Chairman Schumer, Ranking Member Saxton, Vice Chair Maloney, and members of the Committee, thank you for holding this hearing to focus on how the alarming rate of losses on subprime mortgages is affecting consumers, the U.S. economy, and global financial markets. We commend you for focusing on the problem and seeking positive solutions.

I testify as CEO of 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. Self-Help has provided over $5 billion of financing to over 55,000 low-wealth families, small businesses and nonprofit organizations in North Carolina and across the country.

Self Help is a subprime lender, and our loan losses have been less than one percent per year. We are small compared to the commercial finance companies that have produced most subprime loans, but we, too, provide mortgages to people who have lower incomes and credit blemishes. The biggest difference is that we avoid making loans that begin, from the first day, with a high chance of failing; we assess whether the borrower can pay the loan back; and we structure the loan in a way that promotes sustainability. This is Risk Management 101, a course that lenders in the prime market have followed for decades.

In addition to my experience with Self Help, I am also CEO of the Center for Responsible Lending (CRL) (www.responsiblelending.org), 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 work with many other concerned groups to eliminate predatory lending practices and encourage policies that protect family wealth.

During these past few months—as subprime foreclosures shot up to alarming levels, as over 100 mortgage companies closed their doors and laid off tens of thousands of employees, as investments collapsed and banks on several continents felt compelled to take action—the mortgage industry has tried to downplay the enormous damage caused by reckless subprime lending.
I. State of the Market
Today I want to make these points:

- The rate of foreclosures on subprime loans is severe.
- The problem of foreclosures on subprime mortgages is widespread, and has already had a significant negative impact on people with and without subprime mortgages, as well as the economy at large.
- Subprime foreclosures will get much worse in the near future.
- Tightening of credit has been caused by an industry that has run too loosely and without sufficient regulation.
- Market forces are not correcting the situation.
- The impact on homeowners is devastating. We provide one real-life example out of millions.

II. Policy Recommendations
The good news is that workable solutions exist. On the most basic level, we need to ensure that lenders return to common-sense lending that is likely to produce sustainable homeownership. At the same time, we need to do all we can to minimize the damage to families who are struggling today. Our policy recommendations focus on two major areas.

A. Protecting Homeowners in the Future
First, we need strong predatory lending protections to protect homeowners in the future. These include a number of measures that have already been incorporated into state laws and/or guidance issued by regulators.

- Require lenders to determine that their customers have the ability to repay the loan at the fully indexed rate, assuming fully amortizing payments.
- Require lenders to verify a customer’s income using tax documents, payroll or bank records, or other reasonable documentation.
- Require lenders to escrow for real estate taxes and property insurance.
- Ban prepayment penalties and yield-spread premiums on subprime loans.
- Eliminate steering families into unnecessarily expensive loans.
- Hold lenders responsible for abusive lending practices, regardless of whether the loan was originated by the lender or mortgage brokers.
• Hold mortgage brokers accountable for abusive lending practices by establishing rigorous affirmative duties to serve the best interests of their customers.

• Through assignee liability, hold investors accountable for the loans they support.

• Allow the states to continue to take actions to prevent predatory lending.

B. Protecting Homeowners Now Threatened with Foreclosure
Second, we need to employ sensible strategies to minimize the devastation caused by bad loans that have already been made by helping families avoid foreclosure. In recent weeks, some have tried to frame sensible solutions as a “borrower bail-out.” This is absurd. First, any effective measures for addressing the foreclosure crisis will not only help homeowners, they will help entire communities and the nation’s economy as a whole. Second, no one is proposing to remove all debt obligations from homeowners—families will still need to make timely mortgage payments. We and other concerned groups are proposing policy solutions that center on these actions:

• Direct servicers and lenders to make meaningful and sustainable modifications to existing loans.

• Eliminate an anomaly in the Bankruptcy Code, which currently allows judges to modify unaffordable mortgages on a vacation home or investment property, but not on the homeowner’s primary residence.

III. State of the Market - Discussion
A. The foreclosure problem is severe.
Every credible quantification of subprime foreclosures reveals that the problem is severe. The 2nd Quarter National Delinquency Survey, recently released by the Mortgage Bankers Association (MBA), shows that foreclosures on all types of loans have increased, but, as expected, foreclosures in the subprime market are most severe. New foreclosures on subprime adjustable-rate loans in the second quarter 2007 are 90% higher than the same time last year, compared with a 23% increase on prime fixed-rate loans.
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”) estimating that one out of every five subprime mortgages made in 2005 and 2006 ultimately will end in foreclosure. This projection refers to actual homes lost, 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. Even today, the Mortgage Bankers Association continues to insist that the foreclosure problem is relatively small, and that only about 250,000 households with subprime mortgages will lose their homes. Their figure comes from a mis-reading of the research described in the Losing Ground report. As shown here, CRL’s estimate is in line with other credible projections:

<table>
<thead>
<tr>
<th>Source</th>
<th>Loans Analyzed</th>
<th># Loans in Analysis</th>
<th>Projected Foreclosure Rate</th>
<th># Projected Foreclosures</th>
</tr>
</thead>
<tbody>
<tr>
<td>MBA</td>
<td>Not disclosed</td>
<td>Not disclosed</td>
<td>Not disclosed</td>
<td>250,000</td>
</tr>
<tr>
<td>CRL</td>
<td>Subprime loans, owner-occupied properties, 2005 &amp; 3Qs 2006</td>
<td>5,800,000</td>
<td>19.4%</td>
<td>1,125,000</td>
</tr>
<tr>
<td>First American Real Estate Solutions</td>
<td>All adjustable rate mortgages issued in 2004 &amp; 2005</td>
<td>7,700,000</td>
<td>14.3%</td>
<td>1,100,000</td>
</tr>
<tr>
<td>Lehman Brothers</td>
<td>Subprime loans, 2006 vintage only</td>
<td>4,000,000</td>
<td>30%</td>
<td>1,200,000</td>
</tr>
<tr>
<td>Moody’s Economy.com</td>
<td>All loans</td>
<td>Not disclosed</td>
<td>Not disclosed</td>
<td>1,700,000</td>
</tr>
</tbody>
</table>
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 live 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**. In essence, the MBA’s defense of a dismal situation is, “The house is on fire, but the temperature has dropped by three degrees in most rooms.”

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 (e.g. low downpayments, 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 in the same market:

<table>
<thead>
<tr>
<th>% of Outstanding Loans in Foreclosure at end of 2Q 2007</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
</tr>
<tr>
<td>Northeast</td>
</tr>
<tr>
<td>North Central</td>
</tr>
<tr>
<td>South</td>
</tr>
<tr>
<td>West</td>
</tr>
<tr>
<td>United States</td>
</tr>
</tbody>
</table>

*Source: MBA National Delinquency Survey, 2Q 2007*

Lastly, the MBA has claimed that defaults on non-owner occupied properties are the major driver for increased subprime foreclosures. However, 88% of foreclosures are suffered by people living in their primary residence. A higher rate of foreclosures on investor properties is not a new development—default risks have always been
significantly higher for investor properties compared with owner-occupied homes. 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.

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. (See Appendix 1 for a list of mortgage firms sold, closed, or bankrupt as of the end of August, as well as a list of other financial transactions affected by the credit crunch.)

C. Subprime foreclosures will get much worse in the near future.

It is important to recognize that while the rate of subprime foreclosures is alarming today, the worst is still ahead. With as many as 1.7 million foreclosures predicted to occur in the next two to three years, it is imperative that Congress take action to assist homeowners struggling today, not just protect future subprime borrowers.

Even with the recent modest cut in interest rates, many subprime borrowers will face 40 percent or greater increases in their monthly mortgage payments once their initial “teaser” rates expire and their fixed interest rates reset into higher-rate variable rates. As the chart below shows, a large majority of these rate resets will occur in early 2008.
D. Tightening of credit has been caused by an industry that has run too loosely and without sufficient regulation.
The mortgage industry has argued for years that regulation of subprime lending would have the unintended consequence of restricting credit. Today it is apparent that the current tightening of credit has been caused by 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 in the prime market have always followed—it is safe to say we would have avoided the massive problems we are seeing today.

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 Cohort13
(Positive numbers indicate higher risk, after controlling for borrower credit scores)

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

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 loans 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%.
Testimony of Martin Eakes – Sept. 19, 2007

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 that are not already stretched to make their payments or those who 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 (currently 12% plus). 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.”

For the past decade, subprime lenders have been aggressively marketing these dangerous loans and touting the easy availability of mortgages. Now, because of their actions, the market is tighter for everyone.

E. Market forces are not correcting the situation.
Normal market forces are not correcting the subprime crisis. That’s because the subprime mortgage market as currently structured doesn’t have adequate incentives to police itself; in fact, subprime lenders continue to have strong incentives to make harmful loans. Consider these facts:

- Mortgage brokers, who make approximately 70% of subprime mortgages, are not required to offer loans that are in the borrowers’ best interests.
- Subprime mortgage lenders provide financial incentives (compensation for interest rate bumps, called “yield-spread premiums”) to mortgage brokers for putting borrowers in higher interest loans than they deserve. Lenders also provide brokers incentives to include prepayment penalties costing thousands of dollars and carrying significantly higher chances of foreclosure.
- Lenders, until recently, reaped huge profits by ignoring a homeowner’s ability to repay the loan and/or neglecting to document the homeowner’s income.
- Unscrupulous lenders gain a competitive advantage over honest lenders when they exclude the costs of taxes and insurance from monthly mortgage payments.
- Lenders make more money when they steer people into subprime loans – even when those people are qualified for a lower-cost prime loan.
- Since loans typically pass from brokers to lenders to investors, it has been easy to avoid accountability for abusive mortgages.

All of these market incentives point in one direction: If the subprime market continues running without any rules, borrowers will continue to receive abusive loans that lead to foreclosure. The market may tighten up temporarily, but with these perverse incentives firmly in place, future abuses are inevitable.

We support responsible subprime lending, in fact, we’ve done it since 1985, but we are opposed to the reckless way that subprime lending has been conducted in recent years. When subprime mortgages are made with care, they are a valuable tool for giving
families a secure foothold in the middle class. Sustainable homeownership is one of the best options for helping struggling families. But offering a false promise of homeownership is like serving tainted water. If we care about sustainable homeownership, and if we want good credit to be more abundant in the future, then we need to require lenders to return to common-sense loan assessments.

**F. The impact on homeowners is devastating.**

The subprime meltdown has affected markets around the world, but the markets are likely to recover faster and more completely than families who lose their homes to foreclosure. Consider the case of the McGowan family in Gastonia, North Carolina, who recently lost their home to foreclosure in spite of all their best efforts to make payments on a loan they never should have received. Butch McGowan worked as a fire fighter for many years and his wife, Cynthia, was a police dispatcher. They have two children, including a daughter who has had multiple brain surgeries. They have no credit card debt, but because of their health issues, they have carried debts related to medical expenses.

