

August 14, 2006

Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551
Regs.comments@federalreserve.gov

Docket no: OP-1253

Dear Ms. Johnson:

The undersigned nonprofit groups, private firms and public agencies write in response to the Federal Reserve Board's (FRB) request for comments on issues relating to the FRB's recent hearings on the home equity lending market and the adequacy of existing regulatory and legislative provisions in protecting the interests of consumers.

Collectively, we are counseling agencies, community development corporations, legal service providers, advocacy organizations, housing providers, local government, private firms, research establishments, neighborhood community development initiatives and policy think tanks, all of whom are witnessing the devastating impacts of abusive lending practices on families, seniors, people of color, immigrants, low and moderate income households, and the communities in which they live.

In short, current protections are inadequate to protect consumers in California and elsewhere from abusive lending practices in the subprime, nontraditional and reverse mortgage markets. The Board can and must take action to blunt the impact of these practices which, at best, rob unsuspecting consumers of millions of dollars in valuable home equity and, at worst, propel homeowners into a downward spiral towards default and foreclosure.

We urge the FRB to take the following actions:

- 1. Require home loan counseling;**
- 2. Require translation of home loan documents;**
- 3. Strengthen HOEPA regulations and extend assignee liability;**
- 4. Expand HMDA and other regulatory requirements; and**
- 5. Develop and implement a suitability standard that will protect consumers.**

1. Require home loan counseling

Problem

Unscrupulous brokers and loan agents are aggressively selling exotic, risky loan products—including interest-only, option ARM (Adjustable Rate Mortgage) and stated-income loans—to borrowers who cannot afford homeownership and who do not understand their loan terms. With interest rates on hundreds of billions of dollars in loans scheduled to reset in the next few years, we know many will be unable to make their mortgage payments. As their payments dramatically increase, these borrowers will have a difficult time qualifying for refinance loans, and those who can refinance will face very high cost loans and steep prepayment penalties which, in California, will cost individual homeowners thousands of dollars in stripped equity. We anticipate that the result in California will be devastating, with huge numbers of families facing the loss of their hard earned assets as well as their homes.

The home loan process is complex and few homeowners in America fully understand all of their loan documents. To make matters worse, the consumers who are least familiar with financial transactions and most isolated from the financial mainstream are often the very borrowers targeted for today's higher-priced subprime, interest-only, option ARM, and reverse mortgage products, which are much more complex and have significantly more negative impact on consumers than conventional products.

Recommendations

- The FRB should require home loan counseling for all of these complex, high-risk, home loan products.

Mandatory counseling can level the playing field where loan sellers are pushing questionable products on unsophisticated consumers. Specifically, the FRB should require pre-transaction home loan counseling for all nontraditional loans, high cost home loans as defined by the Home Ownership and Equity Protection Act (subject to our recommendations for expanding HOEPA, below), and all reverse mortgages, where actual documents can be reviewed.

Several of the homeowners testifying at the FRB hearing in San Francisco on June 16, 2006, indicated that they probably would not have found themselves in their current difficult circumstances if they had had access to HUD-certified home loan counseling. Mandatory counseling would further the FRB's goals of promoting consumer understanding of their transaction, and fighting predatory practices. Home loan counseling is currently required for many reverse mortgage transactions, and certain states require counseling for certain complex home loan transactions.

- The FRB should work with Congress and other regulatory agencies to meaningfully increase funding for HUD-certified home loan counseling agencies.

Funding for counseling agencies is inadequate. Additional monies would build the capacity of the housing counseling infrastructure and provide more consumers with unbiased and qualified advice, enabling them to make educated decisions. This will inevitably result in a smoother, more efficient marketplace where buyers and sellers of loans knowingly enter into loan transactions. An educated consumer is less likely to be deceived, dissatisfied, financially harmed, or interested in litigation.

