

2. The bill fails to address certain practices inappropriate on any home loan

Fails to effectively address abusive loan flipping. The Ney-Kanjorski bill addresses flipping only for high-cost loans, allowing lenders to repeatedly flip borrowers into loans that provide no net benefit as long as the upfront fees are only 4.99 percent of the loan amount each time and only applying the prohibition when a refinance is within two years of the original loan. The bill's exceptions to its flipping provision create a road map for abusive flips that would be permitted under the law. A more appropriate response would be to apply a prohibition against flipping to <u>all</u> home loans.

Fails to prevent abusive prepayment penalties on subprime loans. While the bill limits prepayment penalties on all home loans to 3 years, it permits lenders to charge a high prepayment fee (typically 4%-5% of the loan). An increasing number of subprime lenders have reduced the amount of these penalties, and the Ney-Kanjorski bill lags behind the market leaders. For instance, HSBC (Household) limits prepayment penalties to two percent of the loan amount. As a result, the bill endorses a practice that requires borrowers who have loans with higher interest rates to pay bigger prepayment penalties in order to refinance into a more affordable loan. Further, if enacted, the proposal would preempt laws in the majority of states that have prohibited or further limited prepayment penalties.

3. Fails to prevent equity-stripping for borrowers who receive high-cost loans.

Protections for high-cost loans apply only in those rare circumstances when borrowers incur more than five percent of the loan amount in points and fees or interest rates above approximately 12.5 percent in today's market, loans that put borrowers at extreme risk of equity loss or foreclosure. The Ney-Kanjorski bill would allow a lender to finance up to five percent of the loan amount in conjunction with a high-cost loan, and would not require any counseling prior to obtaining a loan.

In many high-cost loans, borrowers never realize the significance of the exorbitant hidden fees on the loan because they don't pay for them in cash, but instead finance the points into the loan. Limits on financing high fees and a counseling requirement for high-cost loans are essential to deterring equity stripping through fees, making it much more difficult for lenders to mislead a borrower into agreeing to an overpriced loan and encouraging lenders to put risk into interest rate, a cost that is much more transparent to the borrower.

4. Fails to provide Meaningful Remedies

Fails to ban mandatory arbitration on all home loans. The Ney-Kanjorski proposal bans mandatory arbitration on high-cost home loans only, while the Miller-Watt-Frank bill prohibits the use of mandatory arbitration clauses in all home loans. Most of the leading subprime lenders, including Ameriquest, Countrywide, Option One, New Century, Citigroup, and Washington Mutual, prohibit mandatory arbitration on subprime loans, including subprime loans that fall well below any high-cost definition. As a result, the Ney-Kanjorski bill falls short of best practices in the industry.

Significantly reduces assignee liability protections under existing federal law. The Ney-Kanjorski bill would roll back protections available under current federal law that allow borrowers with high-cost loans to seek recourse if their loan has been sold on the secondary market. Because most subprime loans are sold, these severe limitations on assignee liability will mean that many borrowers will be unable to defend their home against foreclosure if they have received a predatory loan. Once they've lost their house, these borrowers may be able to win a suit against a lender for damages years later, but that is small consolation to a family that is forced out of their home. And this lender might well not be around or solvent to sue later: The Reinvestment Fund found that a quarter of all loans currently in foreclosure in Philadelphia today were originated by lenders no longer in business. In contrast, numerous states, including Illinois, Massachusetts, New Mexico, and North Carolina have found an effective approach to assignee liability that balances the ability of the secondary market to purchase subprime loans and the need for borrowers to be able to protect their home against abusive practices.

5. Broadly preempts state protections for homeowners.

Rather than preserve and strengthen existing state and federal protections for homeowners, the Ney-Kanjorski bill wipes out state anti-predatory lending laws that have been proven effective at preventing abusive practices and significantly weakens some protections available under the federal law today.

Replaces effective state protections against predatory lending with a weak federal standard. H.R. 1295 preempts state anti-predatory mortgage lending laws that have proven effective at curbing abusive lending practices and would replace these state laws with a weak federal standard that falls far short of principles for effective legislation to eliminate predatory lending.