The McGowan family desperately wanted a home of their own, and in 2006, they were very excited when they were told they qualified for financing. When they went to close on the loan, they were expecting to receive a fixed-rate mortgage with an interest rate of 6.75%. Instead, the lender rushed in late and said, “9.75% is the best we can do. Oh, and by the way, the rate will go up even higher in six months – but don’t worry you can refinance.”

“You can refinance” became the refrain of subprime lenders during the lending frenzy we have experienced during the past few years. Homeowners were told not to worry about loans that would have unaffordable increases in interest rates because “you can refinance.” Lenders continued to say this even when concerns about an overheated housing market were pervasive and even when it was doubtful that borrowers would have enough equity to support a refinance. Subprime lenders didn’t have anything to lose. If they could refinance the borrower, they made more money. If a refinance wasn’t possible—which is often the case when prices flatten or drop—well, it was unfortunate, but it didn’t really affect the lender, since they had long ago sold the loan to Wall Street. These practices eventually caught up with virtually all stand-alone subprime lenders over the past several months, but that is small consolation to the McGowans and millions more like them.

To make matters worse for the McGowans, they were told their mortgage payment included property taxes and hazard insurance, but it did not. Even knowing that the McGowans were on a limited, fixed income, the lender failed to escrow for costs the family would be required to pay. The McGowans closed on their mortgage thinking they could somehow find a way to manage a loan at 9.75% until the promised refinance came through. But adding taxes and insurance on top of an expensive loan tipped them over the edge, and even though Mr. and Mrs. McGowan tried their best, they simply couldn’t make the payments. The McGowans have used up all their retirement funds, and they are never sure from one week to the next they will have enough money for groceries.
Mrs. McGowan sums up the situation when she says this: “The only thing I wanted to do is to try to fix something for my children to have after we are gone. And now that we’ve used all of our 401Ks and 457s, there is not much left if we can’t hold on to something.”

IV. Policy Recommendations - Discussion

It is not too late to help families such as the McGowans, and also to prevent abusive subprime mortgages in the future. Both the Federal Reserve Board and Congress have authority to make lenders accountable for reckless lending that harms homeowners, businesses, and investors. As described earlier, the market is structured in a way that encourages brokers and lenders to ignore the quality of mortgage loans and their likelihood of success. These perverse incentives call for reasonable, common-sense interventions.

Our policy recommendations focus on two major areas. First, we need strong predatory lending protections to help homeowners in the future. These items, listed in our summary, include a number of measures that have already been incorporated into state laws and/or guidance issued by regulators.

Second, we need to employ sensible strategies to minimize the devastation caused by bad loans that have already been made by helping families avoid foreclosure. In recent weeks, some have tried to frame sensible solutions as a “borrower bail-out.” This is absurd. First, any effective measures for addressing the foreclosure crisis will not only help homeowners, they will help entire communities and the nation’s economy as a whole. Second, no one is proposing to remove all debt obligations from homeowners—families will still need to make timely mortgage payments. We and other concerned groups are proposing policy solutions that center on these actions:

We discuss these recommendations in more detail in the following sections.

A. Avoiding Tomorrow’s Crisis: Preventing Future Foreclosure Epidemics and Associated Losses.

Today’s crisis in the subprime market was driven by three core market failures. First, the subprime industry forgot the fundamentals of its own business—it failed to underwrite the loans, and failed to assess whether there was an ability to pay the loan. Second, this market lacked competition in the traditional sense. Rather, there were perverse incentives to compete for the business of the middlemen, and for the middlemen to deliver to investors higher-priced and more dangerous products. Finally, the subprime mortgage market lost accountability. Both legal accountability and the accountability resulting from market discipline disappeared into a vacuum created by lack of regulation and securitization. Here we propose reforms that would address each of these issues.

To restore common sense underwriting and assure ability to pay:
• Require lenders to determine that the borrower has the ability to repay the loan at the fully indexed rate, assuming fully amortizing payments. The payment shock associated with adjustable rate or non-fully amortizing loans must be taken into account.

At a minimum, underwriting on adjustable rate mortgages must assess ability to pay on a fully-indexed interest rate, assuming fully amortizing payments. Common public understanding of the mortgage system assumes that lenders underwrite loans and would not make loans to borrowers who do not have the ability to repay them. In the face of an increasingly complicated market and complex products, this reliance on the expertise of the originator and underwriter is not only understandable, it is important for the efficiency and credibility of the industry. This is the case whether the loan is originated by the lender or by a broker.

Federal banking regulators issued strong guidance requiring depositories and their affiliates to underwrite loans at the fully indexed interest rate to ensure that borrowers will be able to repay their mortgages. We need a clear standard in place that applies that same concept to the whole subprime market. Congress should provide a clear guideline for lenders by setting a rebuttable presumption that a debt-to-income ratio (encompassing a family’s housing expenses and all other monthly obligations) of 50% or higher is unaffordable. Without a debt-to-income ratio presumption, lenders can simply increase their debt-to-income ratio lending standards commensurately to underwriting to the fully indexed rate, to a clearly unaffordable level, and then argue that they met the fully indexed standard.

Legislation requiring the determination of a borrower’s ability to repay should be based on these principles:

(1) Lenders must consider an applicant’s ability to repay the loan according to its terms and based on a fully-amortizing repayment schedule.

(2) The debt-to-income ratio must include all debt payments, including total monthly housing-related payments such as principal, interest, taxes, and insurance, and both first and subordinate liens.

(3) Lenders can, on a case-by-case basis, rebut the debt-to-income presumption by showing that the consumer has other verified resources for making loan payments, and/or that there is a specific basis for lowering the consumer’s expenses, and that there are adequate resources available to cover family living expenses after deducting debt service requirements from monthly income. When underwriting its home loans, the Veterans Administration uses a similar approach that allows lenders to consider a number of factors to justify decisions that would normally fall outside established guidelines.

• Require lenders to verify borrower income using tax documents, payroll or bank records, or other reasonable documentation.
Most people can readily document their income using W-2s, 1099s or tax returns, but there are strong incentives for all parties involved to avoid documentation and inflate a loan applicant’s income: Borrowers are able to qualify for bigger loans; brokers receive higher yield-spread premiums for pushing the higher interest rates that comes with stated-income mortgages and by not having to do the work to verify incomes; and lenders and brokers both collect hefty fees with each later refinancing of these unaffordable loans. Inadequate documentation compromises a lender’s ability to assess the true affordability of a loan and makes any reported debt-to-income ratio meaningless. For the small minority of people who can’t use standard documentation, lenders should require bank records or other reasonable verification.

- Require lenders to escrow for real estate taxes and property insurance.

Failing to escrow for taxes and insurance on a subprime loan is an unfair and deceptive practice that contributes to high rates of foreclosure. Requiring such escrows is the norm in the prime market and is rare in subprime. This has distorted the subprime market by making it difficult for responsible lenders to compete. By creating artificially low monthly payment figures, the failure to escrow deceives consumers about the actual cost of these mortgages relative to those offered by competitors that do escrow. Consumers are frequently lured into higher cost or unaffordable loans by misleading comparisons of lower payments that exclude taxes and insurance with payments that include those costs. Non-escrowing lenders have benefited financially from the deception.

To correct distorted pricing incentives and encourage a truly competitive marketplace:

- Ban prepayment penalties and yield-spread premiums on subprime loans.

Prepayment penalties—the “exit tax” for refinancing or otherwise paying off a loan—are a destructive feature of the subprime market that lock borrowers in to high-cost loans, and make it difficult for responsible lenders to refinance them into lower-cost loans. Today prepayment penalties are imposed on about 70 percent of all subprime loans, compared to about 2% of prime loans. This disparity belies any notion that subprime borrowers freely “choose” prepayment penalties. All things being equal, a borrower in a higher-cost loan, or in an unpredictable, adjustable rate loan with a very high margin, would not choose to be inextricably tied to that product by a high exit tax. With common formulations of 6 months’ interest, or amounts of approximately 3% of the principal, the amount of equity lost is significant. For a $200,000 loan, a 3% prepayment penalty costs borrowers $6,000, eating almost entirely the median net worth for African American households.

It has long been recognized that prepayment penalties trap borrowers in disadvantageous, higher cost loans. Indeed, this is the penalty’s purpose – in industry parlance, to “build a fence around the borrower” or “close the back door.” Less well known is the fact that these penalties also increase the cost of the loan at origination because they are linked to
higher rates on loans that pay higher so-called “yield-spread premiums” to brokers.\textsuperscript{30} Thus, contrary to the claims of some lenders, prepayment penalties do not decrease, but, rather, frequently increase the cost of subprime loans.

Yield-spread premiums are a bonus paid by the lender to the mortgage broker as a reward for placing the borrower into a higher cost loan than the borrower qualifies for. Lenders are willing to pay the premium only where they are sure that the borrower will remain in the higher-cost loan long enough to enable the lender to recoup the cost of the premium from the borrower. This is not a theoretical concept; the evidence is clear from examining “rate sheets,” information lenders distribute to mortgage brokers showing which loan products the lender is willing to offer at different interest rate levels for borrowers that represent different credit risks. These sheets also indicate the yield-spread premium the lender is willing to pay.

We provide an example of a recent rate sheet (September 2007) in the appendix. As you can see, the rate sheet shows that the broker collects a 50 basis point (0.50\%) yield-spread premium (called a “rebate” on this rate sheet) for adding 1\% to the borrower’s interest rate. The broker collects an additional 75 basis point yield-spread premium for adding an additional 1\% to the borrower’s interest rate. Thus, with a $200,000 subprime loan, for the broker to receive a 2\% yield-spread premium, or $4,000, the borrower pays 1.25\% more than she actually qualified for, or $10,000 in excess interest expense if he or she stays in the loan for four years. The broker maximizes his compensation by seeking the lender and the loan that allow for the maximum return to him.

It is important to note that this lender reduces the yield-spread premium if the borrower pays a higher interest rate to “buy out” the prepayment penalty—in many cases lenders do not allow the broker to get any yield-spread premium if the loan has no prepayment penalty. Yield-spread premiums and prepayment penalties are intertwined in a way that is harmful to consumers and detrimental to competition (for a fuller discussion of these issues, please refer to our recent comment letter to the Federal Reserve Board, submitted on August 15).\textsuperscript{31}

Thus, the yield-spread premium puts the broker in a direct conflict of interest with the client borrower. Yield-spread premiums and prepayment penalties both substantially undercut the benefits of homeownership by stripping equity from the borrower. Prepayment penalties lock the borrower into a higher-cost loan, strip further equity upon refinance, and have been documented to increase the borrower’s vulnerability to foreclosure.

- **Eliminate steering homeowners into unnecessarily expensive loans.**

The subprime market has long cited “riskier borrowers” or “credit-impaired borrowers” as its justification for the higher prices on these loans. The argument is that investors need the higher prices to justify their risk, yet that extra price burden for the subprime loan puts credit-strapped borrowers that much closer to the edge.
That is one reason why, as we can now see, it serves the interest not only of homeowners, but of the world economy, to assure that all families seeking loans who qualify for lower-cost prime mortgages should receive a prime mortgage, not a subprime loan. We know that far more people have been placed in high-cost loans than should have been.32 Since it is now abundantly clear that “risky loans,” as much or more than “risky borrowers,” are a threat, market professionals – loan originators, whether brokers or retail lenders – should be required to assure that borrowers are put into the rate they qualify for. Market incentives that encourage originators to put as many people as possible into the priciest (and most dangerous) loans possible helped make this problem; prohibiting those incentives is a necessary part of the solution.

