<u>Testimony of Michael D. Calhoun</u>
Center for Responsible Lending

Before the U.S. House Committee on Financial Services
"Legislative Proposals on Reforming Market Practices"

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Chairman Frank, Ranking Member Bachus, and members of the Committee, thank you for holding this hearing to focus on cleaning up the subprime market and restoring confidence in home lending. Families all over the country continue to lose their homes in record numbers, stripping families of their wealth and destroying entire neighborhoods. At the same time, this massive wave of foreclosures has caused major disturbances in national and international markets as lending businesses shut down and thousands of people lose their jobs.

Policymakers in Congress have a long, proud history of taking action to protect the benefits of homeownership. The legislation under review today continues on that path in many ways. We commend the Chairman for his leadership and we hope this committee will endorse strong substantive protections against abusive and reckless lending and support those protections with effective remedies and enforcement.

In my testimony today, I would like to make five key points:

1) 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.

2) Abusive loan products, reckless lending, and lack of accountability have caused the current credit crunch. If sensible limitations had been in place, the mortgage meltdown could have been avoided.

3) The market is <u>not</u> correcting itself. Incentives to make bad loans remain firmly in place. All evidence indicates a lack of self-correction, including recent reports on investment securities backed by subprime mortgages.

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

5) The legislation proposed by Congressmen Frank, Miller and Watt could make a significant difference in preventing the abusive and reckless lending practices that contributed to today's foreclosure crisis. But a lack of adequate remedies for victims of predatory lending and insufficient means for enforcing the law could undermine key protections that would prevent foreclosures in the future.

Before elaborating on our main points, I will provide some brief background. I serve as the President of the Center for Responsible Lending (CRL) (www.responsiblelending.org). CRL is a not-for-profit, non-partisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices.

We also have direct experience as a subprime lender. CRL is an affiliate of the Center for Community Self Help (www.self-help.org), which consists of a credit union and a non-profit loan fund. For the past 26 years, Self-Help has focused on creating ownership opportunities for low-wealth families, primarily through financing home loans to low-income and minority families, those often targeted for subprime loans. Self-Help has provided over $5 billion of financing to 55,000 low-wealth families, small businesses and nonprofit organizations in North Carolina and across the country. Our loan losses have been less than one percent per year.

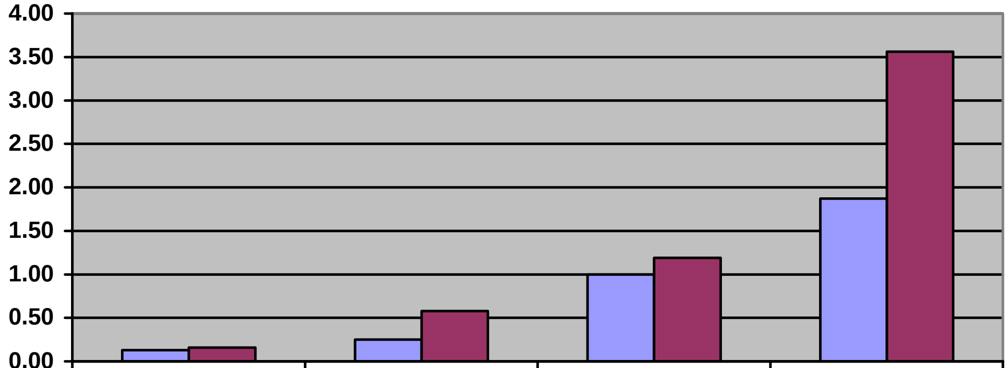
Through this lending experience, I understand the benefits of subprime loans that contribute to sustainable homeownership. Unfortunately, when it comes to fair, affordable mortgages and opportunities for lasting homeownership, the subprime market's record is sorely lacking. The Center for Responsible Lending estimates that 2.2 million families have lost or will lose their homes as a result of abusive subprime loans made in recent years.[1] That is one in every five subprime loans made in 2005 and 2006, a rate unseen in the modern mortgage market. When we consider the subsequent loans subprime borrowers have been refinanced into, the probable foreclosure rate jumps to over one third of all subprime borrowers.

I. Subprime foreclosures: their severity, impact and the misaligned incentives that exacerbate them.

A. The foreclosure problem is severe.

Every credible quantification of subprime foreclosures reveals that the problem is severe. The 2nd Quarter National Delinquency Survey by the Mortgage Bankers Association (MBA) shows that foreclosures on all types of loans have increased, but, as expected, foreclosures in the subprime market are most severe. New foreclosures on subprime adjustable-rate loans in the second quarter 2007 were **90%** higher than the same time last year, compared with a 23% increase on prime fixed-rate loans.

% Foreclosures Started During Quarter



	Prime Fixed-Rate	Prime ARM	Subprime Fixed Rate	Subprime ARM
2Q 2006	0.13	0.25	1.00	1.87
2Q 2007	0.16	0.58	1.19	3.56

Source: MBA National Delinquency Survey

At the same time, the MBA's "point in time" foreclosure statistics mask the extent of the foreclosure problem, because their figures fail to include the high number of subprime loans that were originated recently and have yet to enter their peak foreclosure years. CRL issued a study in December 2006 ("Losing Ground"[2]) estimating that **one out of every five subprime mortgages made in 2005 and 2006 ultimately will end in foreclosure.** This projection refers to <u>actual homes lost</u>, not late payments or foreclosures started but not completed.

When we released our report on subprime foreclosures, the lending industry claimed that our findings were overly pessimistic, and even today some in the industry continue to minimize the problem. However, as shown here, CRL's estimate is in line with other credible projections:[3]

	Loans Analyzed	# Loans in Analysis	Projected Foreclosure Rate (homes lost in foreclosure)	# Projected Foreclosures
MBA	Not disclosed	Not disclosed	Not disclosed	250,000
CRL	Subprime loans, owner-occupied properties, 2005 & 3Qs 2006	5,800,000	19.4%	1,125,000
First American Real Estate Solutions	All adjustable rate mortgages issued in 2004 & 2005[4]	7,700,000	14.3%	1,100,000
Lehman Brothers	Subprime loans, 2006 vintage only[5]	4,000,000[6]	30%	1,200,000
Moody's Economy.com	All loans[7]	Not disclosed	Not disclosed	1,700,000

By any measure, these estimates represent an epidemic of home losses. These foreclosures will not only harm the families who directly lose their homes, but the ripple effects have already begun to extend to the wider local, national and international communities.

B. The foreclosure problem is widespread.

The MBA's recent delinquency report also shows that mortgage loans entering foreclosure have increased in 47 states since this time last year. On average, the increases were 50% higher. Only four states—North Dakota, South Dakota, Utah and Wyoming—did not experience increases in new foreclosures. Less than two percent of the American population lives in those states.