In addition, the bill includes numerous loopholes that undercut the stated purpose of the bill. While the Ney-Kanjorski bill purports to lower the points and fees threshold, changes to the definition of points and fees make the definition less inclusive than current federal law under HOEPA. Exceptions to a prohibition against subterfuge would in fact encourage loan-splitting, allowing lenders to avoid making a high-cost loan and thereby triggering protections for such loans. Exceptions to the ability to repay provision would limit its effectiveness and preempt ongoing state efforts to address such abuses.

B. The Miller-Watt-Frank Bill

In contrast, Representatives Brad Miller (D-NC), Mel Watt (D-NC), and Barney Frank (D-MA) have introduced legislation to amend HOEPA that draws directly on North Carolina's 1999 law. H.R. 1182 ("The Prohibit Predatory Lending Act") provides meaningful and effective consumer protections while relying on provisions with proven success in supporting the subprime mortgage market. Here are some of the key strengths of the bill:

1. Adopts a comprehensive definition of "high-cost home loan."

H.R. 1182 defines high-cost loans as loans with points and fees above five percent of the loan amount and takes a comprehensive approach to which fees count towards that five percent. In contrast to the Ney-Kanjorski proposal, the definition of points and fees includes yield-spread premiums, prepayment penalties and single premium credit insurance. While the North Carolina law does not include yield spread premiums in its points and fees definition, it has addressed yield spread premiums through additional duties imposed on brokers under a separate broker statute. Several additional states, including New Mexico, New Jersey, New York, and Georgia (even after later amendments to the law) include yield spread premiums in their definition of points and fees.

2. Provides protections for abuses that are inappropriate for any home loan.

The Miller-Watt-Frank bill addresses equity-stripping below high-cost thresholds by adopting the North Carolina prohibition against flipping a home loan without any reasonable, tangible benefit to the borrower.

3. Provides effective protections for high-cost loans

As in the North Carolina law, H.R. 1182 prohibits the financing of any fees on a high-cost loan, encouraging lenders to express any additional risk in the loan in terms of interest rate, rather than requiring borrowers to finance high fees out of their home equity.

Many other states have adopted a similar approach, allowing only two or three percent of the loan amount to be financed on a loan with high fees.

Following a precedent set in at least seven state laws (Arkansas, Georgia, Massachusetts, North Carolina, New Jersey, New Mexico, and South Carolina), H.R. 1182 requires counseling for borrowers before they enter into a high-cost loan.

The bill prohibits prepayment penalties on high-cost loans below local FHA loan limits, and also prohibits excessive fees for payoff information, loan modifications, or late payments.

In addition, the bill prohibits practices that increase the risk of foreclosure, such as lending without regard for whether the borrower is able to repay, encouraging a borrower to default, balloon loans, and call provisions.

4. Provides Meaningful Remedies for Borrowers.

The Miller-Watt-Frank bill prohibits mandatory arbitration clauses on all home loans.

Further, it preserves assignee liability protections. The Miller-Watt-Frank bill would maintain existing protections in the Home Ownership and Equity Protection Act (HOEPA) that have been in place and successful since 1994.

5. Allows flexibility for states to address localized and new abuses.

The Miller-Watt-Frank bill preserves existing preemption language under HOEPA, which states that federal standards are a floor, not a ceiling, and allows states to enact additional protections.

C. Preemption of State Laws:

1. Federal preemption of state anti-predatory lending laws would be misguided, as any federal standards should supplement, not replace, existing state efforts.
When the federal government first legislated against predatory home lending through the HOEPA floor, states were free to go further. This dynamic has served the nation well, allowing for a "cooperative federalism" in which state-developed solutions and federal regulatory efforts inform and support each other. While North Carolina was the first state in the nation to pass strong anti-predatory lending legislation, others have followed and identified appropriate solutions for their particular context.[22] States have served as "laboratories of democracy" with respect to predatory lending by helping to refine solutions for important issues.

[22] Acting Commissioner Donald Bryan, New Jersey Department of Banking and Insurance, Letter to Senator Corzine (May 11, 2005). *See also*, New Jersey Department of Banking and Insurance, *New Jersey's Predatory Lending Law Protecting Consumers*, Press Release (December 21, 2004).

2. Federal agencies have learned from state-based efforts to address predatory lending. In at least two cases, federal agencies have learned from and acted upon lessons developed at the state level. In adopting changes to their regulatory framework, the Federal Reserve Board and the Office of Thrift Supervision each exemplified the best ideals of federalism.