Eliminating the practice of steering borrowers to pricier and riskier loans is also critical to assuring a fair marketplace that does not impose a discrimination tax on borrowers of color. We know that for borrowers of color, the odds of receiving a higher-cost loan are greater, even after controlling for legitimate risk factors.33 We are long past the time when we can – or should – close our eyes to this.

**Finally, to restore accountability to the process, we recommend:**

- **Hold lenders responsible for abusive lending practices, regardless of whether the loan was originated by the lender or mortgage brokers.**

As the market operates today, lenders can benefit from abusive loans made by brokers without any adverse consequences. We believe the subprime market will remain a dangerous place for families until lenders are responsible for abusive subprime loans, regardless of whether they originated the loan directly, or whether they acquired the loan through a broker. The lack of accountability for lenders leaves homeowners without adequate remedies. Brokers are commonly thinly capitalized and transitory, leaving no assets for the borrower to recover against. Unclear lender liability means that homeowners face nearly insurmountable legal hurdles in trying to defend their home against foreclosures caused by broker lending abuses.

Lenders, who are mortgage professionals themselves, as well as repeat users of brokers’ services, have the expertise, the leverage and the capacity to exercise oversight of the brokers with whom they do business. Consumers do not. Indeed, the agencies have acknowledged that lenders must engage in just such oversight. The costs of their failure to do so should therefore be borne by lenders, not borrowers.

- **Hold mortgage brokers accountable for abusive lending practices.**

Nor should mortgage brokers be allowed to shirk responsibility for their actions. The broker has specialized market knowledge that the borrower lacks and relies on. And brokers hold themselves out to borrowers as a trusted adviser for navigating the complex mortgage market; why otherwise would a person engage and pay for one? Merely licensing mortgage brokers is insufficient – brokers must have affirmative duties to their customers to turn the tide of abusive lending practices. We commend Senators Schumer, Brown and Casey for introducing the Borrower’s Protection Act of 2007, which offers
key protections that would help hold brokers accountable for abusive practices including establishing a fiduciary duty between brokers and their customers, and a duty of good faith and fair dealing standard for all originators. An additional route for Congress would be to dramatically increase the bonding requirements for mortgage brokers.

- **Hold investors accountable for the loans they support through assignee liability.**

Assignee liability permits homeowners to pursue legal claims against the assignee (the party that has purchased or otherwise taken an interest in the loan) when the loan transaction involves illegal actions or abusive terms. Without it, borrowers are often left without recourse for predatory lending abuses, while retaining the risk of losing their home to the current holder of the predatory note. Since three-quarters of subprime home loans are sold on the secondary market, assignee liability is a critical component of any meaningful market reforms.

All parties that benefit from subprime mortgages should be held accountable. Without legal liability for assignees, a family that has been the victim of a predatory loan cannot stop the foreclosure of their home even if the originator is solvent and well-capitalized. Instead, they end up losing their home, and then they must bring a separate action against the originator. This separate action can take years.

Assignee liability also protects the integrity of the market, providing incentives to police itself, thus curbing inefficiencies. By assuring assignee liability, the law helps to protect responsible investors from misperceived risks and provides incentives for the market to police itself, curbing market inefficiencies. No one is more effective than investors who face financial and legal risk in ensuring that loans are originated to specified standards. It cannot be stressed too much that freeing investors from liability for the mortgages they purchased contributed to the disregard of lending standards that brought about the current crisis.

For example, shielding assignees from liability leads directly to a situation where loans without documented income become more desirable to investors than appropriately-documented loans. Investors’ willingness to pay more for “no doc” loans led loan originators to encourage borrowers to accept such loans rather than appropriately document their income. As the chief executive officer of the now bankrupt Ownit Mortgage Solutions explained when he acknowledged the lowering of underwriting standards, “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?’ The reason investors were happy to pay more for riskier loans was that they were shielded from liability for the consequences. Restoring appropriate assignee liability would help ensure that when investors accept mortgages, with all the corresponding financial benefits, that they also accept the corresponding responsibility.

- **Buttress, but do not impede, the states’ efforts to prevent predatory lending.**

It is imperative that the federal standards set the floor, not the ceiling, on lender conduct. It is a common refrain that we have a “national mortgage market” so we need national standards. But we do not have a national mortgage market. We have a national market—
indeed, we have an international market—in pieces of paper traded around the world. But somewhere down at the bottom of many tiers of “structured finance,” that paper is someone’s home. And there is nothing more local than a home and the neighborhood in which that home is located.

Different parts of the country were subjected to different aspects of the predatory lending problem at different times. In the regions where property values were ballooning, inflated appraisals were not a problem; in regions where property values were stagnant, inflated appraisals were a pervasive and serious part of the problem. Purchase loans with low down payments or high LTV refines were not as serious a threat in areas where the property values were on a steeply upward slope, since a struggling homeowner could refinance or sell. But in areas where property values were stagnant, or appreciating only marginally, the “foreclosure crisis” – and the loans that caused them – is old news.

States are more nimble and more able to accurately target specific problems than federal policymakers and the states have served as valuable laboratories of democracy to inform Congress’ decisions. The last time Congress addressed the predatory lending problem was 1994. The states have been addressing the issues as they arise, all along. Imagine how much worse the present crisis would be if many of the states had not acted in the meantime, and how less well informed Congress would be of what solutions to offer if the states hadn’t been implementing them. Ohio should not have to wait to respond to its crisis until California starts feeling it. Congress should not hamstring the ability of the states, the true “local cops on the beat,” to respond to the calls of distress in their communities.

B. Mitigating the Consequences of Today’s Crisis: Recommendations to Help Current Homeowners

- Direct servicers and lenders to make meaningful and sustainable modifications to existing loans.

The best and most effective help for homeowners placed into loans they cannot afford is for the lender or servicer to modify the loan terms to make them sustainable. This is hardly a give-away, since even lending industry leaders have acknowledged that many of these borrowers qualified for sustainable, 30-year fixed rate subprime mortgages, typically at a cost of only 50 to 80 basis points above the introductory rate on the unsustainable exploding ARM they were provided. In fact, a review of a broad array of lender rate sheets establishes that those borrowers who were given “no doc” loans notwithstanding their ability to document their income could have received 30-year fixed rate fully documented loans at a lower rate than the no-doc 2/28 adjustable-rate mortgages they received. And this does not include the 20% or so of subprime borrowers who qualified for conventional loans from the beginning.

In our estimation, 20% of existing homeowners—those who were able to repay their loans before their rates reset but could not refinance to conventional loans—could save their homes if their current “teaser” interest rate was fixed at that rate. For another 20%
of borrowers—those unable even to pay the teaser rate because they were placed into stated income loans they couldn’t afford, or the cost of taxes and insurance had not been factored in, for example—reducing the principal balance or interest rate up to 50% would make it possible to afford the lowered payments on the reduced loan balance, refinance the loan, or sell.

We believe that, at a minimum, servicers should do such a modification whenever the borrowers’ debt-to-income ratio, including other debts and including escrows, exceeds 50% upon reset. Reducing the interest rate or principal by half would provide the lender with the likely value they would obtain through foreclosure, including foreclosure expenses. Moreover, replacing anticipated foreclosures with modifications would avoid the rash of foreclosures that would produce further home price declines.42

Some lenders have reported to policymakers that they are currently offering loan modifications to troubled borrowers. The housing counselors, community groups and consumer lawyers we hear from tell us that in the vast majority of cases this is not so.43 We also are hearing that in the minority of cases where modifications are offered, they are limited to a one-year or even a six-month extension of the introductory interest rate, a modification that is too short-term and unsustainable to allow a family to engage in meaningful planning for their financing, housing and children’s schooling. Sustainable, meaningful loan modifications would ideally last for the life of the loan but certainly no shorter than five years.

A related and critical concern is that different borrowers will be treated differently (for example, those who cannot afford legal representation may be at a distinct disadvantage and may not be offered the same, or any, options). One need is to standardize the loan modification process to ensure fairness and efficiency.

Finally, when approximately two million households face the threat of foreclosure, any case-by-case resolution will be inadequate. Congress has the power to authorize a number of effective actions to support sustainable homeownership and should take the following steps to maximize the number of borrowers who receive help:

**Loss Mitigation:** The federal regulators have issued a call to lenders and servicers to engage in loss mitigation efforts prior to pursuing foreclosure. But more concrete steps are needed. To adequately stem the tide of foreclosures Congress should act to require specific loss mitigation efforts prior to any foreclosure filing and establish that failure to provide such loss mitigation can be used as an affirmative defense against foreclosure. Legislation such as Senator Reed’s Homeownership Protection and Enhancement Act (S.1386) is a step in the right direction as it would make important inroads on foreclosure prevention by creating an affirmative duty for lenders and servicers to engage in some loss mitigation efforts prior to foreclosure.

**Counseling and Legal Assistance:** Congress can also play a vital role in helping homeowners navigate the complicated process as they work to keep their homes. For example, Congress should provide additional funding for qualified and trained counselors
and legal advocates, and lift the restraints on legal services-funded programs from collecting attorneys’ fees when defending foreclosures. There is also an urgent need to fund for housing counselors and lawyers for low-income homeowners to help them negotiate work-outs with lenders and navigate tax and bankruptcy issues.

Data: To assist policymakers, industry and consumer groups in devising meaningful policy alternatives, more data is urgently needed. Congress should require servicers to report to a central database each time a modification is offered, describing the nature of the modification and how long it is effective. Servicers also should report when lenders pursue foreclosure or collection litigation without first offering a loan modification to the homeowner. Knowing how often servicers modify loans, and what these modifications consist of, is at least as important as knowing origination data reported by HMDA.

FHA support: Another important step is increasing the Federal Housing Administration’s capacity to insure abusive subprime mortgages that can be refinanced. The President’s proposals for the FHA provide a helpful starting point, but we shouldn’t be under any illusions that they alone will substantially address problem.

However, even if we take these steps to encourage loan modifications, the epidemic of subprime foreclosures is much too massive to be handled by these mechanisms alone. To further mitigate the damage caused by unsustainable subprime mortgages, we strongly recommend two further legislative solutions—one to correct an anomaly in the Bankruptcy Code, and another to correct an anomaly in the Internal Revenue Code.

- Most importantly, eliminate an anomaly in the Bankruptcy Code, which currently allows judges to modify mortgages on a borrower’s vacation home or investment property, but not on the homeowner’s primary residence.

