HUD-TREASURY REPORT RECOMMENDS PREDATORY LENDING REMEDIES

This week the Department of Housing and Urban Development (HUD) and the Treasury issued a joint report detailing recommendations for legislative, regulatory and other actions to thwart predatory and abusive home mortgage lending.

A uniform definition of predatory lending has been elusive, but in the agencies' view—whether undertaken by creditors, brokers, or home improvement contractors—it involves deception or fraud, manipulation of the borrower through aggressive sales tactics, or taking unfair advantage of the borrower's lack of understanding about loan terms. These practices are often accompanied by loan terms that, alone or in combination, are abusive or make the borrower more vulnerable to abusive practices.

According to the agencies, predatory lending generally occurs in the subprime market. Most often at risk are borrowers who want to use the collateral in their homes for debt consolidation or other consumer credit. Predatory lending occurs less often in the prime market where consumers have more credit options.

To develop the report and gather information, HUD and Treasury established the National Predatory Lending Task Force, of which ICBA was a member. However, Task Force members did not see the report before it was issued. The agencies also held public forums in Atlanta, Los Angeles, New York, Baltimore and Chicago to gather evidence on the nature and incidence of predatory lending practices. Participants included industry representatives, consumers, consumer advocates and local and state governments.

In the report, HUD and Treasury recommend that Congress, the regulators and states take new action to protect consumers, encourage healthy market competition and improve the information available to mortgage borrowers, especially in the high-cost mortgage loan markets where predatory practices are most likely to occur.

The report recommends four major areas for action: improve consumer literacy and disclosures, prohibit harmful sales practices, restrict abusive terms and conditions on high-cost loans, and improve market structure.

Some of the specific recommendations are:

- Creditors should be required to recommend home mortgage counseling to high-cost loan applicants and disclose credit scores to all borrowers upon request.
- The federal government should improve the financial literacy of mortgage borrowers, especially subprime borrowers.
- The Real Estate Settlement Procedures Act and the Truth in Lending Act should be amended to give borrowers more timely and accurate information on loan costs and terms.
- The Federal Reserve should use existing authority to prohibit abusive lending practices including loan "flipping" and lending to borrowers without regard to their ability to pay. Also, legislation will be needed to increase regulatory authority in this area.

- All mortgage brokers should be required to document the appropriateness of a loan for high-cost applicants and lenders should be liable for broker misconduct if they knew or should have known of the activity.
- Lenders that report to credit bureaus should provide full payment history for their mortgage customers.
- The sale of single-premium insurance products in connection with any loan should be outlawed.

The report also recommends amendments to the Home Ownership and Equity Protection Act (HOEPA), which governs high-cost loans, to expand its application to more borrowers and restrict balloon payments on high-cost loans. The agencies also recommend more restrictions on the use of prepayment penalties and the financing of points and fees for HOEPA loans.

The agencies believe that banks and thrifts should receive favorable CRA consideration if they "promote" borrowers from subprime to prime mortgages. Negative consideration would be given for originating or purchasing loans that violate applicable lending laws.

Some of the recommendations of HUD and Treasury may soon be implemented by heavier enforcement of existing laws and regulations by banking regulators. Others would require regulatory changes. HUD and Treasury plan to develop a legislative proposal to implement other aspects of their recommendations.

The ICBA has expressed concern to both HUD and Treasury about predatory lending and cautioned that solutions must be carefully crafted to avoid unintended consequences of restricting loan products that in the hands of responsible lenders can help first time homebuyers, underserved populations or other borrowers who might otherwise be unable to obtain a loan.