The Federal Reserve Board took important action in 2001 when it moved to incorporate single premium credit insurance within the scope of charges evaluated as a point or fee under HOEPA. But, the Federal Reserve did not arrive at this conclusion in a vacuum. Indeed, the first jurisdiction to reach such a conclusion was the state of North Carolina, which adopted a similar provision in its 1999 law. Even as North Carolina reached the conclusion that such products were harming consumers, it recognized that legitimate forms of credit insurance, calculated and paid on a monthly basis, did not have harmful equity stripping effects and should not be subject to the same scrutiny. Following the law's effective date, Freddie Mac and Fannie Mae and then many lenders publicly disclaimed such products and the market appears to have successfully transitioned to the monthly product. Consequently, the Federal Reserve acted responsibly when it saw that similar benefits could be extended through the federal HOEPA floor to borrowers in all states.

Similarly, some 35 states currently have statutory provisions relating to prepayment penalties on home loans. Yet, federal law had been interpreted to preclude these states from enforcing those laws against state-chartered finance companies and mortgage brokers in adjustable rate mortgages (ARMs) and other alternative mortgage transactions. Increasingly, subprime prepayment penalties in home loans have come under scrutiny and a number of states have moved to prohibit them outright or to limit their application. In recognition of these developments, the Office of Thrift Supervision took commendable action when it revised federal regulations in a way that promoted cooperative federalism by restoring the states' rights to apply their laws to these state-chartered institutions.

3. States are best equipped to respond to abuses in their particular markets. We urge you today to continue in this vein and partner with states to provide protections for the nation's homeowners. In addition to losing the opportunity for synergy with state efforts, federal preemption of state law is not a practical response to predatory lending because states are in the best position to respond to many of the challenges presented by predatory lending, for at least three reasons: (1) many of the bad actors involved in predatory lending are state-chartered entities with minimal capitalization, (2) regional variations in real estate markets require different solutions to predatory lending, and (3) irresponsible lenders can invent new abusive practices virtually overnight, and the federal government is ill-equipped to react quickly to these changes.

First, federal enforcement of financial services laws depends largely on periodic examinations of the practices of large institutions. The broker who just hung a shingle from his door, however, can originate abusive loans without much fear of federal oversight—as can a state-chartered affiliate of a bank that is not likely to affect its larger parent's overall safety and soundness. State attorneys general and bank regulators have been instrumental in investigating abusive practices and in demanding redress for their citizens. They are also the primary regulators of non-depository finance companies, which dominate the subprime market. The federal government simply cannot be everywhere at once to monitor local real estate transactions.

Second, predatory lending laws should address the special characteristics of each state's underlying real estate regime and market. For example, the mechanism for ensuring that a borrower can raise defenses to foreclosure on predatory home loans may depend on whether a state has judicial or non-judicial foreclosure procedures. The appropriate loan-size threshold for when to prohibit prepayment penalties may depend on the real estate values in a given state. North Carolina prohibits prepayment penalties in first-lien home loans of less than $150,000. In California, the most reasonable threshold would perhaps be considerably higher.

Third, new financial services products are developed every day, frequently to exploit loopholes in laws against abuse. If HOEPA preempted state laws back in 1994, North Carolina never could have outlawed single premium credit insurance, and the abusive practice would still be widespread today. In North Carolina, the legislature prohibited the sale of financed credit insurance. Within two years, the similar "but-not-insurance" product of "debt cancellation agreements" was born, and many states have moved to cover such products as they address single premium credit insurance through legislation. State legislatures are better suited than Congress for responding quickly to such changes.

4. Lenders have experience complying with a variety of state laws that affect their business practices, and complying with state-based homeowner protection laws presents no heavier a burden. Given the evidence of success at the state level, Congress would do harm to homeowners by imposing a uniform standard in lieu of state protections. Every day, lenders deal with tremendous variety in state real estate laws and practices, including consumer protection laws.[23] The laws concerning who may act as a settlement agent differ from state to state. Foreclosure law differs from state to state. States have their own fraud and deceptive practices acts, interpreted by state court judges in accordance with state-specific common law.