When releasing the survey, the MBA downplayed new foreclosures by focusing only on changes between the last two quarters. But any minor changes from one quarter to the next are largely meaningless. **The foreclosures occurring today are the worst they've been in at least 25 years**

The MBA has also been quick to claim that the performance of subprime loans is primarily a result of local economic conditions, not loan products or underwriting practices. In fact, it is not an either/or proposition. Local economic conditions can affect house prices appreciation and unemployment levels, which affect foreclosure rates. However, subprime loans have typically included features that are known to increase the rate of foreclosure. Economic studies and empirical research also have shown that the incidence of foreclosure escalates quickly due to "layered risk" factors (such as a combination of low down payments, high debt-to-income ratios, adjustable interest rates, etc.)—exactly the types of loans that have dominated the subprime market in recent years.

Furthermore, if local economic conditions were the dominant factor in subprime loan performance, then there would be little distinction between the performance of subprime loans and FHA loans, which are also aimed at riskier borrowers. However, the MBA's own statistics show subprime loans perform worse than FHA loans <u>in the same market:</u>

	% of Outstanding Loans in Foreclosure at End of 2Q 2007	
	Subprime	**FHA**
Northeast	5.76	2.42
North Central	8.76	3.45
South	4.50	1.76
West	4.40	1.23
United States	5.52	2.15
Source: MBA National Delinquency Survey, 2Q 2007		

The MBA also has claimed that defaults on non-owner occupied properties are the major driver for increased subprime foreclosures.[8] However, 88% of foreclosures are suffered by people living in their primary residence.[9] A higher rate of foreclosures on investor properties is not a new development—default risks have <u>always</u> been significantly higher for investor properties compared with owner-occupied homes.[10] We question why the MBA is surprised by this result, if lenders were making subprime loans with loose underwriting standards to this even-riskier class of borrower. Moreover, this type of lending did nothing to increase homeownership, and instead fueled speculative home-buying, short-term run-ups in house prices, and now increased foreclosures and falling home values that are hurting all the families in these neighborhoods.

C. Families and neighborhoods are suffering as a result.

This year, many stories have appeared in the media describing the hardships imposed on families facing foreclosure. Often people ask, "How did these people get into these loans into the first place?"

While the details vary in every situation, the scenario we hear again and again is that lenders assured families that they had the right loan and were doing the right thing. Any time a borrower raised a question about a loan's interest rate or scheduled rate increase, mortgage brokers routinely assured them, "Don't worry about it. You can refinance." If a person expressed concern about an expensive prepayment penalty, they received similar promises: “Don’t worry, we’ll waive the fee when you refinance.” Today these promises mean nothing, since refinances are no longer available for many of these families. Yet, it’s not surprising that families would rely on brokers and lenders as the experts in mortgage financing. At some point in every mortgage transaction, the borrower must be able to trust the lender. Clearly, the trust has been betrayed.

Earlier this month, an article in the *Los Angeles Times* profiled a California couple, John and Mona Breidenstein, the parents of two children, who spent many months desperately trying to work with Countrywide Financial Corporation to convert an adjustable-rate subprime mortgage into a fixed-rate mortgage. Following the typical pattern, their broker had told the Breidensteins they would be able to refinance before the interest rate went up. The Breidensteins anticipated the interest rate adjustment well in advance, but the lender showed no interest in helping them. The couple spent eight months contacting various people at Countrywide, desperately trying to work out an affordable loan. Until the *LA Times* ran the story, Countrywide refused to offer the couple any option other than selling their home.

On a case-by-case basis, these losses represent a personal catastrophe to the families involved, but the negative results extend far beyond individuals. Entire communities will suffer because of the declines in property values that come with nearby foreclosures. Foreclosures can quickly transform neighborhoods from aspiring, stable communities to rows of boarded-up houses that become a breeding ground for crime.[11]

The cost of the subprime problem extends far beyond lost homes and ruined neighborhoods with dropping property values. Over 100 mortgage lenders already have gone out of business and thousands of workers have lost their jobs. It's harder for mortgage lenders and firms in other business lines to get credit from once-burned, twice-shy investors. The stock market is increasingly volatile and the housing market is facing its first national decline since house prices started being measured in the 1950s. All these factors spell slower (or even negative) economic growth in the U.S and—with German banks worried about subprime loans made in Chicago—bleak prospects for help from players in other global financial markets.[12]

D. The secondary market lacks incentives to support sustainable homeownership.

The secondary market for subprime loans lies at the heart of today’s mortgage meltdown. Back in the days when families went to their local savings and loan to get a mortgage and the thrift held that loan among its own investments, the interests of borrowers and lenders were perfectly aligned: if the borrower did not pay the mortgage, the lender did not make money. But the growth of the secondary market upset that core alignment of interests between lender and borrower by creating a system where each actor was compensated early in the loan transaction, often within the first month of the loan, thereby reducing the incentive to worry about how the borrower would fare later on.[13]

Independent mortgage brokers originate most subprime loans (at least 70%), and receive their compensation from a lender immediately upon brokering the loan. That lender turns around and sells the loan into the secondary market, where it is bundled together with other mortgages and sliced and diced into securities. These securities are then sold to investors, who retain the right to collect payments and enforce the mortgage terms, including foreclosing on the home if the borrower defaults.

As the subprime market grew, Wall Street wanted more and more of these loans offering higher-risk investments with potential for higher returns. The demand from Wall Street was so intense that it encouraged subprime lenders to abandon reasonable qualifying standards, to forget about standard documentation requirements, and to ignore whether borrowers could actually afford the loan. Lenders created new, dangerous loan products that appeared deceptively affordable to borrowers, and brokers pushed these products to earn high fees. After filing for bankruptcy, the CEO of one mortgage lender explained it this way to the New York Times, “The market is paying me to do a no-income-verification loan more than it is paying me to do the full documentation loans,” he said. “What would you do?”

Or 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. We created something which was unsustainable. And it eventually broke. If it weren't for securitization, the subprime-loan market would have been very significantly less than it is in size.”[14] Wall Street rating agencies also turned a blind eye to the increasingly high volume of poorly underwritten, extremely dangerous loans included in mortgage investments. Paid by the securitizers to rate the tranches, the agencies overlooked loans that any experienced underwriter would have known were headed for foreclosure, giving an AAA rating to the majority of the tranches created.[15]

The result of this buck-passing was the market meltdown of this summer, which now seems to be continuing into the fall. One market watcher recently observed that “Anything securitized in 2007 has got to have the worst collateral performance of any trust I've seen in my life."[16]

The best way to re-align the interests of borrowers and lenders is for Congress to insist on meaningful assignee liability. Since most mortgage loans are sold on the secondary market, it is essential that secondary market liability create incentives for the market to police itself. When assignee liability exists, the borrower is allowed to pursue legal claims against the assignee when the loan transaction involves illegal actions or abusive terms. In the case of the mortgage market, strong assignee liability would mean that when investors purchase high-risk mortgages, with all the corresponding financial benefits, they also accept reasonable liability for when the mortgages prove to be abusive and harm homeowners.

