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U.S. House of Representatives
Committee on Financial Services
Subcommittee on Housing and Community Opportunity
Subcommittee on Financial Institutions and Consumer Credit
2129 Rayburn House Office Building
Washington, DC 20515

Re: "Legislative Solutions to Abusive Mortgage Lending Practices" Hearing

Dear Members,

Good morning distinguished members of the House Financial Services Committee, Subcommitees on Housing and Community Opportunity and Financial Institutions and Consumer Credit. It is my pleasure to submit to you this written testimony for your hearing entitled "Legislative Solutions to Abusive Mortgage Lending Practices" this 24th day of May 2005.

My name is Martina Guilfoil and I am the Executive Director of Inglewood Neighborhood Housing Services, as well as President of the National NeighborWorks® Association (NNA). NNA is the national membership association of the 230 NeighborWorks® Organizations throughout the country. NeighborWorks® Organizations work to revitalize over nearly 3,000 communities throughout the country, leveraging resources provided by congressionally-chartered Neighborhood Reinvestment Corporation (dba NeighborWorks® America). NNA members also utilize funding from CDBG, Section 8 and other federal funding to create and sustain economic wealth in low- and moderate-income communities across forty-nine states, the District if Columbia and Puerto Rico.

NNA's work relevant to this hearing includes mortgage counseling, pre- and post-purchasing counseling, individual development accounts and financial literacy programs. Our goal is to educate the low- and moderate-income homebuyer, many of who are first-time homebuyers, and provide them with the tools to *purchase* a home, but more importantly to *keep* their home. Our contribution to this hearing is underscored by the years of experiences our members have gained in advocating for the right to homeownership. Our members across the nation work tirelessly to educate potential homebuyers – we are in the trenches, counseling and advising homebuyers how to recognize the pitfalls of predatory lending.

NeighborWorks® organizations were created in the mid 1970's in response to the problem of redlining in communities across America. People were denied the credit they needed in order to improve their homes. NeighborWorks® made loans to families so that they could continue to live in safe and decent housing. Today the challenges we face have swung the other way. The challenge in our neighborhoods is not the lack of credit, but rather what someone will have to pay for it and under what terms. A variety of financial products have been created that jeopardize homeownership, the general financial stability of families and the health of neighborhoods. Predatory and abusive lending practices undermine the work of Inglewood Neighborhood Housing Services and its peer groups under the National NeighborWorks® Association. All members of NNA strive to combat predatory lending practices through the most effective instrument available – **EDUCATION**.

Financial literacy and pre- and post-purchase mortgage counseling have enormous positive impact in safeguarding those we serve against loan products that ultimately place them into a fragile economic position. The NeighborWorks® Campaign for HomeOwnership boasts default rates better than FHA and VA, and comparable with conventional lenders among homebuyers assisted, yet our achievements will become increasingly ineffective without strong anti-predatory legislation.

NNA members cannot possibly educate all unsophisticated and unaware homebuyers and homeowners. Most of those we serve do not hold the financial expertise and steadfast persistence required to understand the complexities of the mortgage loans being offered by lenders. Their journey is made even more difficult by designing lenders who prey on their inexperience and lack of financial knowledge. It is for this reason that a national anti-predatory law is necessary.

I would like to present some brief stories from our members across the country that describe the detrimental effects of predatory lending practices and their lasting impact. I relate these stories – stories you have no doubt heard several times over – to emphasize how the establishment of a strong national standard would serve to avert future stories of economic misfortunes from ever being told.

One of our groups in Mayville, NY, **Chaulauqua Home Rehabilitation and Improvement Corporation (CHRIC)**, details several of the most commonly used predatory lending practices still in practice today:

> John Thomas is a disabled, 43-year old African-American who received approximately $60,000 from insurance and Social Security benefits following the death of his wife and mother of his three children. He moved his family back to Dunkirk, NY, the place of his birth and a support network of family and friends. Mr. Thomas found a conventional mortgage with NorthWest Mortgage at a rate of 10.5 percent in December of 1997. He made a down payment of $28,000 on a $41,000 house. He invested another $16,000 in home improvements, painting, and furnishing his home for his children.
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> Mr. Thomas began a methodical effort to repair hazards and the home's electrical and plumbing systems. Lacking confidence that he could borrow from any bank (his personal bank had previously denied him a mortgage) Mr. Thomas called Household Finance through a flyer sent to him with a 1-800 number.
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> Household Finance told him they would make the loan, but wanted him to re-finance first. They told him they could refinance his home and give him a separate loan for home improvements. Mr. Thomas was aware there would be some cost, but did not know how much.
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> Household Finance re-financed the NorthWest mortgage at 11.99 percent in January 2000, explaining to Mr. Thomas that his interest rate would go down after two years. His 15-year term Northwest Mortgage with a monthly payment of $356 went to a 15-year term Household Finance mortgage with a monthly payment of $654. The second home equity loan carried an interest rate of 23.9 percent and a monthly payment of $272.