Just as lenders find tools for complying with these and other variations, we believe that they are capable of complying with state-based homeowner protection statutes as well. The market has responded by producing computer products that claim to assist lenders in their compliance obligations across state borders.[24] In fact, the variation in these statutes is actually quite small, and we can expect states to move even closer to a consensus approach as regulation of predatory lending improves in its ability to curb abuses. With the incredible recent growth in subprime lending that has occurred, it is simply not credible to claim that variations in state laws have hamstrung this industry.

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[23] Significantly, federal laws such as the Fair Housing Act and the Equal Credit Opportunity Act regulate the real estate finance market without broadly preempting comparable state regulations.

[24] *See* Bergquist, Eric, "Some Lenders Turning to Compliance Software", American Banker, v168, n62 (April 1, 2003).

Conclusion

As an experienced mortgage lender, we know that risk management is a key element of good lending. Responsible lenders are adept at assessing credit quality and property appraisals to determine whether a particular loan represents a good investment.

Today we are weighing the risks of competing policies that will govern subprime mortgage lending. On the one hand, we have the risk that qualified borrowers will not have sufficient access to subprime mortgage credit. Given the remarkable growth of subprime lending during the past decade and the successful implementation of state anti-predatory lending laws, this risk seems very slight indeed. On the other hand, we have the risk of families losing their hard-earned equity and their homes. Evidence strongly suggests this risk increases with subprime mortgages that include excessive fees, abusive prepayment penalties and weak provisions for lender accountability. In this era where credit is arguably more available than ever before, it seems clear that the risks associated with equity stripping and foreclosures far outweigh concerns about a market that is growing faster than any other area of consumer finance.

Fortunately, it is not necessary to choose between a healthy subprime mortgage lending industry and prosperous borrowers who are building wealth. When policymakers implement policies that demand responsible lending, we can have both. It is our sincere hope that these subcommittees will choose the right policies for the millions of senior citizens and families who depend on homeownership to build a better future.

Appendix A
Significant Increases in Subprime Lending

The subprime mortgage industry has thrived over the past several years, even with the prevalence of state predatory lending laws passed across the nation. This is a clear indication that predatory lending laws and regulations have not hindered the subprime market, as many industry officials had feared would happen. The following list of facts support the claim that predatory lending laws are not stifling credit to low-income and poor-credit borrowers:

- In 2004, there was a **record $530 billion in subprime originations** [1] **-- a 60 percent increase** over the previous year**—compared to a 33% decrease in the prime mortgage market** in the same period. Most major subprime lenders experienced a significant increase in volume in 2004.

Originations for Top 10 Subprime B&C Mortgage Lenders [2]

Lender	2004 Volume ($ in millions)	2003 Volume ($ in millions)	% Increase from '03-'04
Ameriquest Mortgage	$82,675	$41,700	98.3%
New Century Financial	$42,200	$27,400	54.0%
Countrywide Financial	$39,441	$19,827	98.9%
HSBC Consumer Finance	$33,250	$20,336	63.5%
Washington Mutual	$29,563	$19,452	52.0%
First Franklin Financial Corp.	$28,946	$20,081	44.2%
Option One Mortgage	$25,990	$20,136	29.1%
CitiFinancial	$23,543	$21,428	9.9%
Fremont General Corp.	$22,890	$13,110	74.6%
Wells Fargo Home Mortgage	$22,395	$16,485	35.9%
TOTAL	**$350,893**	**$219,955**	**59.5%**

- Subprime lenders originated **18.9 percent** of all mortgages in 2004, **more than doubling the 8.8 percent** market share they held in 2003 [3].

- The 24 states that had a predatory lending law in effect during 2003 had a **45 percent increase** in subprime origination volume since 2001, whereas states without a predatory lending law experienced only a **20 percent increase** in volume.[4]

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[1] *Subprime Lenders Outpace The Mortgage Market in Record 2004*, Inside B&C Lending, February 14, 2005
[2] *Top 25 B&C Lenders in 2004*, Inside B&C Lending, February 14, 2005
[3] *Subprime Lenders Outpace The Mortgage Market in Record 2004*, Inside B&C Lending, February 14, 2005
[4] State origination data for 2004 not yet available.