If this legislation is passed without meaningful assignee liability, the impact of its substantive provisions will be dramatically decreased. The fact is, public enforcement can never be adequate: there is a shortage of resources to match against the millions of loans made to borrowers, and in some cases, a lack of will to take significant action. Investigations will inevitably be too slow for the homeowners who face foreclosure in the meantime, and while public enforcement can achieve some relief, it will rarely, if ever, be enough to make most individual borrowers whole. If the substantive provisions of this bill are to be enforced, it will be done because wronged borrowers are able to move against the holder of their loan, just as they would have been able to do when lenders held the mortgage for the life of the loan.

II. Abusive lending, not regulation, has led to tighter credit.

While the mortgage industry has argued for years that regulation of subprime lending would have the unintended consequence of restricting credit, it is now apparent that the recent credit crunch was 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.

At Self-Help, we know that it is possible to structure subprime loans in such a way that homeowners have a high chance of achieving sustainable ownership. Unfortunately, that's not what most subprime lenders have done in recent years. In fact, they have done the opposite. Typical subprime mortgages have been refinances that include adjustable interest rates, prepayment penalties, and little or no documentation of the borrower's income.

In the "Losing Ground" study, we examined subprime mortgages made from 1998 through 2003 to assess the relationship between specific loan characteristics and the loan's performance. As shown in the chart below, the typical features on subprime mortgages are strongly linked with higher rates of foreclosure:

% Increase in Foreclosure Risk for Specific Loan Features by Annual Loan Cohort[17]

(Positive numbers indicate higher risk, after controlling for borrower credit scores)

	1998	1999	2000	2001	2002	2003
ARM vs. Fixed-Rate Loan	123.31***	86.03***	72.03***	61.80***	77.85***	117.11***
Balloon vs. Fixed-Rate Amortizing Loan	75.67***	51.77***	36.02***	21.66***	14.08*	85.92***
Loan with Prepayment Penalty vs. Loan with No Prepayment Penalty	70.4***	65.0***	52.4***	35.8***	25.8***	18.7***
Loan with No or Low Documentation vs. Full-Doc Loan	5.57**	19.02***	29.00***	25.75***	44.72***	63.69***
Purchase Money Loan vs. Refinance Loan	19.3** *	20.7***	28.5***	37.9***	61.0***	102.0 ***

Confidence levels: * = 95%, ** = 99%, *** = 99.9%. Detailed results available upon request.

This table shows that, even after controlling for a homeowner's credit score, typical subprime loan products and terms increase the chance of loan failures. For example, on adjustable-rate mortgages compared with fixed-rate mortgages, the foreclosure rate was 62 – 123% higher. Loans with prepayment penalties carried a higher foreclosure risk ranging from 19% to 70%.

Some of these loan characteristics can work fine for homeowners when their lenders have carefully evaluated the loan's risk. For example, adjustable-interest rates are a reasonable option for families who reasonably expect a future increase in income. But in recent years, the subprime market became dominated by adjustable rate mortgages that allowed families no chance to sustain them: they were set only to go up, could not go down, and had such high margins (6% to 6.5%) over a cost of funds index (LIBOR) that they quickly jumped to highly unaffordable levels. Further, typical subprime loans included multiple higher-risk features that became even more lethal when packed together in one loan. The 2-28 subprime "exploding ARMs" comprised "nearly 80% of subprime originations in 2006."[18]

For the past decade, subprime lenders have been aggressively marketing these dangerous loans and touting the easy availability of mortgages. Wall Street firms provided false assurances they knew their business. Now, because of their actions, the market is tighter for everyone, and trust in American markets has been eroded across the globe.

III. The market is not self-correcting.

Despite the widespread assumption that the market has corrected itself, we have yet to see evidence that lenders have significantly changed their practices. Last week, Standard & Poor's announced that it had downgraded 1,713 classes of residential mortgage-backed securities (RMBS) backed by subprime and Alt-A mortgages issued in the first half of 2007.[19] Similarly, a recent market analysis by an investment management firm, FBR Capital Markets, notes that the default rate on loans included in RMBS increased dramatically between July and August this year.[20] For RMBS made up of adjustable-rate subprime loans, the default rate increased by 44% in August over the previous month, and even for securities with fixed-rate subprime loans, the increase was 36%. The FBR analysis is clear in blaming high default rates on lax underwriting practices, and the report notes that as of June 2007, "We find little difference between the salient risk characteristics of subprime loans originated in 2007 and 2006."[21]

Moreover, advertisements for dangerous loan products still abound. For example, click on the ubiquitous popup internet ad for LowerMyBills.com—it's the one with the dancing alien and other animated creatures—and you'll be given an opportunity for a "deep discount" on a loan – most likely, a payment option ARM. And Chevy Chase Bank recently sent a flyer to its brokers featuring the excited announcement, "Good New Travels Fast: Stated Income is Back!" Attached to that announcement are guidelines and a rate sheet that show not only is the bank still making stated income loans, but even retirees on fixed incomes can get them.[22]

The truth is, the subprime mortgage market as currently structured doesn't have adequate incentives to change its practices. To the contrary, 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. The market may tighten up temporarily, but with so much money at stake, future abuses are inevitable.

Common-sense protections would prevent this catastrophe from happening again. We need a combination of targeted substantive protections combined with effective remedies and strong enforcement provisions.

IV. Disclosures are inadequate.

Industry representatives have urged policymakers to focus their response on requiring lenders to make further written disclosures to consumers—adding to the mountain of papers whose real significance is often difficult for the average consumer to assess, and is frequently contradicted by the oral explanations and assurances provided by mortgage brokers and lenders.

This response is insufficient, and reflects an inadequate appreciation of the problem's causes and scope. The failure to assess the risks and consequences of current lending practices is what created the problem to begin with. It must not be repeated as Congress contemplates solutions.

A common fallacy is that borrowers consciously choose and accept the loan terms they get because they read and sign an array of disclosure documents during the loan closing. In fact, most terms on a standard mortgage contract are buried in pre-printed loan documents, and are dictated by the lender, not negotiated by consumers. Further, the documents outlining critical loan terms are typically only three to five documents out of dozens in a standard loan closing.6

As former MBA President Robert M. Couch has 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."[23]

Other issues that hinder disclosure from being effective include the complexity of many mortgage products and the difficulty of comprehending many disclosure forms that are allegedly in "plain English." For example, according to the commonly used Flesch Readability Score, the Truth in Lending form disclosures are comparable to reading the Wall Street Journal or Harvard Business Review. In short, improved disclosures are not likely to help borrowers, and in some cases they may make the situation worse.