Bankruptcy has served as a safety net in the past for borrowers as an option of last resort, but for struggling homeowners, it has become a serious obstacle to recovering from foreclosures. The problem is that Chapter 13 of the Bankruptcy Code – the Chapter that applies to consumer bankruptcy reorganizations where borrowers go on a payment plan – makes the home mortgage virtually the only debt that the court cannot modify and therefore the home the only asset it cannot protect. Since a home is typically the largest and most important asset a family has, and the home mortgage loan is the family’s largest single debt, the exclusion of the principal residence from modification prevents bankruptcy protection from reaching where it is needed most. Bankruptcy is a critical tool to help homeowners, it is an efficient mechanism and is, from a government perspective, a solution that does not require direct appropriations.

The current bankruptcy language dates back to 1978. It was indefensible policy then; a family’s personal residence should be their most protected asset in bankruptcy, not the least. This provision is particularly harmful today, however, as exploding ARMs are the single most important factor causing financial crisis for millions. In fact, hundreds of thousands of families face rate resets at the same time that their houses are worth less than the balance on their mortgage. Thus, they cannot sell their house or refinance their
loan. Some will receive loan modifications from their servicers, but for a number of reasons, most will not. Unless Congress passes the Act, these families will lose their homes.

Eliminating this anomaly would not require Congress to revisit the 2005 amendments to the bankruptcy code. In fact, those amendments were intended to encourage debtors to file under Chapter 13. But as currently drafted, Chapter 13 has rendered Bankruptcy Courts powerless to provide relief at a time when it is so urgently needed.

Not only is current bankruptcy policy unwise; it is unjust. Because the home mortgage exception applies only to primary residences, borrowers wealthy enough to own two homes can obtain relief from the mortgage on their vacation or investment home, thereby retaining at least one shelter for their family. Nor does the exception apply to the homes of family farmers, who file under Chapter 12, or to commercial real estate owned by businesses filing under Chapter 11. The law thus deprives mostly low-wealth and middle class families of protections available to all other debtors. If the borrowers cannot restructure these debts, then they can neither save their home nor get back on their feet financially.

The crux of the problem is found in section 1322 of the Bankruptcy Code, which should be revised, very simply, as follows:

1322 Contents of plan

(b) Subject to subsections (a) and (c) of this section, the plan may –

(2) modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor’s principal residence, or of holders of unsecured claims, or leave unaffected the rights of holders of any class of claims;

A narrowly-tailored amendment to the Bankruptcy Code soon to be introduced by Senator Durbin, and under consideration by other members, would correct this anomaly in a measured way that would provide urgently needed relief. It could help more than 600,000 of these financially-troubled families keep their homes by giving bankruptcy judges the authority to modify these mortgages in Chapter 13. In addition, it would save American families facing foreclosure $72.5 billion in wealth by avoiding 600,000 foreclosures by their neighbors. Finally, it would still guarantee lenders at least the value they would obtain through foreclosure, since a foreclosure sale can only recover the market value of the home. In addition, it would save lenders the high cost and significant delays of foreclosure.

- Eliminate an anomaly in the Internal Revenue Code, which does not tax homeowners on the first $500,000 (for couples) they earn when they sell their home at a gain, but does tax homeowners when the lender declines to sue them for any balance due when the home is sold at a loss.
Consistent with the long-standing American policy of encouraging home ownership, the Internal Revenue Code provides a generous tax break – even beyond the well-known mortgage interest deduction – for homeowners fortunate enough to sell their homes at a price in excess of what they paid. Each taxpayer can write off – that is, they are excused from paying taxes on – $250,000 worth of profits they make on the sale of their home. Couples get to write off $500,000 in profits.

However, while the law is extremely generous with families that make money on their homes, it is remarkably ungenerous with those that lose. Under current law, where a homeowner owes the bank more than the home is worth, and is in sufficient financial trouble that the bank relinquishes its claim for the excess balance over the home’s value, the federal government taxes the homeowner on this excess. This is so even where the borrower loses the home in foreclosure.48

Given a policy that provides homeowners with a tax exemption for up to a half-million dollars in homeownership-related gains, it is deeply unjust to refuse a comparable exemption for families facing homeownership losses. A recent proposal by President Bush and bills introduced by Representative Andrews and Senator Stabenow partially address the problem. To impact more than a minority of financially troubled homeowners, the bills should also be revised to cover loan balances incurred through so-called “cash-out refinancings” – refinancings encouraged by government officials. Most subprime loans over the last several years were cash-out refinancings, cash which often went to pay high broker and lender fees.49 Additionally, the bills need to be revised to ensure that they relate not only to tax forgiveness upon the sale of the home, but also tax forgiveness through modifications that enable the homeowner to keep the home.

**Conclusion**

Not so long ago, the best interests of financial institutions and homeowners were 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 and held onto the loan. Today 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, 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 set 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. The losses in wealth to neighbors, through the negative impact of foreclosures on property values, is even larger.

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 take our recommended actions to protect homeowners and promote sustainable homeownership.
END NOTES


3 Mortgage Finance Industry Overview, Lehman Brothers Equity Research (December 22, 2006).


6 We are unable to verify the extent of this problem because the MBA is using proprietary data to make this claim.


8 For example, Genworth Mortgage Insurance's "A-Minus Rate Sheet" dated December 1, 2005 shows a 0.5% premium for investor loans added to a base rate of 1.66% annually for coverage on a 90% LTV A-minus loan with a credit score of 600-619.


11 Into the Woods, note 5.


13 Losing Ground, note 1 at page 21.


In a rising interest rate environment, such as we saw between 2004 and 2006, even using a fully-indexed rate is likely to understate the risk. For that reason, some have suggested more stringent underwriting tests, such as the fully indexed rate plus 1%, see, e.g. AARP Comments to the Federal Reserve Board on Home Ownership and Equity Protection Act, Dkt OP-1288 (8/15/07) p. 11 available at http://www.federalreserve.gov/SECRS/2007/August/20070816/OP-1288/OP-1288_51_1.pdf. AARP makes the strong argument that lenders should underwrite the loan at the fully indexed rate plus 1%, to provide a small cushion against interest rate increases; this would be particularly important when short-term rates are abnormally loan and future increases could be expected. Other suggestions to address the rising rate environment conundrum include using as the benchmark the maximum rate to which the loan rate may rise during a specific period, see, e.g. Comments of the National Consumer Law Center and the National Association of Consumer Advocates to the Federal Reserve Board Regarding the Board’s Authority to Prohibit Unfair Acts and Practices In Connection With Mortgage Lending Under HOEPA (8/15/07), available at http://www.federalreserve.gov/SECRS/2007/August/20070816/OP-1288/OP-1288_52_1.pdf. Particularly in view of the unfortunate fact that subprime borrowers were never “buying” the opportunity to take advantage of a falling rate environment with their ARMs, because subprime ARMs were “up-escalator only” ARMS, it would not be unfair to offer an extra cushion to protect against rising rate index exacerbating the payment shock.

The maximum debt-to-income ratio set by the Federal Housing Administration for FHA loans is 41%. See http://www.fha-home-loans.com/debt_ratios_fha_loans.htm. Fannie Mae has guidelines that describe how the debt-to-income ratio should be calculated. Fannie Mae Selling Guide, Chapter 7, X, 703: Benchmark Ratios (Jan. 31, 2006).

“It should also be clearly understood from this information that no single factor is a final determinant in any applicant's qualification for a VA-guaranteed loan. Once the residual income has been established, other important factors must be examined. One such consideration is the amount being paid currently for rental or housing expenses. If the proposed shelter expense is materially in excess of what is currently being paid, the case may require closer scrutiny. In such cases, consideration should be given to the ability of the borrower and spouse to accumulate liquid assets, such as cash and bonds, and to the amount of debts incurred while paying a lesser amount for shelter. . . . [I]t is important to remember that the figures provided below for residual income are to be used as a guide and should be used in conjunction with the steps outlined in paragraphs (c) through (j) of this section.” 38 CFR 36.4337.

However, in many cases, borrowers are unaware that the broker or originator has inflated the income, often after the borrower provided the documentation, such as W-2 forms, according to attorneys and governmental investigators who have worked on such cases. The adjective in the frequently used term “liar’s loans,” then, should not be thought to apply just to the applicant.


Dugan at 4-5.

See “Losing Ground,” supra note at 27.
Testimony of Martin Eakes – Sept. 19, 2007

23 See, e.g., Fannie Mae “Single Family Selling Guide” Part VII, Section 104.05 (“First mortgages generally must provide for the deposit of escrow funds to pay as they come due taxes, ground rents, premiums for borrower-purchased mortgage insurance (if applicable), and premiums for hazard insurance and flood insurance. . . . The lender may waive the escrow deposit account requirement for an individual first mortgage, as long as the standard escrow provision remains in the mortgage documents—however, we do not recommend waiving it for a borrower who has a blemished credit record because the borrower may find it difficult to maintain homeownership if faced with the need to make lump-sum payments for taxes and/or insurance and any other periodic payment items.”)

24 See, e.g., “B&C Escrow Rate Called Low,” Mortgage Servicing News Bulletin (February 23, 2005), “Servicers of subprime mortgage loans face a perplexing conundrum: only about a quarter of the loans include escrow accounts to ensure payment of insurance premiums and property taxes, yet subprime borrowers are the least likely to save money to make such payments.”

25 See, e.g. States’ settlement agreement with Ameriquest, IV-B-5, States’ settlement agreement with Citigroup et al., Civ. No 1:01-CV-00606 (E.D. Ga., filed ), Complaint, Para. 18-19, A recent CRL review of 2007 securitizations showed a penetration rate for prepayment penalties averaging over 70%.

26 See, e.g. David W. Berson, Challenges and Emerging Risks in the Home Mortgage Business: Characteristics of Loans Backing Private Label Subprime ABS, Presentation at the National Housing Forum, Office of Thrift Supervision (December 11, 2006). According to MBA data, there was a 69.2% penetration rate for prepayment penalties on subprime ARMs originated in 2006. Doug Duncan, Sources and Implications of the Subprime Meltdown, Manufactured Housing Institute, (July 13, 2007). A recent CRL review of 2007 securitizations showed a penetration rate for prepayment penalties averaging over 70%.

27 See Berson, id. A recent MBA analysis shows that 97.6% of prime ARMs originated in 2006 had no prepayment penalty, and 99% of 2006 prime FRM had no penalty. Doug Duncan, id.

28 Marketing jargon in the industry is more honest about the role of prepayment penalties, along with high-LTV loans: “Build a fence around the customer:” or bring them in and “close the back door” are phrases that surfaced during regulatory investigations of subprime lenders in which one of the authors of this Comment was involved.