Appendix B
North Carolina versus Neighboring States

FLOW OF CREDIT*

Growth in Subprime **Refinance** Lending per 100,000 Adults, 1998-2003*

Year	GA	NC	SC	TN	VA	US
1998-99	59%	70%	68%	63%	33%	48%
1999-00	11%	-6%	5%	11%	6%	0%
2000-01	42%	13%	16%	10%	43%	35%
2001-02	-4%	31%	12%	17%	45%	46%
2002-03	28%	32%	32%	34%	77%	53%
1998-2003	208%	214%	204%	211%	416%	345%

Growth in Subprime **Purchase** Lending per 100,000 Adults, 1998-2003*

Year	GA	NC	SC	TN	VA	US
1998-99	21%	48%	88%	34%	31%	48%
1999-00	11%	26%	12%	28%	30%	13%
2000-01	11%	34%	27%	29%	28%	11%
2001-02	-3%	25%	36%	21%	34%	29%
2002-03	46%	50%	61%	50%	40%	49%
1998-2003	110%	366%	484%	306%	308%	256%

***** This data is derived from the Loan Performance Database are for borrowers' whose loans meet the following criteria: Full Doc, 30-Years, No Jumbo, 1st Lien, single-family home, owner-occupied. These criteria were chosen because they reflect those of a typical subprime borrower.

Appendix C
North Carolina versus Neighboring States

COST OF CREDIT*

Mean **Initial Interest** Subprime **Refinance** Lending, 1998-2003*

Year	GA	NC	SC	TN	VA	US
1998	9.4	9.56	9.8	9.54	9.25	9.13
1999	10.06	10.02	10.03	10.12	9.88	9.75
2000	10.78	11.02	11.08	10.9	10.64	10.56
2001	9.73	10.11	10.06	9.96	9.47	9.51
2002	8.89	9.15	9.12	9.13	8.57	8.6
2003	7.88	8.07	8.06	8.08	7.62	7.62
2004 (partial)	7.47	7.69	7.82	7.67	7.22	7.16

Mean **APR Spread** of HMDA Verified Subprime **Refinance** Lending, 2004**

Year	GA	NC	SC	TN	VA	US
2004	4.31	4.40	4.51	4.43	4.10	4.13%

Percent of Subprime **Refinance** Loans with **Prepayment Penalties**, 1998-2003*

Year	GA	NC	SC	TN	VA	US
1998	76	22	8	76	55	63
1999	87	33	16	87	85	74
2000	91	36	23	93	89	78
2001	90	28	34	95	84	79
2002	83	20	32	93	85	79
2003	16	11	39	94	85	74
2004 (partial)	16	13	5	93	86	71

Percent of Subprime **Refinance** Loans with **36 Month or Longer Prepayment Penalties**, 1998-2003*

Year	GA	NC	SC	TN	VA	US
1998	54	14	6	58	40	41
1999	65	25	11	71	64	52
2000	64	20	16	73	65	51
2001	61	4	24	71	58	50
2002	46	1	18	60	43	42
2003	8	1	21	58	42	37
2004 (partial)	5	0	1	53	35	33

Continued next page.

Appendix C - continued

Mean **Initial Interest** Subprime **Purchase** Lending, 1998-2003*

Year	GA	NC	SC	TN	VA	US
1998	9.66	9.59	9.88	9.73	8.63	9.32
1999	10.07	10.15	9.89	10.15	9.73	9.87
2000	10.57	10.63	10.71	10.73	10.35	10.44
2001	9.58	9.81	9.76	9.81	9.24	9.51
2002	8.66	8.59	8.52	8.8	8.32	8.42
2003	7.42	7.74	7.7	7.92	7.39	7.46
2004 (partial)	6.76	7.22	7.44	7.51	6.78	6.95

Mean **APR SPREAD** of HMDA Verified Subprime **Purchase** Lending, 2004**

Year	GA	NC	SC	TN	VA	US
2004	3.95	4.05	4.17	4.07	3.96	3.91

Percent of Subprime **Purchase** Loans with **Prepayment Penalties**, 1998-2003*

Year	GA	NC	SC	TN	VA	US
1998	68	22	10	66	38	55
1999	78	39	19	83	68	73
2000	83	33	23	86	72	75
2001	76	23	28	82	68	71
2002	73	19	27	82	69	75
2003	22	8	38	89	71	73
2004 (partial)	25	11	4	91	70	68

Percent of Subprime **Purchase** Loans with **36 Month or Longer Prepayment Penalties**, 1998-2003*