V. The proposed legislation provides many strong and crucial substantive provisions, but remedies should be improved.

H.R. 3915 takes a comprehensive approach to the reckless and abusive mortgage lending practices that contributed to today's foreclosure crisis. We welcome Chairman Frank's, Congressmen Miller and Watt, and other committee members' leadership in tackling these issues. As I noted earlier, it is now clear beyond all doubt that inadequate regulation poses a greater threat to access to *productive* credit than does sound regulation.

We welcome the expansion of the protections to the highest-cost segment of the market promised by the bill – the expansion of HOEPA protections in Title III of the bill. The enhanced provisions will bring to the national market the benefits of several states' experience since 1999 with improving HOEPA to better address evolving problems in the high cost market. HOEPA was somewhat successful in addressing the abuses it targeted in 1994, but the market did not stand still. Because HOEPA did not preempt state law, states were able to, and did, move to address many of the next generation of problems that appeared in the years following HOEPA's enactment. We know that these laws work, and work without impeding access to credit, because we have been able to study their impact. The evidence suggests that legitimate, honest competitors benefit from the law, as well as consumers.[24] It counters the effect of a "Gresham's Law," wherein bad lending drives out good lending. The result is a "win-win" for consumers and for an efficient, marketplace that operates with integrity. We believe that extending the benefit of those leading-edge states nationally through the enactment of Title III can only be a positive benefit all around.

Titles I and II of the proposed bill would bring badly needed reform to broader segments of the market than HOEPA covers. These are central to reforming practices that led to the recent crisis: the abandonment of basic, common sense underwriting practices and the perverse incentives in the market that encouraged risky, rather than responsible, lending. In their eagerness to simply originate more volume to feed a hungry Wall Street, market players at all stages of the process forgot basic business values. They forgot that it is a basic part of the lending business to evaluate whether the borrower can pay back the loan. And they forgot that it is a basic part of any business to match the product to the borrower's needs. No one would ever defend an electrician who, asked to wire a home for a dryer, put in a 110 instead of a 220 outlet. Yet today's foreclosure fires were fueled by equally reckless actions. Sadly, the market justified its conduct by false assertions that it was homeowners who "chose" the inappropriate, dangerous 110 wiring, and that clamping down on such electricians would limit the overall supply.

In Titles I and II, the bill addresses common subprime practices that have fueled subprime foreclosures. Key, vital reforms are included in the substantive provisions of the bill:

* It would prohibit yield spread premiums. This should eliminate the perverse incentive to place borrowers in higher-cost loans than they qualify for to maximize brokers' compensation.

* It would prohibit prepayment penalties in the subprime market, where they have acted as what we have called "the glue for steering." The link to steering arises because brokers typically can get paid more (a higher yield spread premium) to deliver a loan with a prepayment penalty to a creditor. The prepayment penalty then, puts the consumer between a rock and a hard place. It either locks the consumer into an expensive, troublesome loan, or forces them to pay a steep "exit tax" to get out of it.

* It aims to bring more common sense underwriting practices to the market, primarily the subprime ARM market segment.

* It aims to assure that loans are better matched to the needs and capacity of the borrowers.

* It provides significant other reforms, including a ban on pre-dispute binding mandatory arbitration, and a prohibition on financing credit insurance and related products.

* In addition, it provides some long-needed updating to Truth in Lending remedies generally, increasing the civil damages and permitting consumers to raise rescission as a defense to foreclosure after the three year cut-off.

Together, these welcome reforms address key market failures that brought us to this pass. We are strongly supportive of the direction these substantive reforms would take, as we will explain in this testimony. They are crucial to restoring common sense to an industry that lost its way.

We also are pleased that this bill does not contain explicit preemption provisions. Over the years, we have seen many states respond swiftly and effectively to the growth of predatory lending practices in their jurisdictions, and we believe that it is critical for states to continue to have the ability to respond to new challenges as they arise. There is a risk, however, that regulations issued by certain regulators envisioned by this proposal, such as the OCC and OTS, may be interpreted to preempt state laws as a result of the National Bank Act and the Homeowners Loan Act, independent of the explicit preemption standards in this law itself. We hope that the rule-making authority envisioned do not result in unintended preemption.[25]

We do, however, have serious concerns about whether the incentives for compliance with the reforms are adequate. Most neutral arbiters acknowledge that the massive meltdown was a result of the separation of actions and consequences all along the chain, with a resulting break down in accountability. That is to say, Wall Street is part of the problem. That means that it must be part of the solution. While in the past, some have argued that exposing the secondary market too much to potential liability would result in dried up credit for subprime borrowers, we now see that too little exposure made them too reckless – and that resulted in a much more widespread credit crunch than virtually anyone imagined. Consequently, Wall Street can no longer assure us that its own market discipline will suffice. There must be adequate accountability for it, too. We understand, of course, that a balance must be struck. Unlimited, uncertain liability would likely impede liquidity. The question is whether the legislation, as proposed, strikes that balance.

As the bill currently stands, we fear that the remedies and enforcement provisions may well not ensure that the protections are meaningful and that industry participants, including the secondary market, take the protections seriously.

A. The bill includes vitally important protections that are critical to restoring responsible underwriting and origination practices to the market.

1. Requiring a determination that the borrower has an ability to repay is a key step to avert a recurrence of today's crisis

We welcome the bill's proposal that would require more realistic underwriting standards. It would require qualifying borrowers at the fully-indexed rate for the loan, and would require that taxes and insurance (both homeowners insurance and any mortgage insurance) costs be included when assessing a borrower's ability to repay.

By the industry's own admission, underwriting standards in the subprime market have become extremely loose in recent years, and analysts have cited this laxness as a key driver in foreclosures. For example, lenders who have marketed 2/28s and other hybrid ARMs generally have not considered whether the homeowner will be able to pay when the loan's interest rate resets, setting the borrower up for failure. Subprime lenders' public disclosures indicate that most are qualifying borrowers at or near the initial start rate, even when it is clear from the terms of the loan that the interest rate will rise significantly even if interest rates in the economy stay constant, giving the borrower a much higher monthly payment. In fact, it is not uncommon for 2/28 mortgages to be originated with an interest rate four percentage points under the fully-indexed rate. For a loan with an eight percent start rate, a four-percentage point increase to twelve percent is tantamount to a 40 percent increase in the monthly principal and interest payment amount. As the lenders well know, virtually no subprime borrower can afford such an increase.