29 Indeed, according to one study, it would exceed the median net worth in 2002 for African American households ($5,988). And it drains almost 7% of the median net worth for white households that year ($88,651). Rakesh Kochhar, The Wealth of Hispanic Household: 1996-2002 p. 5, (Pew Center for Hispanic Studies), http://pewhispanic.org/files/reports/34.pdf

30 Christopher A. Richardson and Keith S. Ernst, Borrowers Gain No Interest Rate Benefits from Prepayment Penalties on Subprime Mortgages, Center for Responsible Lending (January 2005),


32 Mike Hudson and E. Scott Reckard, More Homeowners with Good Credit Getting Stuck in Higher-Rate Loans, L.A. Times, p. A-1 (October 24, 2005). For most types of subprime loans, African-Americans and Latino borrowers are more likely to be given a higher- cost loan even after controlling for legitimate risk factors. Debbie Gruenstein Bocian, Keith S. Ernst and Wei Li, Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages, Center for Responsible Lending, (May 31, 2006) at
33 Debbie Gruenstein Bocian, Keith S. Ernst and Wei Li, Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages, Center for Responsible Lending (May 31, 2006). Study finds that African-American and Latino borrowers are at greater risk of receiving higher-rate loans than white borrowers, even after controlling for legitimate risk factors. For example, African-American borrowers with prepayment penalties on their subprime home loans were 6 to 34 percent more likely to receive a higher-rate loan than if they had been white borrowers with similar qualifications.

34 Standard & Poor’s Weighs in on the U.S. Subprime Mortgage Market (April 2, 2007), cited by Sheila Bair, Chair, Federal Deposit Insurance Corporation in a statement to the Committee on Financial Services, U.S. House of Representatives (April 17, 2007).

35 An “assignee” is a party who purchases or otherwise takes a financial interest in the loan. The assignee has the right to collect payments and enforce the terms of the loan, including foreclosing on a house if a borrower defaults.


37 Recently Harvard issued a study that also recommended lifting current restrictions on assignee liability – see note 7.

38 See, e.g., Wei Li and Keith Ernst, The Best Value in the Subprime Market: State Predatory Lending Reforms, Center for Responsible Lending (February 23, 2006).

39 See January 25, 2007 letter from the Coalition for Fair & Affordable Lending (CFAL), an industry association, to the heads of the federal banking regulators, urging the regulators not to apply the October 4 2006 Interagency Guidance on Nontraditional Mortgage Product Risks to subprime 2-28 ARM loans.

40 As recently as July, 2007, even as the debacle was unfolding, that remained the case. For example, a borrower with a 620 FICO score, 90% LTV, and 1 –30 day delinquency, could get a 30-year fixed rate mortgage at 10.25% from Option One, compared to 11.9% for a 3/27 stated doc loan. At WaMu’s Long Beach Mortgage, that borrower could get a 10.1% 30-year fixed rate loan, compared to a 10.95% 2/28 Stated income loan.


43 See, e.g., http://sfgate.com/cgi-bin/article.cgi?f=/c/a/2007/09/13/MNJ8S1FKC.DTL.
In 2005, the bankruptcy law was amended to treat some recent purchase money loans for automobiles in a similar fashion, but the dollar figures for such loans pale in comparison to the amount of a home loan and, depending on fair market value, the amount of equity associated with the residence. Moreover, such loans can still be modified with respect to interest rate and payment amounts.

The family farm Chapter 12 corollary to section 1322(b)(2), found at 11 USC § 1222(b)(2), provides the bankruptcy court with power to “modify the rights of holders of secured claims, or of holders of unsecured claims…” Similarly, the corresponding provision of Chapter 11, found at 11 U.S.C. § 1132(b)(5), contains language identical to that in section 1322(b)(2), reaffirming the exemption for loans secured by the debtor’s primary residence, but imposing no corresponding exemption for a company’s principle place of business or any other property.

Calculations by the CRL using data from its “Losing Ground” report cited above, research from the University of North Carolina, the Home Mortgage Disclosure Act, and Bloomberg research.


Based on MBA's originations survey, cash-out refinancings comprised 80.6% of all subprime refinances in 2006.
**Maximum Interest Rate**

To bring rate into compliance, buy-down plan may apply.

**Logon to cwbc**

Effective: September 5, 2007

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**Rebate / Discount Pricing**

- Rebate: Max 2 pts. (Max 1 pt if prepay is bought out)
- Add 50% to rate for 1st pt., 75% for the 2nd
- Discount: Max 3 pts
- 40% off rate for each discount point paid on fixed
- 50% off rate for each discount point paid on ARM
Lehman Shuts Unit; Toll of Lenders Tops 100: Subprime Scorecard

By Rick Green

Aug. 23 (Bloomberg) -- Lehman Brothers Holdings Inc.'s shutdown of its subprime lending unit helped push the tally of mortgage companies that have halted operations or sought buyers since the start of 2006 to at least 100.

Lehman became the first of Wall Street's five biggest securities firms to close its subprime business yesterday when it shut BNC Mortgage LLC. The New York-based firm bought BNC in 2004 to expand lending to borrowers with weak credit.

Until last year, sales of mortgage companies fetched hundreds of millions of dollars, capped by Merrill Lynch & Co.'s $1.3 billion purchase of First Franklin on Dec. 30. Since then, 15 have gone bankrupt and about 50 have suspended loans or closed entirely. The total may be higher because some defunct firms didn't make public announcements or court filings.

``I don't think we are going to see the bottom for at least another six months,'' Edward Resendez, ex-chief executive officer of Resmae Mortgage Corp., said yesterday. Resendez sold Resmae to Citadel Investment Group at a bankruptcy auction. ``The lenders that are struggling out there are not going to survive. As soon as their liquidity runs out, they are going to go under.''

The industry slump pushed shares of mortgage companies down 58 percent from June 14, 2005, through yesterday, according to Bloomberg's index of mortgage real estate investment trusts, compared with a 22 percent gain for the Standard & Poor's 500 stock index. Among last year's 20 largest subprime lenders ranked by Inside Mortgage Finance, a trade publication, more than half have tried to sell themselves or left the business.

RESOURCES

- Bloomberg TV
- Bloomberg Radio
- Bloomberg Podcasts
- Bloomberg Press

Late Loans

Overdue payments on U.S. subprime mortgages rose to the highest level since 2002 during the first quarter of this year, according to the Mortgage Bankers Association. That's made investors who buy mortgages reluctant to bid, driving
down prices and cutting into the profit of home lenders.

Subprime loans are made to borrowers with poor credit ratings or heavy debts. The mortgages often charge higher interest rates to compensate for the greater risk of default.

The table below tracks sales, shutdowns, bankruptcies and transactions tied to home lenders. The list includes companies that may have offered subprime, prime or Alternative-A loans. The latter are an alternative for A-rated borrowers who fall just short of standards for regular prime mortgages.

Some of the most recent developments:

-- Accredited Home Lenders Holding Co. will close "substantially all" of its retail lending business and halt U.S. loan applications. About 1,600 people will lose their jobs.

-- Capital One Financial Corp. shut its GreenPoint Mortgage unit, eliminating 1,900 jobs.

-- Quality Home Loans, a California-based subprime lender, filed for bankruptcy.

-- Amstar Financial Holdings Inc., a Houston-based lender, said its mortgage division will cease operations.

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Notes:

-- Some names have been abbreviated for space. Companies listed may have engaged in conventional, Alternative A or subprime mortgage lending. Status of deals and companies, prices and terms are subject to adjustment after the announcement date.

N/D Not disclosed or not available.

* Announced date, first known disclosure or effective date if disclosed after completion. Some announced closings have not yet been completed.

** Asset sale

*** Citigroup obtained an option to buy ACC Capital's wholesale mortgage origination and servicing businesses.

**** Per Goldman Chief Financial Officer David Viniar 6/14/07 in conversation with reporters. Web site lists company name as Avelo Mortgage LLC d/b/a Senderra Funding.

(a) Retail assets

(b) Wholesale assets

(c) Actual price before taxes, per 10-Q filing. Centex's release cited after-tax proceeds of about $540 million.

(d) Residential subprime unit

(e) After sale of PHH Corp. to General Electric Co.

(f) Purchased in July 2007 for $188 million.

(g) Projected, after taxes, from partial divestiture.

(h) Units served mortgage brokers and bought home loans from mortgage bankers, thrifts, builders and credit unions.

(i) Formally known as Mortgage Investment Lending Associates.

(j) Confirmed by company e-mail on July 5, 2007.

(k) Owners included Cerberus Capital Management LP. Retail lending halted in June, wholesale lending in August.

To contact the reporter on this story: Rick Green in New York at rgreen18@bloomberg.net.

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SCORECARD: DEBT DILEMMAS

How Credit-Market Tremors Have Affected Junk Bonds, LBOs and Hedge Funds

The days of easy credit may be coming to an end. The jitters began with losses at two Bear Stearns hedge funds that invested in subprime-mortgage debt that now are worth almost nothing. And over the past few weeks, a string of companies has delayed or canceled debt offerings, a sign that investors may be less interested in debt deals that don't adequately reward them for potential risk. — Compiled by Annelena Lobb and Cassandra Vinograd

Click on the category names to sort the columns.

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<th>Problems First Reported †</th>
<th>Issuer or Fund</th>
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<td>09/17/2007</td>
<td>E*Trade Financial Corp.</td>
<td>Earnings warning</td>
<td>The popular retail online brokerage said it expects profits to come in 31% below the most recent guidance it had given analysts -- partly due to its exposure to the mortgage business.</td>
<td>E*Trade, a buyer of mortgages from third parties, plans to get out of that business altogether and has set aside $245 million, up from $70 million, to cover related losses over the next four quarters.</td>
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<td>09/14/2007</td>
<td>Northern Rock PLC</td>
<td>Liquidity crunch</td>
<td>The Bank of England agreed to provide emergency funding to Northern Rock, one of the U.K.'s largest mortgage lenders, to offset a &quot;severe liquidity squeeze&quot; that cut off its access to capital.</td>
<td>If current conditions persist through year-end, &quot;there will clearly be an impact on Northern Rock's 2007 asset growth and, therefore, on profits,&quot; the Newcastle, England-based bank said in a statement.</td>
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<td>09/11/2007</td>
<td>Y2K Finance Inc.</td>
<td>Hedge fund losses</td>
<td>The $2 billion hedge fund, managed by London-based Wharton Asset Management, suspended investor redemptions until at least Dec. 1 because of market turbulence.</td>
<td>The Ireland-registered fund, which invests in residential mortgage-backed securities and other asset-backed debt, also said it plans to postpone calculating its net asset value.</td>
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<td>09/10/2007</td>
<td>Insight Communications</td>
<td>Auction delayed</td>
<td>Carlyle Group shelved the sale of the New York cable company, Deal Journal reported, citing people familiar with the matter. The surge in borrowing costs in the leveraged loan and bond markets derailed the deal, as bids didn't live up to Carlyle's expectations.</td>
<td>Carlyle still plans to sell Insight, which it bought for about $2 billion including debt in 2005. One banker involved in the deal said this could just be a tactic on Carlyle's part to get the bidders to raise their offers.</td>
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<td>09/06/2007</td>
<td>TPG-Axon Capital Management</td>
<td>Fund losses</td>
<td>The $11 billion hedge fund has had to write down to virtually zero its $275 million investment in Axon Financial Funding, a structured investment vehicle hit by subprime-mortgage troubles.</td>
<td>If Axon Financial -- a hedge for TPG-Axon manager Dinakar Singh, who has successfully bet on trouble in the subprime market -- gets through this rough period, the hedge fund's stake in the company could rise in value.</td>
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<tr>
<td>08/28/2007</td>
<td>Cheyne Finance</td>
<td>Liquidity crunch</td>
<td>Cheyne Finance, a $6.6 billion structured investment vehicle managed by Cheyne Capital, one of London's biggest hedge fund groups, has started selling assets amid a debt squeeze. Cheyne said it breached tests measuring the value of its assets against its liabilities, forcing it to start liquidating holdings.</td>
<td>Cheyne Finance said it has enough cash on hand to pay back debt maturing before the end of November, and will try to avoid completely winding down by reaching an agreement with lenders.</td>
</tr>
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</table>
08/27/2007  Nacco Industries  Spinoff scrapped  The Cleveland-based holding company of lift trucks, housewares and mining business said the recent period of market volatility isn’t conducive to spinning off its Hamilton Beach unit.  Hamilton Beach, a maker of electric household appliances, will continue to operate as usual.