Year	GA	NC	SC	TN	VA	US
1998	32	11	4	36	21	26
1999	47	24	12	54	42	42
2000	46	14	12	55	45	41
2001	40	4	15	52	39	38
2002	29	1	11	41	28	33
2003	6	1	12	37	27	26
2004 (partial)	6	0	1	28	20	19

*This data is derived from the Loan Performance Database are for borrowers' whose loans meet the following criteria: Full Doc, 30-Years, No Jumbo, 1st Lien, single-family home, owner-occupied. These criteria were chosen because they reflect those of a typical subprime borrower

Appendix D
North Carolina versus Neighboring States

BORROWERS SERVED BY THE SUBPRIME MARKET

Mean **FICO** Subprime **Refinance** Lending, 1998-2003*

Year	GA	NC	SC	TN	VA	US
1998	586	579	568	581	565	600
1999	581	580	581	580	576	590
2000	574	573	576	575	567	581
2001	576	575	572	579	572	592
2002	576	574	572	575	573	594
2003	587	582	580	582	581	604
2004 (partial)	607	602	597	601	605	605

Mean **LTV** Subprime **Refinance** Lending, 1998-2003*

Year	GA	NC	SC	TN	VA	US
1998	80	79	80	80	80	77
1999	80	79	80	80	80	77
2000	81	79	80	81	79	78
2001	82	81	81	82	81	79
2002	82	83	83	83	81	79
2003	83	83	84	85	81	80
2004 (partial)	83	83	84	85	80	79

Ratio of **African-American to White, Non-Hispanic** HMDA Verified Subprime **Refinance** Lending per Adult, 2004**

Year	GA	NC	SC	TN	VA	US
2004	2.2	2.1	1.8	2.2	2.9	2.0

Ratio of **Hispanic to White, Non-Hispanic** HMDA Verified Subprime **Refinance** Lending per Adult, 2004**

Year	GA	NC	SC	TN	VA	US
2004	2.2	1.3	1.8	1.6	1.9	1.6

HMDA Verified LMI Proportion of Total Subprime **Refinance** Lending, 2004**

Year	GA	NC	SC	TN	VA	US
2004	51.9	47.6	56.0	53.9	67.7	51.2

Continued next page.

Mean **FICO** Subprime **Purchase** Lending, 1998-2003*

Year	GA	NC	SC	TN	VA	US
1998	604	600	603	599	626	613
1999	601	601	596	595	609	605
2000	608	602	598	605	609	608
2001	615	616	613	612	627	619
2002	617	627	629	618	638	628
2003	642	634	633	626	646	639
2004 (partial)	651	634	628	621	655	641

Mean **LTV** Subprime **Purchase** Lending, 1998-2003*

Year	GA	NC	SC	TN	VA	US
1998	86	85	85	86	86	84
1999	86	84	84	84	84	83
2000	87	86	86	85	86	85
2001	89	89	89	88	88	87
2002	89	89	90	89	88	87
2003	90	91	93	91	90	89
2004 (partial)	87	87	90	90	86	87

Ratio of **African-American to White, Non-Hispanic** HMDA Verified Subprime **Purchase** Lending per Adult, 2004**

Year	GA	NC	SC	TN	VA	US
2004	3.7	2.3	1.6	3.3	2.5	2.6

Ratio of **Hispanic to White, Non-Hispanic** HMDA Verified Subprime **Purchase** Lending per Adult, 2004**

Year	GA	NC	SC	TN	VA	US
2004	4.3	5.3	2.8	5.1	8.4	2.9

HMDA Verified LMI Proportion of Total Subprime **Purchase** Lending, 2004**

Year	GA	NC	SC	TN	VA	US
2004	50.3	48.9	59.4	60.5	54.0	48.35

* Source: Loan Performance ABS Subprime Database (as of December 2004)
**** Source: CRL 2004 HMDA Lending Database (as of May 15, 2005).** The CRL HMDA database (as of May 15, 2005) includes 5.5 million home loans originated in 2004 by more than 300 reporting institutions, for a total amount in excess of $1 trillion. 20% of these loans by number of originations and 12% by dollar amount exceeded the subprime APR reporting threshold set by HMDA. The data contain information from a wide range of major subprime lenders, including Ameriquest, Citigroup, Countrywide, Household, GMAC, National City, New Century, and Option One Mortgage Corporation.