2. Require translation of home loan documents

Problem

The FRB should protect consumers from unscrupulous lenders and brokers who seek to take advantage of borrowers who have limited English proficiency. The San Francisco hearings also highlighted the pervasive problem of brokers and loan officers who sell loans in languages other than English. These negotiations are cemented at the closing table with a huge stack of English-only documents that borrowers do not understand, often include different terms than what borrowers were promised, and sometimes come with pressure by brokers and loan officers for borrowers to just sign and stop asking questions. Advocates and consumers testified directly to this issue at the hearings.

A common practice is for lenders or brokers to promise very attractive loan features. The borrowers trust their broker—who is usually a member of their ethnic community—to take them through the complex loan process. Borrowers are rushed or otherwise pressured by the lender or broker to sign documents without the ability to read or review them. If the borrower can somehow identify discrepancies, the lender or broker often coerces the borrower into signing with promises to “fix” mistakes, or even threaten legal action.

Recommendation

- The FRB should make it an unlawful and deceptive practice to provide English-only documents to a consumer where the lender or the broker has negotiated the home loan transaction in a language other than English.
- The FRB should develop guidance for lenders that builds upon California Civil Code §1632 to require that key loan documents, including but not limited to, the promissory note, HUD-1, TILA disclosure notice, GFE and Notices of Cancellation are available in the languages spoken in different markets, and that these translated documents be available through all retail and wholesale channels.

Otherwise, there is a basic failure of contract in that the consumer is not fully informed about the transaction and puts at risk what is almost certainly the largest asset he or she owns.

3. Strengthen HOEPA regulations and extend assignee liability

Problem

HOEPA represents the primary federal attempt to address predatory lending abuses in the high-cost home loan market. Unfortunately, many high-cost loans that are susceptible to abuse are not subject to HOEPA's protections. The limitations in the HOEPA regulations are a reflection of how today's market and today's abuses have outpaced the current regulatory scheme.

Specifically, when HOEPA was enacted, abuses were more likely to predominate in the refinance market. Today, we see an increasing number of abuses in the home purchase market. Additionally, the thresholds under HOEPA are unreasonably high and therefore do not provide coverage to more than a few loans, especially in California with our high housing prices. Further, subprime borrowers are much more likely to be stuck with yield spread premiums that reward brokers for charging them more, and prepayment penalties which trap them in bad and predatory loans.

Recommendation:

- The FRB should expand HOEPA so that it covers more loans, in the following ways:
 - Extend coverage of HOEPA to home purchase loans, as well as home equity loans that exceed \$10,000.
 - Lower the points and fees threshold to 5% of the total loan amount
 - Lower the rate threshold to 6% above comparable Treasuries
 - Expand the definition of points and fees to include Yield Spread Premiums and pay off of prepayment penalty provisions.

HOEPA is important in light of its unique position as a federal anti-predatory lending law. A main reason why predatory lending persists is that secondary market actors enjoy high returns on subprime loans, and have little interest in performing the necessary due diligence to ensure they are not financing predatory loans. HOEPA, with its assignee liability provision, can go far to protect vulnerable consumers if regulations can be tightened to expand its reach. The FRB has raised the issue of the secondary market in its proposed guidance on nontraditional loan products. We believe that secondary market actors must be included in any effort to restrict predatory lending, and a more relevant HOEPA framework could accomplish that. We also note that the Federal Trade Commission is reportedly investigating the secondary market practices of Bear Stearns' EMC unit, suggesting that this has become an increasingly important and visible issue.

- The FRB should prohibit prepayment penalties that extend beyond the loan's initial interest rate period.

At the hearing in San Francisco, it seemed there might be consensus on this point among consumer, industry, and FRB representatives. We believe that prepayment penalties are unfair, trap borrowers in bad loans, and are not sought or bargained for by consumers. Worse still is a common practice of loan sellers to tell apprehensive borrowers not to worry because they can always refinance if there are problems, thereby guaranteeing that a few thousand dollars in prepayment penalties will be incurred. Many products currently being sold in California will put borrowers in the position of seeing their monthly payments rise without being able to refinance out into a less expensive loan. Most borrowers do not understand this dynamic at all.