08/22/2007  Carlyle Capital  Liquidity crunch  The listed investment fund, which trades on the Euronext Amsterdam exchange, recently received $200 million in emergency financing from U.S. private equity firm Carlyle Group. The fund said it will seek new forms of financing and reduce its target leverage. CEO John Stomber said funding conditions are worse than in 1998, at the time of the collapse of Long-Term Capital Management.

08/22/2007  The Republic of Belarus  Auction delayed  The government put on hold plans to issue $500 million-equivalent of Eurobonds. "Taking under consideration current unfavorable market conditions we have decided to postpone any decision on the issue of Eurobonds until markets improve," said First Deputy Finance Minister Andrei Kharkovets. Mr. Kharkovets said he doesn’t expect to make any decision on the Eurobond until the end of September.

08/22/2007  Coventree Inc.  Profit problems  The Toronto financial firm said short-term revenue will be severely impacted by the turmoil in Canada’s asset-backed commercial paper market. Due to the market turmoil and other factors facing the company, Coventree said it “has decided to suspend any additional investments in new concepts or business opportunities. In particular, Coventree will not be pursuing the creation of a U.S. conduit or the launch of a retail bank at this time.”

08/22/2007  H&R Block  Liquidity crunch  The tax preparer was forced to tap $850 million under existing backup bank credit lines to replace commercial paper as it came due. The company became the latest issuer with mortgage exposure to find itself unable to borrow the funds it needed in the commercial-paper market.

08/20/2007  Solent Capital Partners LLP  Liquidity crunch  The London hedge-fund and money manager said it couldn’t raise money, finding few buyers for the euro and U.S. short-term debt a debt vehicle used for financing, and may have to sell some assets. The debt vehicle, Mainsail II Ltd., owns about $2 billion in securities supported by assets that include U.S. mortgages, according to a Fitch Ratings report. Mainsail said it had turned to backup bank lines of credit for funding.

08/17/2007  Barclays Capital  Liquidity crunch  Two structured investment vehicles of Barclays Capital, the investment-banking division of Barclays PLC, have collapsed, while two others may have to wind down after having trouble raising short-term funding. Barclays Capital's European head of collateralized debt obligations, Edward Cahill, resigned. On Sept. 10, Bob Diamond, head of investment banking at Barclays, said Barclays Capital was profitable, easing investor concerns. He also said Barclays had been restructuring its SIVs, but said those efforts were not “bailouts”

08/17/2007  Sachsen LB  Liquidity crunch  A consortium of banks stepped in to bail out the small German state-owned bank after an affiliate faced difficulties selling commercial paper to finance its operations. Sachsen was sold to Stuttgart-based state-owned bank Landesbank Baden-Wuerttemberg. Under the terms of the deal, Gov. Guenther Oettinger said, the state of Saxony, which holds 37% in Sachsen, and the Sachsen-Finanzgruppe, owner of 63%, will receive stakes in LBBW, but that exactly how large these stakes will only be determined on Dec. 31.

08/15/2007  KKR Financial Holdings Inc.  Profit problems  The San Francisco affiliate of buyout firm KKR said it could lose more than $200 million from leveraged investments in mortgage-backed securities, KKR Financial said it is talking to other investors in its portfolio about how to resolve potential funding disruptions. KKR partners promised on Aug. 20 that in a worst-case
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<th>Date</th>
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<th>Description</th>
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<td>08/14/2007</td>
<td>RAMS Home Loans Group Ltd.</td>
<td>Profit problems</td>
<td>The Australian non-bank lender said volatile credit markets could hit its earnings, sending shares in the recently listed lender down as much as 32%.</td>
<td>The first Australian mortgage company to suffer from global credit squeeze and the first to have problems related to the asset-backed commercial paper market in the U.S.</td>
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<tr>
<td>08/14/2007</td>
<td>Thornburg Mortgage</td>
<td>Liquidity crunch</td>
<td>The Santa Fe, N.M.-based REIT, which originates &quot;jumbo&quot; mortgage loans of more than $417,000, stopped locking in rates on mortgages, citing &quot;unprecedented and irrational sentiment&quot; in the credit market. Moody's downgraded its credit and several analysts downgraded its stock.</td>
<td>Thornburg delayed its dividend payment after getting margin calls and finding it more difficult to fund its mortgage assets in the commercial-paper and asset-backed securities markets. It cut the book value of its mortgage assets by 26%. Its shares plunged 46% on the day of these announcements. A week later, it sold $20.5 billion in top-rated mortgage-backed securities to pay down short-term borrowings, resulting in a third-quarter capital loss of about $930 million.</td>
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<td>08/14/2007</td>
<td>Sentinel Management Group</td>
<td>Liquidity crunch</td>
<td>The Northbrook, Ill., firm, which manages short-term cash for commodity trading firms and hedge funds, stopped allowing its clients to withdraw funds, saying a lack of liquidity in the credit markets has made it impossible to meet redemptions without selling securities well below their fair value.</td>
<td>The company has filed for bankruptcy-court protection. On Aug. 20, the SEC filed civil-fraud charges against Sentinel, accusing it of &quot;undisclosed use of leverage, commingling and misappropriation of clients' securities.&quot;</td>
</tr>
<tr>
<td>08/13/2007</td>
<td>Mission West</td>
<td>Buyout scuttled</td>
<td>The real-estate investment trust said closure is unlikely on its $1.8 billion buyout by an unnamed private-equity firm due to the withdrawal of the buyer's primary and secondary lenders from the market.</td>
<td>Mission West is in talks with three other potential acquirers with internal sources of financing.</td>
</tr>
<tr>
<td>08/09/2007</td>
<td>Tarragon Corp.</td>
<td>Profit problems</td>
<td>The New York real-estate developer said there were doubts about its ability to to continue as a going concern, citing &quot;liquidity issues&quot; and market conditions. It also delayed its 10Q filing and postponed a spinoff of its homebuilding business.</td>
<td>The company has hired Lazard to explore strategic alternatives. Its shares have plunged to less than $1.</td>
</tr>
<tr>
<td>08/09/2007</td>
<td>NIBC</td>
<td>Profit problems</td>
<td>The Dutch merchant bank, owned by former Goldman Sachs banker Christopher Flowers, said it has lost at least $187 million on subprime investments.</td>
<td>Investors in NIBC unable to buy protection against a default of the company's debt amid concerns about the bank's health and rumors it was being prepared for a sale. JC Flowers, the private equity firm that owns NIBC with a consortium of fellow investors, is believed to be preparing to sell the embattled bank.</td>
</tr>
<tr>
<td>08/09/2007</td>
<td>Home Depot</td>
<td>Buyback trimmed</td>
<td>The retailer will now buy back shares in a modified Dutch auction at $37 to $42 a share, down from the range of $39 to $44 a share announced in July.</td>
<td>Extended tender offer deadline to Aug. 31. Home Depot's board agreed on Aug. 26 to sell the supply business for $8.5 billion to Bain Capital. Carlyle Group and Clayton, Dubilier &amp; Rice, about 18% less than the price hammered out in June when the buyout boom was at its peak. Home Depot will also be left holding a 12.5% equity stake in the unit.</td>
</tr>
<tr>
<td>08/09/2007</td>
<td>American International Group</td>
<td>Profit problems</td>
<td>Operating income at its consumer-finance operations, which includes a subprime-mortgage lender, fell 71%; Acknowledged that housing-market weakness led to a significant increase in losses for its domestic mortgage-insurance business, but</td>
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</table>
08/07/2007  United Overseas Bank Ltd.  Profit problems  The Singapore bank reported a markdown of about $22.4 million on its portfolio of collateralized debt obligations, the first Singapore bank to acknowledge such a loss amid the subprime crisis.  UOB said it expects to incur a further loss as of the end of July.

08/07/2007  BNP Paribas Investment Bankers  Funds suspended  The "complete evaporation" of liquidity in certain parts of the subprime mortgage market pressured funds  Bank said it would suspend three funds, Parvest Dynamic ABS, BNP Paribas ABS Euribor and BNP Paris ABS Eonia, worth a total of about €1.5 billion. On Aug. 23, said it planned to resume trading in the funds the following week.

08/06/2007  Luminent Mortgage Capital  Margin calls  A week after reassuring investors of its liquidity and ability to pay a dividend, the San Francisco home-loan investment company said it was facing significant margin calls, suspending its dividend and exploring strategic alternatives. It said the secondary market for mortgage loans and mortgage-backed securities "has seized-up."  Luminent said it's trying to "enhance its liquidity and preserve the value" of its portfolio of assets.

08/06/2007  Archstone-Smith Trust  Buyout delayed  A joint venture of Tishman Speyer Properties and Lehman Brothers Holdings said it would delay the completion of its $15.2 billion acquisition of apartment-owning titan Archstone-Smith to early October.  Financiers of this deal -- seen as a bellwether in the real-estate market -- may be looking for fresh financing sources to minimize their own risk. On Aug. 21, shareholders approved the deal, a positive sign.

08/03/2007  KfW  Profit problems  German state-owned development bank said it assumed "expected possible losses" of as much as $1.37 billion from bailing out midsize lender IKB  KfW put up the lion's share of the 3.5 billion euro rescue fund set up to cover IKB's likely losses when IKB does sell its investments; IKB said it has reserves that are strong enough to cover it for the next 12 months.

08/02/2007  Mitchells & Butler  Venture postponed  U.K. pub operator had planned to separate out its property assets from its operating divisions  Planned property joint venture put on hold due to unstable credit market conditions

08/01/2007  Oddo & Cie  Fund losses  French securities firm struggles with plunge in collateralized debt obligations  Three funds totaling 1 billion euros will be closed (Correction: An earlier version of this table incorrectly said these were hedge funds)

08/01/2007  Fortress Investments  Hedge fund losses  Macquarie bank's high-yield Australian fund said investors could face losses of up to 25% due to U.S. market fallout  Fortress has had to sell some assets, said average price of assets in the portfolios had fallen by 4% in June and may have fallen another 20-25% in July; could face margin calls if assets don't sell well

07/31/2007  CNA Financial  Profit problems  Chicago commercial insurer reported lower quarterly earnings as investment losses increased due to write-downs on subprime debt  Company says it suffered $91 million in losses, partly due to a $20 million write-down related to subprime debt; this contributed to a 9% decline in quarterly profit

07/31/2007  Sowood  Hedge fund losses  Boston firm suffered losses of more than 50% this month, dropping the firm's assets to about $1.5 billion from $3 billion  Sowood said it will wind down its two funds

07/31/2007  C-Bass  Margin calls  MGIC Investment and Radian Group say joint venture C-Bass  MGIC and Radian agreed to terminate their merger pact
has been subject to an "unprecedented" amount of margin calls, adversely affecting liquidity because of losses at C-Bass. All litigation the firms filed against each other will be withdrawn and that no money changed hands in ending the merger agreement.

