Testimony before the

COMMITTEE ON FINANCIAL SERVICES

Subcommittee on Financial Institutions and Consumer Credit

regarding

"An Examination of the Challenges Facing Community Financial Institutions in West Virginia"

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Madam Chairman and Members of the Committee, thank you for inviting Mountain State Justice to testify before you today on behalf of the low-income West Virginians we represent.

Mountain State Justice is a non-profit law firm committed to combating predatory mortgage lending in the state of West Virginia. Predatory mortgage lenders target low-income and minority homeowners and solicit these vulnerable consumers into loans that exceed the value of their homes and that contain excessive and/or adjustable rates of interest. Predatory lending practices, which result in impossibly high monthly payments for unsuspecting borrowers, make default and foreclosure likely on homes that have often been in families for generations. These practices also disadvantage honest and credible lending institutions, by enticing borrowers away from them and into exploitative loans based on representations that really are too good to be true. Mountain State Justice attorneys seek to protect West Virginian homeowners from foreclosure through state and federal litigation, specifically targeted at assisting individual homeowners and creating positive legal precedent.

Recent regulatory reform is not only necessary to protect West Virginia consumers, but also to level the playing field and enable community financial institutions to compete with national mortgage lenders.

Dodd-Frank and its Regulations Protect West Virginians

Mountain State Justice represents hundreds of consumers in active litigation stemming from predatory mortgage lending. As illustrated below, the predatory loans originated for our clients are designed to lead to foreclosure. Because our office is only able to represent a fraction of West Virginia homeowners facing foreclosure, changes to the law that alter the practices of the mortgage lending market are essential to protecting consumers. The Dodd-Frank Act specifically prohibits practices that were standard in the mortgage market beginning in the late 1990s. The following illustrations are real life examples of the hundreds of homeowners Mountain State Justice has seen suffer from similar problems.

<u>Unaffordable Loan</u>

For example, Jay and Annette Adame of Cool Ridge, West Virginia, were solicited by a broker to refinance their mortgage. At the time, Mr. and Mrs. Adame were current on payments for their fixed rate loan and initially refused offers to refinance. After repeated and aggressive telephone calls, Mrs. Adame ultimately agreed to refinance her home loan, relying on the broker's promise of a lower monthly payment. Unbeknownst to the Adames, the broker and mortgage lender provided a lower monthly payment by originating a PayOption Adjustable Rate Mortgage.

The note sets an initial monthly payment amount that is insufficient to cover the amount of interest, resulting in negative amortization. The fully amortized monthly payment amount is *higher* than the payment on the Adame's original loan. If the Adames make the initial monthly payment amount—the reduced monthly payment they were promised—the principal balance of their loan may rise to 115% of the original principal balance and result in a new minimum payment well in excess of the monthly obligation under their prior financing.

Not only did the monthly payment become unaffordable, as a result of the negative amortization, the principal balance equals or exceeds the value of the Adame's home, making it impossible to refinance. Without resort to litigation, Mr. and Mrs. Adame would have been foreclosed upon—simply because they trusted their mortgage broker and lender. This exploitative loan could not have been made under the provisions of Dodd-Frank, which prohibits making a loan without properly considering a borrower's ability to repay, a precaution that reputable community lenders have always taken.

<u>Fraudulent Appraisal</u>

Luke and Keveney Bair live in Sinks Grove, West Virginia, in the home Luke built on land adjacent to his parents' farm. A broker induced the Bairs to refinance their existing mortgage loan and consolidated unsecured debts into an adjustable rate mortgage by his promise to refinance their loan to a lower, fixed rate after one year. The broker and mortgage lender obtained an appraisal valuing the property at $160,000, when in fact, the property was only worth $99,000. In reliance on the fraudulent appraisal and promise to refinance, the Bairs entered a loan with an interest rate that started at 10.45% and may adjust upward to 16.45%.

In exchange for directing the Bairs to this loan product, their broker received a fee of $3,869.20 and an additional yield spread premium of $2,412.00. The broker failed to refinance the Bairs after the promised one year and the Bairs are unable to refinance with another institution because their mortgage loan is in excess of the value of their home.

The appraisal valuing the Bairs property in excess of its true market value violated many of the Uniform Standards of Professional Appraisal Practice. The Dodd-Frank Act requires that both appraisers and lenders ensure appraisals are performed fairly and accurately and prohibits the extra kick-backs to mortgage brokers of yield spread premiums that create incentives for brokers to originate loans for specific lenders, even if other lenders in the community might offer a better deal for the borrower.

<u>Unaffordable Loan and Fraudulent Valuation Secured by a Mobile Home</u>

Virginia Richards is an 83-year-old widow residing in Mammoth, West Virginia. Mrs. Richards received a solicitation in the mail informing her that she had been pre-selected to refinancing her mobile home loan to receive a lower monthly payment. The solicitation told her to skip her next payment and that she would have no out of pocket expenses. The lender failed to complete a valuation of Mrs. Richards's property, instead using the National Automobile Dealers Association book value for the make and model of the home and then *increasing* the amount well above the book value of the home by thousands of dollars, without any consideration of the actual features of the specific home. This practice erroneously assumed that mobile homes will appreciate from purchase; instead, mobile homes (unlike real property) depreciate over time.

Despite her high credit score, the lender provided Mrs. Richards a loan with an APR of 10.10%. The lender further added hundreds of dollars to Mrs. Richards's actual fixed income in order to qualify her for the loan. The lender further financed three years of property insurance premiums, causing Mrs. Richards's initial monthly loan payment to appear smaller. However, the principal and interest payment on the refinanced loan is higher than the principal and interest payment on her prior loan, and when the insurance premiums are due after the third year, Mrs. Richards's total monthly housing expense is significantly higher.

This loan is both unaffordable and for an amount in excess of the home's value. While the Dodd-Frank Act makes such practices illegal, it is crucial that these protections continue to cover manufactured and mobile homes.

The Dodd-Frank Act makes each of these three loans illegal. Under its provisions, the loans would never have been made and would never be sold to a reputable investor. The Consumer Financial Protection Bureau and the bank enforcement agencies would exercise oversight over lenders that attempted to make these loans.

The Dodd-Frank Act and its regulations work to remedy the mortgage foreclosure crisis resulting from a failure of regulation that allowed mortgage loans that were not affordable, not legitimately underwritten, and premised on fraudulent representations of value, rates, and promises to refinance. By eliminating predatory loans like the Pay Option ARM and yield spread premiums payable to brokers as well as strengthening requirements for valuation and determination of ability to pay, the Dodd-Frank Act provides essential consumer protection.

Regulation Levels the Playing Field and Enables Community Financial Institutions to Compete

The protections of the Dodd-Frank Act benefit community financial institutions by eliminating incentives for brokers to steer borrowers to national lenders and requiring national mortgage lenders to properly underwrite the loans they originate—just like our community lenders have always done. By doing so, the Dodd-Frank Act allows community financial institutes to compete for a larger share of the mortgage lending market, which benefits our clients, our communities, and our community lending institutions.

Conclusion

The Dodd-Frank Act means fewer West Virginians will lose their home to foreclosure resulting from predatory mortgage lending. I urge the members of this Subcommittee not to support repeal of any aspect of the Dodd-Frank Act and its consumer protections.