We note that, though captioned as a protection for "all home loans," the existence of safe harbors seems to mean that, functionally, this provision applies primarily to subprime ARM loans. That is a signal improvement, as it appears that the structural market failure was in those loans. However, by no means was reckless underwriting limited to that segment. Indeed, unaffordable fixed rate loans were all-too common among that segment of the market not fixated on the hybrid ARMs. For example, the Associates and Household loans, which were the subject of regulatory action by the FTC and the states, respectively, primarily involved fixed-rate subprime loans.

2. The proposal recognizes that verification and documentation is essential to assuring that the ability to pay requirement is meaningful.[26]

The bill further requires that the determination of ability to pay be based on "verified and documented information." The unwarranted, unnecessary, and widespread use of stated income, and lo- or no-doc loans facilitated the epidemic of unsustainable lending. Lenders may evaluate the risk of a loan before approving it, but without adequate documentation of income, a lender's approval of a loan is meaningless. Even as the problem became undeniable, too many loans continued to be made on this basis into 2007. Based on our review of 10 mortgage-backed securities, we find that, on average, more than one third--37%--of these recently securitized subprime loans were approved based on stated income or reduced documentation standards for verifying the borrower's income.[27] The vast majority of borrowers have readily documentable W-2 income; by putting them in low-doc loans, lenders are either charging them up to 1 percent higher interest for no reason, or inventing non-existent income in order to make them a loan that is doomed to fail.

As Comptroller of the Currency, John Dugan, has stated, "Sound underwriting—and, for that matter—simple common sense—suggest that a mortgage lender would almost always want to verify the income of a riskier subprime borrower to make sure that he or she has the means to make the required monthly payment. Most subprime borrowers are salaried employees for whom verifying income by producing copies of W-2 forms is just not that difficult." We see no justification for lenders failing to use readily available data on a borrower's income, and are pleased that the bill recognizes this.

3. Requiring that originators serve the interests of their clients and customers is a lynchpin of market reform

The proposal would reverse an unfortunate trend in which originators lost sight of the basic purpose of their business – to provide their clients and customers with a loan product geared to their needs, and that they could sustain. Buying or refinancing a home is the biggest investment that most families ever make, and particularly in the subprime market, this transaction is often decisive in determining a family's future financial security. A broker has specialized market knowledge that the borrower relies on. Indeed, brokers hold themselves out to borrowers as a trusted adviser for navigating the complex mortgage market; that is the service they sell, and it is the service consumers assume they are buying.

Yet, mortgage brokers, for the most part, deny that they have any legal or ethical responsibility to refrain from selling inappropriate, unaffordable loans, or to avoid benefiting personally at the expense of their borrowers. Brokers and lenders have been too focused on feeding investor demand in exchange for high fees, regardless of how particular products affect individual homeowners. Moreover, because of the way they are compensated, brokers have strong incentives to sell excessively expensive loans

Experts on mortgage financing have long raised concerns about problems inherent in a market dominated by broker originations. For example, the chairman of the Federal Reserve Board, Ben S. Bernanke, recently noted that placing significant pricing discretion in the hands of financially motivated mortgage brokers in the sales of mortgage products can be a prescription for trouble, as it can lead to behavior not in compliance with fair lending laws. Similarly, a report issued by Harvard University's Joint Center for Housing Studies, stated, "Having no long term interest in the performance of the loan, a broker's incentive is to close the loan while charging the highest combination of fees and mortgage interest rates the market will bear."

We welcome the bill's intent to establish a floor for the duties that originators must observe in dealing with their customers. Like the electrician, mortgage brokers' value lie in their specialized knowledge of a highly complex world. Their job is to help people less familiar with that world navigate it. Trust – *earned* trust – is essential to make that front-end segment of the market work. These reforms, properly implemented, will preclude brokers from denying that they must act responsibly toward their customers.

4. The anti-steering provisions take aim at one of the most insidious of market abuses – the discriminatory practice of steering families into unnecessarily expensive home loans, and it eliminates the perverse market incentives that encouraged it. The prohibition against yield spread premiums is among the most significant reforms proposed.

The bill takes on steering both directly, by mandating rules that will prohibit it, and by removing the perverse compensation incentive that encouraged it. We believe that the prohibition on yield spread premiums is one of the most significant reforms proposed, and we commend the bill's sponsors for tackling the problem head-on. The bill would eliminate this perverse market incentive, so that brokers would not maximize their own compensation by increasing both cost and risk to their clients.

Efficient financial markets should provide equally qualified borrowers with equally competitive prices on subprime home loans. However, both quantitative research and anecdotal evidence suggests that there are significant price disparities in subprime lending that indicate that some borrowers, particularly African-American and Latino families, pay more than necessary for subprime mortgages.

In May 2006, CRL analyzed data submitted by mortgage lenders for loans made in 2004 to assess the effects of race and ethnicity on pricing in the subprime market while controlling for the major risk factors used to determine loan prices. Our findings showed that, for most types of subprime home loans, African-American and Latino families were at greater risk of receiving higher-rate loans than white borrowers, even after controlling for legitimate risk factors. In other words, if two families received subprime loans, one African American and one white, and they had the same credit score and were similarly qualified in every other way, the African-American family has a significant chance of receiving a higher-cost loan.

We welcome this effort to eliminate this practice that has caused so much wealth to be lost from so many families and communities.

5. Requiring a net tangible benefit for refinances will reduce equity stripping and stanch further loss of wealth.

The proposed legislation would incorporate some of the state reforms aimed at assuring that loans served a purpose other than transferring equity from the homeowner to the lender. Requiring that refinance loans provide a net tangible benefit to consumers extends to the entire nation the benefits of state laws that have proven effective. Loan flipping has, since the beginning of the subprime market, been a prime tool for stripping the equity from homeowners. Not only are they effective in curbing the practice, but they have not resulted in reduced access to legitimate credit.[28]

6. The elimination of prepayment penalties in the subprime market removes the "exit tax" for borrowers seeking to refinance to better terms, and complements the prohibition on yield spread premiums.

The proposal would prohibit prepayment penalties in the subprime market, where they have been a linchpin of market abuses. Eliminating them would eliminate another of the perverse incentives in the subprime market.

Prepayment penalties are an unfair practice in the subprime market because they have provided no net economic benefit to consumers. Not only are prepayment penalties expensive, but they also significantly increase the possibility that a homeowner will face foreclosure. Industry representatives often claim that borrowers receive a reduction in interest rates in exchange for prepayment penalties, but in the subprime market, this is not typically the case. According to quantitative research conducted by CRL, not only do prepayment penalties lock borrowers into higher-cost loans or force them to give up the wealth they have built through homeownership, but they also offer no benefit in the form of lower interest rates.[29]

This finding is often confirmed in subprime rate sheets that lenders distribute to brokers to give up-to-date information on loan pricing. These same rate sheets show that brokers receive a "yield-spread premium" for charging a higher interest rate than the borrower qualifies for on mortgages, often only if the broker convinces the borrower also to accept a prepayment penalty. In this way, even if there is a nominal reduction in the interest rate due to the prepayment penalty, this is offset or more than offset by the higher rate due to the yield- spread premium. Then, once borrowers receive the loan, they are faced with the Hobbesian choice of remaining stuck in it and paying excess interest each year, or of getting out of the loan and forfeiting significant amounts of family wealth as a result. This situation has become more serious for families as property appreciation has slowed down in many areas of the country.