07/30/2007  Commerzbank  Hedge fund losses
German bank said its total exposure to the US subprime market is 1.2 billion euros
Set aside 80 million euros to cover exposure to US subprime market

07/30/2007  Insight Communications  Offering delayed
Bids for the New York cable operator were due yesterday, now delayed more than a week by the firm's bankers
Bankers at Morgan Stanley delayed to give private-equity bidders more time to line up financing

07/30/2007  Stoneridge  Offering delayed
$200 million senior secured term loan postponed indefinitely due to "unfavorable market conditions"
The electronic component maker was forced to cancel its tender offer to purchase its $200 million in outstanding senior notes

07/30/2007  American Home Mortgage Investment  Margin calls
Banks demanded more cash after the lender wrote down the value of its loan and security portfolios
Shares of the real-estate investment trust were halted for more than a day; lender delayed paying dividends on common stock, may delay payments on preferred shares because of margin calls; said may have to sell assets, find new financing, or restructure debt to meet banks' demands. Filed Chapter 11 bankruptcy Aug. 6 after laying off majority of its workforce the week before

07/30/2007  IKB Deutsche Industriebank AG  Liquidity crunch
The German bank set up an affiliate to invest in complex U.S. debt securities. The affiliate, Rhineland Funding Capital Corp., had to renew its short-term borrowings frequently. When investors realized its collateral included subprime mortgages, they shut off the spigot. Suddenly, Rhineland couldn't repay other debt that was coming due and needed a bailout by Germany's financial regulator, with contributions from major German banks.
Three of IKB's top executives, including Chief Executive Stefan Orteifen, departed. The bank formed a task force to sort out its problems. Its stock has tumbled sharply since the crisis began.

07/27/2007  AA/Saga  Offering delayed
Merger underwriters Barclays and Mizuho banks have so far failed to find sub-underwriters to spread £4.8 billion risk
The sale of the GBP 4.8 billion of debt backing the merger of Saga, a group specializing in services for over-50s, and motor-vehicle recovery and insurance company AA has been postponed.

07/27/2007  Dana Gas  Offering delayed
The U.A.E.-based firm postponed pricing its $1 billion convertible Islamic bond due to market volatility
Dana Gas was advised by Barclays and Cit to delay pricing until September

07/27/2007  Sowood Capital Management  Hedge fund losses
Down about 10% so far this year
Sold various positions to raise cash to deal with credit difficulties and potential margin calls; faces no redemptions until end of 2008

07/27/2007  Cadbury Schweppes  Auction delayed
Final bids in the auction of its U.S. drinks business, including the 7-Up, Snapple and Dr. Pepper brands, were due at the start of next week
Extended the bid deadline, citing "extreme volatility" in the leveraged debt markets

07/26/2007  Beazer Homes  Credit reduced
Banks halved the home builder's credit line to $500 million from $1 billion
Beazer vehemently denies rumors it will file for bankruptcy

07/26/2007  Gazprom  Offering delayed
Gazprom, the world's largest gas company, decided not to price its 30-year benchmark dollar Eurobond, citing market conditions
Gazprom said it will release the bond as soon as the market settles