In May of 2001, Mr. Thomas made a payment of $641 on a principal balance of $58,970. After the payment was credited, his principal balance was still $58,970. All of the payment was applied to interest and "other charges". As CHRIC interviewed Mr. Thomas and reviewed his loan papers, the disclosure notices indicate that this mortgage was set up with a 15-year balloon payment. CHRIC had to explain to Mr. Thomas that fifteen years from the date of his loan he will be required to fully repay the balance or re-finance the unpaid balance with another mortgage.

Mr. Thomas feels like he has been duped. He has gone from a positive equity position to a negative one in a very short time. He blames himself in part, taking responsibility for making poor decisions. Yet he also feels that he was misled, deceived in part by lack of full disclosure, and encouraged to make bad decisions by persons with a financial self-interest.

Our group in Chicago, **NHS of Chicago,** has been at the forefront of creating strong Illinois state anti-predatory lending laws. The recently enacted state law has prevented future predatory practices like the one described below, from proliferating in the state of Illinois.

CS, a 70-year-old widow, has lived in her home in Chicago's Austin community for over 25 years. Her monthly income is $1,250 (Social Security and pension). From 1993 to 1998, CS obtained three separate loans from sub-prime lenders in order to make repairs to her home. By July 1998, her mortgage payments had increased to **$784.00** a month with a total mortgage debt of $68,000, but she was current on her payments. In July 1998, in an attempt to borrow $4,000 to repair her front steps, she responded to a mortgage broker's solicitation stating that loans were available in amounts up to 125 percent without need for income verification.

The mortgage broker told CS that she would need to borrow more than $4,000 to "make the loan worthwhile" and originated a $93,500 loan at a 12.5 percent rate, increasing her monthly P & I payment to $890.43, and depleting her equity by $25,000. In this transaction, the broker received a fee of $8,925 (9.6 percent of loan amount). There was an additional $1,500 in fees paid to the lender. All of these were included in the financing. With tax and insurance costs, CS' housing expense was now $**1,035** monthly.

Two stories from our group in Aberdeen, WA, **Aberdeen NeighborWorks® of Grays Harbor County** show that age, whether young or old, cannot prevent the unqualified from making poor decisions.

Two couples in their 70's and 80's who believed they were securing a reverse equity mortgage were given forward mortgages by Wells Fargo with payments that exceeded their repayment ability. They both ultimately lost their homes due to their inability to meet the high mortgage payments and were forced to leave their homes after 30 and 40 years. The information on both cases was sent to the Washington State Attorney General's office who is currently investigating the lender. Another couple with the same scenario but different lender was assisted in locating alternative housing after also not being able to maintain monthly payments on a mortgage refinance.

> A young first time home buying couple were days from committing to mortgage loans with predatory terms. The lender would create two loans (80/20), one with an ARM and a balloon payment in five years and the other with an extremely high interest rate. The combined monthly payments were a substantial portion of the couple's monthly income resulting in ratios outside customary, acceptable levels. We calculated and determined the young couple would have lost the house within six months as a result of inability to maintain the payments.

In Los Angeles County, our member-group, **Neighborhood Partnership Housing Services (NPHS)**, nicely illustrates the uninformed borrower.

> A homeowner came to NPHS to seek assistance on refinancing his second trust deed. The lender was carrying the paper and was charging 29 percent interest. The borrower felt the rate was high, but thought since it was a private loan, a higher interest rate was customary. NPHS assisted the borrower using a partner financial institution and completely refinanced for a reduced rate and better terms.

Members of the Committees - I cannot impress enough - predatory lending firms like Household Finance, Wells Fargo and others fully understand their predatory practices and the extremely high margins they obtain from exploiting the inexperienced homeowner or homebuyer. They have found a market niche to earn considerable profits. This niche, however, is clearly directed at exploiting the uninformed, unaware and in most cases, minority neighborhoods . How ever these firms may wish to defend their practices, any poor, elderly black man from Mayville, NY or young couple from Aberdeen, WA can quickly rebuff and tell you of the extraordinary deleterious effects of predatory lending.