By prohibiting yield spread premiums generally, and prohibiting prepayment penalties in the subprime market, the bill would break the bonds of the glue that links prepayment penalties to steering.

B. The proposal addresses additional long-standing problems in the market.

1. The prohibition against mandatory arbitration on any residential mortgage loans opens the door to transparent, neutral avenues for relief.

The proposal restores arbitration to its proper place. It cannot be imposed in a contract of adhesion to close the door to the courthouse for consumers, yet it remains an option where both parties choose to resolve a dispute after it has arisen.

Many lenders have favored placing pre-dispute, mandatory binding arbitration clauses in their loan contracts, although, since Fannie Mae and Freddie Mac adopted a policy refusing to buy loans that included mandatory arbitration, this practice has decreased somewhat. Mandatory arbitration imposes high costs on consumers in terms of filing fees and the costs of arbitration proceedings.[30] But arbitration also imposes more harmful costs on consumer-lender disputes by limiting the availability of counsel, cutting off traditional procedural protections such as rules of discovery and evidence, slowing dispute resolution, and restricting judicial review.[31]

Lenders, the "repeat players" in arbitration, benefit unfairly from that status. In some cases, lenders have used the mandatory arbitration clause to designate an arbiter within the industry, producing biased decisions. Lenders also are able to use arbitration to handle disputes in secret, avoiding open and public trials which would expose unfair lending practices to the public at large.[32]

This situation has only been made worse as many mandatory arbitration clauses have been expanded to also contain provisions that waive the consumers' right to participate in class action suits against the lender, making it more difficult for smaller claims to prevail. For these reasons, mandatory arbitration clauses are unfair to consumers who have no choice but to sign adhesion contracts.

2. Firmly closing the door on the use of credit insurance products will prevent a resurgence of a favorite equity-stripping tool.

Again incorporating the experience from the state laboratories for reform, the proposal prohibits the financing of single-premium credit insurance. It further assures that new variants, such as "debt suspension" agreements, are not used to evade restrictions on credit insurance.

3. The expanded scope and protections to HOEPA will give much needed new protections to the highest-cost mortgage market.

As we noted earlier, these amendments to HOEPA are necessary responses to a market segment that has evolved significantly in the 13 years since HOEPA was enacted. We know these reforms work, as they build on the experiences of states.

Together with the other provisions of the bill, we believe that new standards applicable to all segments of the home mortgage market would be positive for homeowners, the communities they live in, the industry, and the economy. In substance, the reforms are a positive step forward.

C. The proposed remedies should be improved to assure both sufficient incentives for the market to fully comply with the reforms and to assure that consumers have the ability to vindicate their rights.

It is critical that the important reforms described above take deep root and change market behavior. We now know that they are critical for the protection of consumers, but for their neighbors, for their communities, for investors, and for the economy as a whole. This is a key piece of restoring trust in the market – a trust that has been shaken at home and abroad.

We fear, however, that there are insufficient remedies for consumers affected by violations of the law, and that there may be insufficient disincentives in the bill to effectuate the necessary change in market behavior.

1. Violations of the originators' duties, including the anti-steering provision, would leave the consumer in unsuitable, inappropriate, or unnecessarily costly loans.

The remedy for violations of the provisions established in Title I – the originators' duty of care, and the anti-steering provisions – is limited to Truth in Lending damages (as amended in this bill), up to a maximum of three times the originator's compensation.[33]

The damages claims may be difficult to pursue. These limited damages would be available against the originator. Unfortunately, many originators are thinly capitalized, or often do not remain in business long. While the bill would set up minimum bonding requirements of $100,000, in today's mortgage market that would quickly be eaten up. While the first dozen victims of a broker might recover, the next victim may well be out of luck. Further, as we mentioned above, over 100 major originators in the past year have gone into bankruptcy, gone out of business, or disappeared into other entities,[34] leaving it difficult, if not virtually impossible for the consumer to pursue the claim against the originator.

As we interpret the bill, possibly this violation could be asserted against an assignee only where the violation is "apparent on the face of the documents," although that is not clear.[35] (As the bill is drafted, it is unclear whether this general rule would apply at all to claims against originators who were not also "creditors" as TIL defines that term.) We are uncertain as to the value of the claim for damages for a violation of the anti-steering provision when the homeowner is trying to raise the violation in any way other than a separate lawsuit against the originator. Can it be raised against the holder of the mortgage, with damages to be credited against the loan balance? If so, can that be done as an affirmative claim? Or can it be raised only in response to impending foreclosure?

Given the difficulty of obtaining a judgment against a broker and collecting on it, we believe that it is imperative that the consumer be able, at a minimum, to be able to apply the benefit of the claim to the outstanding obligation. This would not expose the secondary market to unreasonable liability.

More critically, the consumer is left to live with the terms of the unsuitable, inappropriate, or most costly loan. Consider the situation of a borrower placed into a 9% fixed rate subprime loan for $150,000 by a broker who receives a total compensation equaling three percent, or $4500, though she would have qualified for a 30-year fixed rate prime loan at 6.5%. Her maximum damages are $13,500. Yet she still has that 9% loan. Over the full life of the loan, she would pay unnecessarily an extra $136,308 – more than 10 times the damages she received. Even if she were able to refinance at five years, the loss to her caused by the steering would be over $28,000 – more than double her damages under this proposal.[36]

To assure that that there are adequate incentives for compliance with the badly needed reforms in Title I throughout the market, and to assure that consumers get the benefit of the reform, we believe that it is necessary to add a reformation remedy, which allows the consumer to reform the terms of the loan *ab initio* to one that would have complied with the requirements of Title I.

2. The remedies for violations of the ability to pay and the net tangible benefit provisions are a good start, but need improvement.

As we understand the remedies available for violations of the provisions mandating the ability to pay and net tangible benefit, there's a "two-gate" system which consumers must be able to penetrate before obtaining relief. As we read the legislation, it would work this way:
There is an "outer gate" that the consumer must unlock -- the ""qualified safe harbor mortgage."[37]

A subprime loan is a "qualified safe harbor mortgage" when it:

* meets **either** of two core requirements:

  - fixed payments for minimum of seven years, **or**

  - in the case of an adjustable rate loan, the margin is less than 3% over a recognized index,

* **and** meets all five additional requirements: a) income and resources are documented and verified; b) underwriting is based on a fully-indexed rate and takes all insurances and taxes into account; c) results in a DTI of 50% or less, or other standards to be set by regulation; d) is not negatively amortizing, and e) meets other requirements set by regulation.