07/26/2007  Tyco  Offering
Called off $1.5 billion bond deal, Tyco had come to the market with a
<table>
<thead>
<tr>
<th>Date</th>
<th>Company</th>
<th>Action</th>
<th>Description</th>
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<tbody>
<tr>
<td>07/26/2007</td>
<td>Brazilian Federal</td>
<td>Offering</td>
<td>Pulled citing &quot;unfavorable&quot; market conditions</td>
<td>Early next week, Treasury will issue its August schedule; typically holds bond sales once or twice a week</td>
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<td>Treasury</td>
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<td>07/26/2007</td>
<td>DAE Aviation</td>
<td>Offering</td>
<td>Delayed citing market conditions</td>
<td>Barclay's successfully priced $325 million in senior notes tied to the same deal</td>
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<td>07/26/2007</td>
<td>Absolute Capital</td>
<td>Hedge fund</td>
<td>Losses citing market conditions</td>
<td>Withdrawals suspended until market liquidity improves</td>
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<td>07/25/2007</td>
<td>Nomura Holdings</td>
<td>Profit</td>
<td>Problems citing market conditions</td>
<td>Nomura slashed its subprime positions to $589 million from $1.74 billion and downsized its mortgage bond business. It also shuttered its New York fixed-income research team, led by Mark Adelson, its high-profile managing director of structured finance research</td>
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<tr>
<td>07/25/2007</td>
<td>Countrywide Financial</td>
<td>Profit</td>
<td>Problems citing market conditions</td>
<td>Lender said prime mortgage loan losses contributed to 33% drop in second-quarter net income; slashed earnings forecast, citing &quot;increasingly challenging housing and mortgage markets.&quot; Announced Aug. 9 that &quot;unprecedented disruptions&quot; in debt and mortgage-finance markets could hurt the company's financial condition. Merrill Lynch downgraded the stock to &quot;sell,&quot; warning bankruptcy was possible. Countrywide tapped an $11.5 billion line of credit and had its banking arm provide a greater share of funding for its loans. Bank of America made a $2 billion equity investment in Countrywide, offering it a dose of security</td>
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<td>07/25/2007</td>
<td>Silverton Casino</td>
<td>Offering</td>
<td>Pulled citing market conditions</td>
<td>The casino operator says it remains committed to the project</td>
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<td>07/25/2007</td>
<td>Oneida</td>
<td>Offering</td>
<td>Pulled citing market conditions</td>
<td>The seven-year term loan was led by Credit Suisse; rates had been higher than investors expected</td>
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<td>07/25/2007</td>
<td>Stolle Machinery</td>
<td>Offering</td>
<td>Pulled citing market conditions</td>
<td>Machinery supplier forced to pull its Goldman Sachs-led loan; earlier, Stolle had offered rates higher than investors expected and had restructured the initial deal by adding a second-lien price</td>
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<td>07/24/2007</td>
<td>Oxygen Media</td>
<td>Offering</td>
<td>Pulled citing market conditions</td>
<td>J.P. Morgan and RBS Securities had launched the senior secured financing</td>
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<td>07/24/2007</td>
<td>Allison Transmission</td>
<td>Offering</td>
<td>Delayed citing market conditions</td>
<td>The sale of Allison to Carlyle Group and Onex Group is likely to proceed, but trouble raising debt complicates matters. On Sept. 11, Deal Journal reported that banks have managed to sell $1 billion of the loans they were holding -- though they were still on the hook for the rest of the loans, in addition to another $1.1 billion in junk bonds.</td>
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<td>Date</td>
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<tr>
<td>07/23/2007</td>
<td>Manchester United</td>
<td>Offering delayed</td>
<td>The U.K. soccer club delayed its plans to refinance $1.4 billion in debt</td>
<td>Manchester United cited turbulence in the markets as the reason behind its decision</td>
</tr>
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<td>07/23/2007</td>
<td>Intergen</td>
<td>Offering revised</td>
<td>The power company revised size and structure of its bond issuance</td>
<td>Intergen lowered the value of three-currency bond issuance to $1.875 billion from $1.975 billion</td>
</tr>
<tr>
<td>07/23/2007</td>
<td>Y2K Finance</td>
<td>Hedge fund losses</td>
<td>$2 billion London hedge fund blamed price drops on its holdings of U.S. subprime assets in a letter to investors explaining losses</td>
<td>The firm, part of Wharton Management, said its investments dropped 7.3% in June; fund is down 5.24% this year</td>
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<tr>
<td>07/20/2007</td>
<td>Stone Tower Credit Fund</td>
<td>Hedge fund losses</td>
<td>Fund told investors its portfolio value fell by 1.2% in June</td>
<td>June was the first down month since the fund, with $637 million under management, began investing in 2001; value reportedly continues to decline</td>
</tr>
<tr>
<td>07/20/2007</td>
<td>Basis Capital Funds Management</td>
<td>Hedge fund losses</td>
<td>Two funds invested in instruments related to U.S. subprime mortgages posted steep losses last month</td>
<td>The Sydney fund restricted investor withdrawals and is trying to restructure. It was the first hedge fund in Asia to show significant fallout related to U.S. subprime woes. Recently said losses in its Yield Alpha Fund may exceed 80%.</td>
</tr>
<tr>
<td>07/20/2007</td>
<td>Alliance Boots</td>
<td>Offering delayed</td>
<td>Having trouble raising the dollar equivalent of $18.4 billion in loans</td>
<td>Senior loan postponed indefinitely until market conditions improve; junior loans being offered to investors at interest rates higher than planned</td>
</tr>
<tr>
<td>07/20/2007</td>
<td>Chrysler Group</td>
<td>Offering delayed</td>
<td>Struggle to raise $20 billion in loans to finance Cerberus Capital Management's purchase of an 80% stake in Chrysler from DaimlerChrysler, which is still slated for August 3</td>
<td>Bankers have postponed a sale of $12 billion in debt for the auto company, citing weak demand, and plan to fund the bulk of that debt from their own pockets for the time being. Bankers still expect to raise another $8 billion in loans for Chrysler's profitable finance unit, though they have had to raise interest rates on those loans.</td>
</tr>
<tr>
<td>07/19/2007</td>
<td>Cyrela Brazil Realty</td>
<td>Offering delayed</td>
<td>Upscale Brazilian real estate developer postponed its $265 million overseas bond issue amidst unfavorable market conditions</td>
<td>Cyrela cited growing investor risk aversion for the reason behind the postponement</td>
</tr>
<tr>
<td>07/19/2007</td>
<td>Edenor</td>
<td>Offering delayed</td>
<td>The Argentine electricity distributor, also known as Empresa Distribuidora, postponed a $220 million planned bond offering due to market conditions</td>
<td>Edenor said it would contemplate returning to the market over the near term, subject to regulations and market conditions</td>
</tr>
<tr>
<td>07/18/2007</td>
<td>AXA SA</td>
<td>Fund losses</td>
<td>French insurer's billion dollar bond fund lost about 40% of its value last month when credit markets slid</td>
<td>Money-management unit has offered to cash out investors at current estimated values, to avoid having to conduct a rapid sale of securities to meet redemptions; had earlier had to temporarily close two funds</td>
</tr>
<tr>
<td>07/18/2007</td>
<td>Harmony Gold</td>
<td>Offering delayed</td>
<td>Delayed $350 million bond issue</td>
<td>Plans on hold pending market improvement</td>
</tr>
<tr>
<td>07/18/2007</td>
<td>OAC Rosneft</td>
<td>Offering delayed</td>
<td>Postponed bond placement, pulled a $2 billion two-tranche offer</td>
<td>Rosneft still trying to refinance part of the $22 billion of debt it took on to buy assets of OAO Yukos earlier this year.</td>
</tr>
<tr>
<td>07/17/2007</td>
<td>A-TEC</td>
<td>Offering delayed</td>
<td>Delayed hybrid eurobond release</td>
<td>Plans on hold pending market improvement</td>
</tr>
<tr>
<td>07/16/2007</td>
<td>Telemobil S.A.</td>
<td>Offering delayed</td>
<td>The Romanian telecommunications company postponed its $125 million inaugural senior secured notes offering due to market volatility</td>
<td>On hold indefinitely</td>
</tr>
<tr>
<td>Date</td>
<td>Company</td>
<td>Offering Type</td>
<td>Description</td>
<td>Impact/Outcome</td>
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<tr>
<td>07/16/2007</td>
<td>Maxeda</td>
<td>Offering pulled</td>
<td>$1.4 billion offering canceled</td>
<td>KKR forced to alter loan financing after Citigroup and ABN Amro canceled plans to sell $1.4 billion in debt</td>
</tr>
<tr>
<td>07/12/2007</td>
<td>Aozora</td>
<td>Offering delayed</td>
<td>The Japan-based bank postponed issuance of its dollar-denominated, step-up, callable, subordinated bond due to market volatility</td>
<td>The bank said it intends to return to the bond market once conditions stabilize</td>
</tr>
<tr>
<td>07/11/2007</td>
<td>First Gulf Bank</td>
<td>Offering delayed</td>
<td>Delayed launch of $3.5 billion eurobond program due to market volatility</td>
<td>Plans on hold pending market improvement</td>
</tr>
<tr>
<td>07/11/2007</td>
<td>Quebecor</td>
<td>Offering pulled</td>
<td>$750 million bond sale, which was to be used to acquire Osprey Media Income Fund, postponed</td>
<td>Could get a bank bridge loan</td>
</tr>
<tr>
<td>07/10/2007</td>
<td>Swift &amp; Co.</td>
<td>Offering pulled</td>
<td>The meat processing company was offering $600 in notes to finance the buyout of J&amp;F Participacoes</td>
<td>The offering, run jointly by J.P. Morgan and Credit Suisse, was withdrawn</td>
</tr>
<tr>
<td>07/06/2007</td>
<td>Bank of Moscow</td>
<td>Offering delayed</td>
<td>The bank postponed its inaugural, five-year $272.7 million bond issue due to market volatility</td>
<td>Unsure when or if the bank will still carry out the euro-denominated issue</td>
</tr>
<tr>
<td>07/06/2007</td>
<td>Caliber Global Investment</td>
<td>Hedge fund losses</td>
<td>Cambridge Place's London-based fund, once worth $908 million, had majority of its investments in US subprime mortgage debts</td>
<td>Suffered net loss of 8.8 million euros in the first quarter alone; fund will close, money to be returned to investors</td>
</tr>
<tr>
<td>07/05/2007</td>
<td>Braddock Financial</td>
<td>Hedge fund losses</td>
<td>Fund invested mainly in bonds backed by subprime mortgages; investors withdrew money</td>
<td>$100 million in losses in the Galena Street Fund; fund closed</td>
</tr>
<tr>
<td>07/04/2007</td>
<td>Carphone Warehouse</td>
<td>Offering delayed</td>
<td>U.K. mobile-phone retailer put its sterling-denominated bond issue on hold because of turbulence in credit markets</td>
<td>Carphone Warehouse is expected to return to the market in the fall, when conditions are more favorable</td>
</tr>
<tr>
<td>07/03/2007</td>
<td>CanWest Mediaworks</td>
<td>Offering reduced</td>
<td>Market conditions caused CanWest to abandon a high-yield debt issue in connection with its purchase of Alliance Atlantis</td>
<td>CanWest and partner Goldman Sachs said bridge financing has been lined up and the $2.3 billion deal will close on Aug. 15, a one-week delay from the previous plan.</td>
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<tr>
<td>07/03/2007</td>
<td>United Capital Asset Management</td>
<td>Hedge fund losses</td>
<td>Held $500 million in assets, heavily tied to subprime mortgages</td>
<td>Stopped letting investors withdraw money after a deluge of withdrawal requests</td>
</tr>
<tr>
<td>06/29/2007</td>
<td>Bombardier Recreational Products</td>
<td>Loan postponed</td>
<td>Subprime fallout forces postponement of $1.12 billion bank loan, according to Reuters</td>
<td>Waiting for the market to settle</td>
</tr>
<tr>
<td>06/29/2007</td>
<td>Oreck</td>
<td>Offering pulled</td>
<td>Vacuum company's $200 million debt refinancing loan withdrawn due to market conditions</td>
<td>Plans on hold indefinitely</td>
</tr>
<tr>
<td>06/28/2007</td>
<td>Dollar General</td>
<td>Offering terms changed</td>
<td>Dollar General, which is being acquired by private equity firms, changes terms of $1.9 billion junk bond offering and raises interest rates to entice buyers</td>
<td>Offering closed; bonds had 14 new covenants</td>
</tr>
<tr>
<td>06/27/2007</td>
<td>KIA Motors</td>
<td>Offering pulled</td>
<td>South Korea's KIA pulled a five-year $500 million bond offering due to market conditions</td>
<td>Company rumored to consider trying again when market conditions become more favorable</td>
</tr>
<tr>
<td>06/27/2007</td>
<td>MISC BHD</td>
<td>Offering delayed</td>
<td>Market volatility postpones $750 million bond issue</td>
<td>The Malaysian carrier of liquefied natural gas put its 10-year bond issue on hold until market improves</td>
</tr>
<tr>
<td>06/27/2007</td>
<td>Myers Industries</td>
<td>Offering delayed</td>
<td>Delayed launch of a buyout-financing deal in the hope the market would settle down in coming days</td>
<td>Plans still on hold</td>
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<tr>
<td>Date</td>
<td>Company</td>
<td>Type of Offering</td>
<td>Details</td>
<td>Underwriters or Investors</td>
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<tr>
<td>06/27/2007</td>
<td>Magnum Coal</td>
<td>Offering delayed</td>
<td>Delayed a $350 million junk offering</td>
<td>Underwriters postponed offer indefinitely</td>
</tr>
<tr>
<td>06/26/2007</td>
<td>U.S. Foodservice</td>
<td>Offering pulled</td>
<td>Investors balk over terms of $3.6 billion bond-and-loan deal needed to finance sale of firm to private equity firms KKR and Clayton Dubilier.</td>
<td>Underwriters left holding debt on their books and will try to sell later; so far, have shopped it around to a frosty reception</td>
</tr>
<tr>
<td>06/26/2007</td>
<td>ServiceMaster</td>
<td>Offering pulled</td>
<td>Called off a $1.15 billion sale of junk to pay for ServiceMaster's LBO; bond investors balked at provisions that would have enabled the company to put off interest payments and instead take on additional debt if the company were to run short of cash.</td>
<td>Received its financing from a bridge loan directly from the underwriters</td>
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<tr>
<td>06/26/2007</td>
<td>Catalyst Paper</td>
<td>Offering pulled</td>
<td>Citing &quot;adverse&quot; conditions, the company pulled a $150 million offering that had already been cut from $200 million, planned for funding its business and other investments</td>
<td>Underwriters postponed offer indefinitely</td>
</tr>
<tr>
<td>06/26/2007</td>
<td>ServiceMaster</td>
<td>Offering delayed</td>
<td>Put off plans to issue $1.34 billion in bonds, citing turbulent debt market</td>
<td>Plans still on hold</td>
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<tr>
<td>06/26/2007</td>
<td>Arcelor Finance</td>
<td>Offering pulled</td>
<td>Called off a $1.15 billion sale of junk to pay for ServiceMaster's LBO; bond investors balked at provisions that would have enabled the company to put off interest payments and instead take on additional debt if the company were to run short of cash.</td>
<td>Received its financing from a bridge loan directly from the underwriters</td>
</tr>
<tr>
<td>06/22/2007</td>
<td>Thomson Learning</td>
<td>Selling bonds</td>
<td>Received its financing from a bridge loan directly from the underwriters</td>
<td>Underwriters left holding the debt</td>
</tr>
<tr>
<td>06/12/2007</td>
<td>Bear Stearns</td>
<td>Hedge fund losses</td>
<td>Two funds, which once controlled $10 billion, had invested in subprime-mortgage debt; a third had practically no exposure to subprime mortgages but had suffered from a series of refund requests and markdowns on a range of mortgages</td>
<td>The Enhanced Leverage Fund quickly went belly up. High-Grade Structured Credit Strategies got a $1.6 billion bailout from Bear Stearns, but lenders have seized most of the fund's remaining assets. Both funds are now nearly worthless, and filed for bankruptcy protection Aug. 1. Withdrawals from the Asset-Backed Securities Fund, which had put about $850 million into mortgage investments, were suspended Aug. 1. Conference call Aug. 3 tried to reassure investors, said firm is facing worst market conditions in years. Co-President Warren Spector resigned.</td>
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<tr>
<td>05/07/2007</td>
<td>Dillon Read Capital Management</td>
<td>Hedge fund losses</td>
<td>UBS' in-house hedge fund trading in mortgage securities</td>
<td>$123 million in losses from trades on mortgage securities; fund closed after losses weighed on bank's fixed income revenue; UBS said it expects the bank to book costs of up to $300 million to shut the fund</td>
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<td>08/9/2007</td>
<td>Highbridge Capital Management</td>
<td>Hedge fund losses</td>
<td>The hedge-fund manager told investors its Highbridge Statistical Opportunities Fund was down 16% as of Aug. 8 and was down 16% for the year. The $1.8 billion publicly traded Highbridge Statistical Market Neutral Fund was down 5.2% for the month.</td>
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<td>08/9/2007</td>
<td>Renaissance Technologies Corp.</td>
<td>Hedge fund losses</td>
<td>The hedge-fund company run by Jim Simons had been a standout performer in recent years, but told investors that a key fund has The computer-model-driven fund has since rebounded a bit. Mr. Simons sent a letter to investors saying, &quot;The culprit is not the Basic</td>
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Goldman's famed, $9 billion Global Alpha fund was down about 16% on the year at the beginning of August, while its $3.6 billion Global Equity Opportunities Fund lost more than 30% of its value in one week in early August, and its $757 million North American Equity Opportunities fund was down about 15%.

All three funds were forced to sell risky positions. Like many other hedge funds suffering lately, both rely on computer models that were blindsided by the turmoil of financial markets sparked by credit worries. Goldman tried to bolster confidence in the Global fund by a letter to investors calling its performance "disappointing" but saying it expected no shortage of liquidity.

Sources: WSJ.com research, Dow Jones Newswires, Reuters, S&P, Barings

Write to the Online Journal's editors at newseditors@wsj.com

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