Appendix E
States with Strong Anti-Predatory Lending Laws
vs. States with Weaker Laws

A. FLOW OF CREDIT:

Growth in Subprime **Refinance** Lending per 100,000 Adults, 1998-2003*

Year	FL	NC	NJ	NM	OH	PA	US
1998-99	31%	70%	64%	28%	54%	46%	48%
1999-00	1%	-6%	-5%	-28%	9%	6%	0%
2000-01	30%	13%	44%	6%	17%	10%	35%
2001-02	61%	31%	129%	22%	18%	40%	46%
2002-03	79%	32%	78%	40%	28%	52%	53%
1998-2003	396%	214%	822%	67%	196%	261%	345%

Growth in Subprime **Purchase** Lending per 100,000 Adults, 1998-2003*

Year	FL	NC	NJ	NM	OH	PA	US
1998-99	47%	48%	21%	54%	58%	44%	48%
1999-00	14%	26%	14%	-3%	9%	8%	13%
2000-01	7%	34%	4%	-1%	15%	22%	11%
2001-02	25%	25%	35%	38%	21%	21%	29%
2002-03	48%	50%	39%	33%	60%	29%	49%
1998-2003	231%	366%	169%	173%	283%	195%	256%

B. COST OF CREDIT:

Mean **Initial Interest** Subprime **Refinance** Lending, 1998-2003*

Year	FL	NC	NJ	NM	OH	PA	US
1998	9.28	9.56	9.14	9.21	9.27	9.43	9.13
1999	9.82	10.02	9.47	9.84	9.7	10.02	9.75
2000	10.5	11.02	10.49	10.53	10.52	10.76	10.56
2001	9.57	10.11	9.31	9.64	9.73	9.85	9.51
2002	8.78	9.15	8.43	8.84	8.83	8.79	8.6
2003	7.77	8.07	7.63	7.9	7.91	7.89	7.62
2004 (partial)	7.34	7.69	7.19	7.44	7.46	7.47	7.16

Mean **APR SPREAD** of HMDA Verified Subprime **Refinance** Lending, 2004**

Year	FL	NC	NJ	NM	OH	PA	US
2004	4.01	4.40	4.04	4.40	4.09	4.21	4.13

Percent of Subprime **Refinance** Loans with **Prepayment Penalties**, 1998-2003*

Year	FL	NC	NJ	NM	OH	PA	US
1998	81	22	12	11	83	56	63
1999	90	33	47	46	92	72	74
2000	93	36	57	58	94	77	78
2001	93	28	60	65	95	85	79
2002	93	20	67	63	94	88	79
2003	94	11	31	29	91	89	74
2004 (partial)	95	13	0	2	88	91	71

Percent of Subprime **Refinance** Loans with **36 Month or Longer Prepayment Penalties**, 1998-2003*

Year	FL	NC	NJ	NM	OH	PA	US
1998	64	14	8	6	72	42	41
1999	73	25	34	29	81	55	52
2000	72	20	34	35	74	54	51
2001	71	4	32	40	74	61	50
2002	56	1	25	30	60	52	42
2003	55	1	11	11	55	55	37
2004 (partial)	53	0	0	1	46	50	33

Mean **Initial Interest** Subprime **Purchase** Lending, 1998-2003*

Year	FL	NC	NJ	NM	OH	PA	US
1998	9.71	9.59	9.03	9.24	9.4	9.38	9.32
1999	10.03	10.15	9.86	9.77	9.73	9.96	9.87
2000	10.62	10.63	10.55	10.36	10.53	10.75	10.44
2001	9.75	9.81	9.32	9.66	9.79	9.71	9.51
2002	8.7	8.59	8.3	8.82	8.76	8.79	8.42
2003	7.67	7.74	7.36	7.77	7.84	7.79	7.46
2004 (partial)	7.05	7.22	6.9	7.42	7.47	7.37	6.95

Mean **APR SPREAD** of HMDA Verified Subprime **Purchase** Lending, 2004**

Year	FL	NC	NJ	NM	OH	PA	US
2004	3.81	4.05	3.81	3.86	4.00	4.04	3.91

Percent of Subprime **Purchase** Loans with **Prepayment Penalties**, 1998-2003*

Year	FL	NC	NJ	NM	OH	PA	US
1998	74	22	6	16	77	37	55
1999	89	39	38	52	85	54	73
2000	87	33	54	67	87	69	75
2001	84	23	50	60	84	71	71
2002	88	19	60	67	85	73	75
2003	92	8	31	36	86	78	73
2004 (partial)	88	11	1	3	85	79	68