Similar stories can be told by NeighborWorks® organizations across the country and in each of the districts you serve. In states and localities without strong anti-predatory lending, the result is clear: economic ruin for families. A strong federal law would substantially prompt abusive lenders to rethinking their business plans. The above anecdotal stories could have been avoided had there been a strong national law eliminating predatory lending practices. As various studies have shown, elimination of predatory lending does not entail an elimination of profitable subprime lending. A strong national law simply levels the playing field.

NNA does not ask that you enact burdensome legislation that extinguishes firms' profitable niches. Nor do we condone the argument of ignorance. We simply advise you to construct thoughtful and articulate legislation that serves a practical purpose – helping individuals purchase or refinance a home using clear and fair lending products and services that are more easily understood by the consumer. Congress must balance the benefits of economic enterprise with the obvious costs associated with that pursuit. For example, the Center for Responsible Lending estimates that abusive home mortgage lending practices cost homeowners $9.1 billion each year. During a session where members decry the potential loss of $4 billion-plus of the CDBG program, this $9.1 billion is worth your legislative attention. NNA urges Congress to enact legislation with provisions aligned with the recommendations set forth in this written testimony.

NNA and INHS vigorously support a national anti-predatory lending law that employs provisions similar to those found in current state laws, most notably, the state of North Carolina. Our membership supports a national law that serves as a floor, allowing states with more legislative safeguards to be excused from preemption by federal law. A more detailed synopsis of the provisions we recommend is included below.

On par with NNA's goal to educate homebuyers and homeowners, NNA suggests that any federal law enacted be sensitive to these critical areas: education and disclosure, transparency, reasonableness and fairness. NNA strongly encourages these legislative committees to err on the side of the consumer - as academic evidence and anecdotal hearsay illustrate, the consumer is the party left worse off.

Take away a predatory lender's ability to hide fees and subtle provisions and you promote an efficient and fair lending process. This levels the playing field for homebuyers who cannot understand all the complex aspects of the agreement to which he/she enters. It is reasonable for firms like Ameriquest and Countrywide to hedge the risk of borrowing to an individual with poor credit by pricing their loan accordingly. This does not, and should not, sanction the use of unreasonably high fees or penalties, deceptive lending practices, or exploitation of an interested, but unqualified borrower.

I encourage these committees to review my following recommendations and observations when debating the merits of a national anti-predatory lending bill.

- **Federal Floor**: States must continue to enact their own legislation based on the prevalence of predatory lending in their region – the niche described above is more easily exploitable in some markets. Therefore, in areas of substantial predatory lending practices (e.g. North Carolina pre-1999), more stringent state laws are necessary. A federal standard, especially a weak law, will do little in a predatory practice-heavy state whose laws have become pre-empted and therefore meaningless. States like North Carolina, Illinois, New Jersey and New Mexico have laws that have been proven effective. Eliminating these effective and fair laws by a preemptive federal law is as unwise as it is costly.

- **Full Disclosure and Education**: The homebuyer must be aware of how fees are accounted for in the loan, and at what price. The abusive and misleading practice of financing fees into the loan amount is essentially duping the homebuyer into an agreement no knowledgeable person would ever enter. As your colleagues in the Senate so judiciously acted to require full-disclosure of publicly-traded firms, so must be required of subprime lenders to borrowers. The lender must make efforts to determine the borrower's repayment ability. This entails information gathering and processing. Complete information is not only more economically efficient, it is also morally fair. It is unreasonable to apply the fallacious argument of "you should have known" to an eighty-year-old grandmother who repeatedly re-finances her mortgage (and incurs more fees) because she did not know any better.

- **Excessive Fees and Penalties:** There must be an economically-justified limit on penalties and fees. The law must appropriately balance the risk a lender assumes when financing an individual with poor credit with the fees charged to that individual. An individual must not be financially penalized *ex ante* for bad credit history and must certainly not be penalized, but rather encouraged, to pay on their mortgage in a timely fashion. For an individual to incur a prepayment fee as a "reward" for improving his/her credit is unacceptable. Fees must reasonably match the credit risk – nothing less is fair or prudent.

Thank you for the opportunity to share my thoughts and on behalf of NNA and INHS I thank you for your leadership in addressing this critical issue on a national level. If I can be of any service, please do not hesitate to contact me, or the Director of NNA, David C. Brown, dbrown@nnwa.us.