The impact of the fixed payment prong, it appears is that these requirements, for all practical purposes, will apply primarily to subprime adjustable rate mortgages. (As we noted above, unaffordable and no-benefit fixed rate mortgages have also been common in the subprime.[38])

As we understand the process, if the loan falls within this safe harbor, the consumer could pursue a claim for a violation against the **creditor**, if he is able to rebut the presumption created by the fact that the loan is in that "safe harbor." If he does successfully rebut it, then the remedy against a creditor appears to be the civil monetary remedies generally available for violations of TIL under Section 1640. It is our understanding that the intent of the drafters was to also make the rescission remedy available, although, as drafted currently, violations of Title II would not trigger the rescission right at all. (We understand that this will be corrected.)

However, if the loan has been sold on the secondary market, as the majority of loans are today, the consumer has **no** right to pursue a claim against the **assignee, securitizer, or holder.** It is not clear if the consumer can even pursue this claim in defense of foreclosure. But certainly short of foreclosure, there is no way for the consumer to unlock the gate and raise a violation of these two provisions against an assignee in if the loan meets this "qualified safe harbor mortgage" status. Hence little meaningful relief would be available to a consumer before losing the house, despite a violation of the law.

If the loan does not fall within the qualified safe harbor, the consumer is then confronted with a second locked gate. An assignee or securitizer is exempt from even limited liability if it meets a 3-pronged test: it has a policy in place of not buying loans that are not "qualified safe harbor mortgages" or subprime mortgages, exercises due diligence to make sure they do not, and obtains representations and warranties from the seller, then the consumer can do nothing but wait for foreclosure. An assignee or securitizer who cannot meet the test for exemption has a right to cure the loan.

If the consumer can get past those two separate gates, we understand that the remedy intended to be available against assignees or securitizers is rescission. However, the trust – the true owner of the loan at this stage – does not appear from the language to be considered an "assignee or securitizer – and so there is, in effect, yet another hurdle for the consumer. (The separation of trusts from "assignees" and securitizers will make the process very cumbersome.)

Ultimately, because of all these hurdles, the primary remedy for consumers whose loans have been sold on the secondary market will be the ability to raise violations of those provisions in defense to an impending foreclosure. Thus, only once foreclosure has been initiated can a consumer do anything to vindicate these rights where it counts – in connection with the loan itself. In other words, then and only then can the consumer assert Truth in Lending's rescission remedy. (Again, this assumes that the necessary technical corrections will be met. As released on October 22, this remedy would not be available at all.)

Unfortunately, this puts a consumer between a rock and a hard place***:*** she must tempt a foreclosure, entailing the consequent reduction in her FICO score which is likely to follow her for years, and may even make it harder for her to effectuate her rescission remedy by impeding her ability to tender.

Finally, no class actions are permitted for these violations against any assignee. The bill prohibits class actions for violations of these provisions. As a practical matter, with this protection and the other liability caps in place, there is no need for additional insulation from liability for the secondary market, much less the extraordinarily high level of insulation offered by this bill.

Reckless underwriting is at the heart of the recent crisis, and was as much a creation of the secondary market as the originators. We believe that the secondary market has too much insulation in this proposal for it to have adequate incentive for change, and consumers have too little opportunity to vindicate their rights. Yet we do understand that unlimited, uncertain exposure may have adverse effects.

Here, too, the experience of the states should prove instructive. In states with assignee liability in the context of subprime mortgages, the secondary market has continued to function – so well, in fact, that in some states the origination and subsequent securitization of such mortgages rose after the passage of the legislation imposing the liability. This effect may be because borrowers feel more comfortable accepting such loans when they know that anti-predatory legislation is in effect and can be enforced by private actors.

Indeed, the recent crisis of confidence in the rating agencies much vaunted ability to rate risk may well do the same. Investors may feel more confident in the force of law than in the now tainted ratings by a self-interested and self-dealing market.

As we have more time to study the proposed bill in depth, we will be happy to work with you in an effort to find the proper calibration.

3. The proposal to increase the amount of TIL monetary damages and permit rescission after three years is welcome.

Civil monetary remedies for TIL violations as applied to mortgages have been capped at $2000, and $1000 for other loans, since the 1970's,[39] an amount insufficient either to provide adequate deterrence for non-compliance or adequate relief for consumers. An increase in these remedies is long overdue, and we appreciate the leadership of the committee in bringing updating this aspect of the law

Similarly, we appreciate the recognition in the bill that a consumer who faces foreclosure 37 months into a loan needs to be able to assert rescission just as much as one who faces foreclosure 35 months into a loan.

Conclusion

Historically, the best interests of financial institutions and homeowners were closely aligned. When a home foreclosed, it was a loss not only to the family who lived in the home, but also to the lender who had provided the loan. Today, particularly in the in the subprime market we have a disconnect between these interests, and that needs to change. To restore the world's confidence in our markets and recover a reasonable expectation of integrity to our mortgage financing system, we need decisive policy actions to realign the interests of people who buy homes and institutions that provide the loans and the entities that invest in those mortgages. As long as subprime lenders have little or no incentive to make a loan successful, we will continue to push families back financially, and rather than building our nation's prosperity through homeownership, we will continue to lose economic ground.

The subprime lending system has failed millions of middle-class families. These are people who were trying to do everything right: they worked hard at their jobs, they took care of their children, and they were seeking a more secure future. Now these families are on the verge of losing any semblance of security, and we all will be worse off as a result. As outlined here, policymakers have a number of tools at their disposal to mitigate the harm caused by this situation and prevent it from happening again in the future. We strongly urge you to consider our recommendations for making a strong bill even stronger.

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[1] Ellen Schloemer, Wei Li, Keith Ernst, and Kathleen Keest, *Losing Ground: Foreclosures in the Subprime Market and Their Cost to Homeowners*, (December 2006) at http://www.responsiblelending.org/issues/mortgage/reports/page.jsp?itemID=31214551.

[2] *Losing Ground*, note 1.

[3] In addition, see Bob Ivry, "Subprime Borrowers to Lose Homes at Record Pace as Rates Rise," Bloomberg.com (September 19, 2007).

[4] Christopher L. Cagan, *Mortgage Payment Reset: The Issue and the Impact*, *First American CoreLogic* (March 19, 2007), available at http://www.facorelogic.com/uploadedFiles/Newsroom/Studies_and_Briefs/Studies/20070048MortgagePaymentResetStudy_FINAL.pdf

[5] Mortgage Finance Industry Overview, Lehman Brothers Equity Research (December 22, 2006).