Percent of Subprime **Purchase** Loans with **36 Month or Longer Prepayment Penalties**, 1998-2003*

Year	FL	NC	NJ	NM	OH	PA	US
1998	44	11	3	6	66	19	26
1999	62	24	12	30	75	31	42
2000	60	14	17	41	68	33	41
2001	54	4	14	31	58	33	38
2002	46	1	11	31	48	31	33
2003	36	1	4	13	43	36	26
2004 (partial)	27	0	1	1	31	30	19

C. BORROWERS SERVED BY THE SUBPRIME MARKET:

Mean **FICO** Subprime **Refinance** Lending, 1998-2003*

Year	FL	NC	NJ	NM	OH	PA	US
1998	593	579	610	603	587	589	600
1999	591	580	599	593	581	587	590
2000	587	573	588	586	574	578	581
2001	591	575	596	587	584	590	592
2002	588	574	592	598	585	594	594
2003	596	582	595	606	596	599	604
2004 (partial)	592	602	597	609	598	594	605

Mean **LTV** Subprime **Refinance** Lending, 1998-2003*

Year	FL	NC	NJ	NM	OH	PA	US
1998	78	79	75	77	78	77	77
1999	79	79	76	78	78	78	77
2000	79	79	76	79	79	78	78
2001	80	81	77	80	81	79	79
2002	80	83	77	81	82	81	79
2003	80	83	76	83	84	82	80
2004 (partial)	80	83	75	83	85	81	79

Ratio of **African-American to White, Non-Hispanic** HMDA Verified Subprime **Refinance** Lending per Adult, 2004**

Year	FL	NC	NJ	NM	OH	PA	US
2004	2.2	2.1	1.9	1.5	1.9	1.6	2.0

Ratio of **Hispanic to White, Non-Hispanic** HMDA Verified Subprime **Refinance** Lending per Adult, 2004**

Year	FL	NC	NJ	NM	OH	PA	US
2004	1.7	1.3	1.5	2.1	1.3	1.6	1.6

HMDA Verified LMI Proportion of Total Subprime **Refinance** Lending, 2004**

Year	FL	NC	NJ	NM	OH	PA	US
2004	46.6	47.6	51.8	42.9	63.2	56.6	51.2

Mean **FICO** Subprime **Purchase** Lending, 1998-2003*

Year	FL	NC	NJ	NM	OH	PA	US
1998	595	600	627	615	599	608	613
1999	599	601	611	597	602	604	605
2000	604	602	609	607	600	601	608
2001	613	616	619	605	609	618	619
2002	619	627	620	617	614	622	628
2003	629	634	634	638	626	639	639
2004 (partial)	635	634	643	633	624	635	641

Mean **LTV** Subprime **Purchase** Lending, 1998-2003*

Year	FL	NC	NJ	NM	OH	PA	US
1998	84	85	84	83	82	84	84
1999	84	84	84	83	82	84	83
2000	86	86	84	85	84	86	85
2001	87	89	86	87	86	88	87
2002	87	89	84	88	88	89	87
2003	89	91	86	89	91	91	89
2004 (partial)	87	87	86	88	89	89	87

Ratio of **African-American to White, Non-Hispanic** HMDA Verified Subprime **Purchase** Lending per Adult, 2004**

Year	FL	NC	NJ	NM	OH	PA	US
2004	2.6	2.3	2.4	1.3	2.7	2.0	2.6

Ratio of **Hispanic to White, Non-Hispanic** HMDA Verified Subprime **Purchase** Lending per Adult, 2004**

Year	FL	NC	NJ	NM	OH	PA	US
2004	4.4	5.3	3.6	1.4	2.0	4.2	2.9

HMDA Verified LMI Proportion of Total Subprime **Purchase** Lending, 2004**

Year	FL	NC	NJ	NM	OH	PA	US
2004	36.5	48.9	40.2	39.8	71.0	62.1	48.4

* Source: Loan Performance ABS Subprime Database (as of December 2004)
** Source: CRL 2004 HMDA Lending Database (as of May 15, 2005)