[6] Robert B. Avery, Kenneth P. Brevoort and Glenn B. Canner, "The 2006 HMDA Data," Federal Reserve Board (September 12, 2007), available at http://www.federalreserve.gov/pubs/bulletin/2007/pdf/hmda06draft.pdf.

[7] Moody's Economy.com, "Into the Woods: Mortgage Credit Quality, Its Prospects, and Implications," a study incorporating unique data from Equifax and Moody's Investors Service (2007).

[8] We are unable to verify the extent of this problem because the MBA used proprietary data to make this claim.

[9] Mortgage Bankers Association Press Release "Investor Loans Major Part of Defaults in States with Fastest Rising Delinquencies" 8/30/2007, at http://www.mbaa.org/NewsandMedia/PressCenter/56535.htm

[10] See, e.g., "HomeRefi Now," American Fidelity Mortgage at http://www.homerefinow.com/mortgage-info/investor_loans.asp ("The fact is that the default rate on small investor loans is significantly higher than that of their owner occupied counterparts...").

[11] Jim Rokakis, "The Shadow of Debt: Slavic Village is Fast Becoming a Ghost Town," *Washington Post* (September 30, 2007).

[12] See, e.g., Nicola Clark, "Bank in Germany Posts Loss Because of Bad Stock Trades," *New York Times* (August 31, 2007); Jenny Anderson and Heather Timmons, "Why a U.S. Subprime Mortgage Crisis is Felt Across the World," *New York Times* (August 31, 2007). Indeed, the globalization of the consequences has left people on other continents asking for an international oversight role: "Why should the rules of lending in the U.S. be left to U.S. regulators when the consequences go everywhere?" Heather Timmons and Katrin Bennhold, "Calls Grow for Foreigners to Have a Say in U.S. Market Rules," *New York Times* C1, (August 29, 2007).

[13] Chairman Bernanke makes this point in a recent presentation: "Housing, Housing Finance, and Monetary Policy, remarks by Ben Bernanke, Chairman, Board of Governors of the Federal Reserve System at the Federal Reserve Bank of Kansas City's Economic Symposium – Jackson, Hole, Wyoming (August 31, 2007), pp. 16 – 17.

[14] "The Oracle Reveals All," *Newsweek* (Sept. 24, 2007) pp. 32, 33.

[15] *See, e.g.* Allan Sloan, "An Unsavory Slice of Subprime," *Washington Post* (October 16, 2007) ("Even though individual loans … looked like financial toxic waste," 68% of the issue was rated AAA.)

[16] Shannon D. Harrington and Mark Pittman, " Subprime Delinquencies Accelerating, Moody's Says," (October 5, 2007), available at http://www.bloomberg.com/apps/news?pid=email_en&refer=home&sid=a8Mzhz09jHP8

[17] Losing Ground, note 1 at page 21.

[18] Credit Suisse, *Mortgage Liquidity du Jour: Underestimated No More,* (March 12, 2007) p. 6.

[19] "S&P downgrades 1,713 classes of mortgage-backed securities issued in the first half of 2007," Associated Press (October 17, 2007).

[20] FBR Capital Markets, "Structured Finance Insights," FBR Investment Management, Inc. (September 28, 2007).

[21] FBR Capital Markets, note 14 at p. 2.

[22] Copies on file with the Center for Responsible Lending.

[23] Robert Couch testimony before the U.S. House of Representatives Financial Services Subcommittee (November 2003), cited in "Financial Education: No Substitute for Predatory Lending Reform," Issue Paper No. 7, Center for Responsible Lending (September 13, 2004).

[24] *See* Wei Li and Keith S. Ernst, *The Best Value in the Subprime Market: State Predatory Lending Reforms*, Center for Responsible Lending (February 23, 2006).

[25] I will not discuss this issue in this testimony, but would welcome the opportunity to expand on it following this hearing.

[26] As with the ability to pay, though included in protections available for "all loans", the operations of the proposed two safe harbors would, for the most part, mean that this functionally applies primarily to subprime adjustable rate loans, as we read the bill.

[27] *See, e.g.* Testimony of Michael Calhoun, Before the US Senate Committee on Banking, Housing and Urban Affairs; Subc. on Transportation, Housing and Urban Affairs, *Ending Mortgage Abuse: Safeguarding Homebuyers*, Appx 1, (June 26, 2007), *available a t*http://www.responsiblelending.org/pdfs/senate-testimony-m-calhoun-june-26-2007.pdf.

[28] *See* Wei Li and Keith S. Ernst, *The Best Value in the Subprime Market: State Predatory Lending Reforms*, Center for Responsible Lending (February 23, 2006)

[29] Keith Ernst, "Borrowers Gain No Interest Rate Benefits from Prepayment Penalties on Subprime Mortgages ," Center for Responsible Lending (January 2005).

[30] *See* Victoria Nugent, *Arbitration Clauses that Require Individuals to Pay Excessive Fees are Unconscionable,* THE CONSUMER ADVOCATE 8, 9-10 (Sept./Oct. 1999).

[31] Paul D. Carrington and Paul H. Haagen, *Contract and Jurisdiction*, 1996 SUP. CT. REV. 331, 346-9 (1996).

[32] *See* John Vail, *Defeating Mandatory Arbitration Clauses*, TRIAL 70 (Jan. 2000).

[33] The general TIL monetary damages include actual damages and statutory damages of $2000 for mortgage loans. Court interpretations, however, have recently made actual damages very difficult to win. *See generally* National Consumer Law Center, *Truth in Lending*,§ 8.5.4 (5th Ed. 2003). It is possible that violation of the duty, or of the steering requirement, will be more susceptible to actual damage awards by courts, but that remains to be seen if that is the test.

[34] A list was attached to the testimony of Martin Eakes before the Joint Economic Committee, pp. 28-41, (September 19, 2007.)

[35] As a general rule, except as otherwise specified, monetary remedies for violations of TIL's requirements can be brought against assignees only when the violation is "apparent on the face of the documents." 15 U.S.C. § 1641(a),(e). As the bill is drafted, it is unclear whether this general rule would apply at all to claims against originators. Indeed, it is unclear how this definition is intended to apply with respect to table-funded loans.

[36] During the first 60 months, the extra cost in monthly payments would be over $378, ($1206.93, compared to $828.30) for a total loss of nearly $22,800. The payoff balance after 60 months would be nearly $5600 more.

[37] We understand that the bill will be changed so that the prime loan "safe harbor" will no longer be a safe harbor. Instead, these two provisions will only apply to subprime loans in the first instance. This testimony assumes that change.

[38] Fixed rate mortgages were the standard first lien products for Household and Associates, both targets of public enforcement actions and much private litigation. Flipping and making loans with out regard to repayment ability was standard.

[39] 15 USC 1640(a)(2)(A)(i).