4. Expand HMDA and other regulatory requirements

The Problem

Borrowers of color, low- and moderate-income borrowers, and their neighborhoods are much more likely to get stuck with overpriced home loans. Our analysis of 2004 Home Mortgage Disclosure Act data revealed that minority neighborhoods in California were nearly four times as likely to get higher cost home purchase loans than nonminority neighborhoods, and we estimate that people of color in the state are paying millions more per month as a result of higher priced home loans. This dynamic means many homeowners are being robbed of additional equity they could have used to support their families, send a child to college, or plan for retirement. Anecdotally, and through testing by fair housing groups, we know that certain racial and ethnic and senior communities are targeted for problematic home loans.

Though HMDA data are designed to help identify discriminatory lending patterns, HMDA data have their limitations. Currently, HMDA data do not include key underwriting criteria that could better help regulators, the industry, and the public determine if unfair and discriminatory lending is occurring. Additionally, there is no information available through HMDA as to whether a homeowner is a senior, one of the primary groups targeted for home equity scams and predatory lending. Also of note is that the banking regulators are expressing concern about the impact of nontraditional mortgage products on underserved communities. Yet the HMDA data do not identify nontraditional loans, so that a stated income or negatively amortizing loan made to a low-income Latino household in a minority neighborhood will look like a prime loan that could qualify for Community Reinvestment Act credit.

In addition, when the FRB released the 2004 HMDA data with new pricing information, it provided some interesting analysis to help explain the data. Amongst other findings, the FRB staff noted there were lending disparities that showed race and ethnic groups were more likely to receive higher priced home loans, but that these disparities were reduced within a bank's Community Reinvestment Act (CRA) assessment area. In other words, where banks had CRA responsibilities subject to regulatory oversight, their lending appeared to be more equally and fairly distributed. Yet at the same time, the bank regulators have allowed certain companies such as H&R Block Bank, Countrywide Bank,

and Charles Schwab Bank to minimize their CRA responsibilities to a small fraction of the communities where they lend money.

Recommendation

- The FRB should expand Home Mortgage Disclosure Act reporting requirements, so more data are available to better detect areas of discrimination, specifically by including: credit score; loan-to-value and debt-to-income ratios; the age of the borrower; and whether a loan is a nontraditional loan.
- The FRB should expand CRA requirements to promote fair lending. Specifically, the banking regulators should revise outdated definitions of what constitutes a “branch” subject to CRA responsibility, by looking at where banking companies lend and where their depositors live.

5. Develop and implement a suitability standard for loans that will protect consumers

Problem

As discussed above, complex and harmful loan products are being sold to unsuspecting consumers. Yesterday, we were alarmed by high-cost subprime loans that did not reflect borrowers’ credit profiles. Today, we are talking about nontraditional loan products. Tomorrow, there will likely be new practices and products that have the potential to threaten consumer wealth and assets.

Recommendation

- The FRB should develop meaningful suitability standards that protect borrowers from being pushed into loans that are not suitable to them. The FRB should seek Congressional authorization to accomplish this if that is deemed necessary.

As one example, industry representatives assert that stated-income loans are appropriate for certain consumers, perhaps those who cannot easily document their income. But even if that were true, we know that this product creates massive opportunities for abuse by some unscrupulous brokers and lenders. The stated-income feature allows some brokers to state borrowers’ incomes in a manner designed to make a deal happen—regardless of whether the loan is appropriate for the borrower—and increase broker fees.

We understand that there is discussion about creating a suitability standard for home loans akin to what exists in the securities realm. We support the development of such a standard that would force loan sellers to ensure that a given deal is appropriate for that given borrower, given the totality of that borrower’s circumstances and profile. Where unsuitable loans are sold, as is rampant today, borrowers must have meaningful redress.

We write with a sense of urgency. Homeowners in California and elsewhere are suffering at the hands of unscrupulous industry actors. Current regulations are insufficient to protect consumers who are stripped of their home equity and often lose homes they have worked hard to buy. We urgently request that the FRB follow up on the hearings with decisive action that will better protect consumers.

Thank you for your consideration of these views.

Signed

California Coalition for Rural Housing (Sacramento)
California Community Economic Development Association (Los Angeles)
California/Nevada Community Action Partnership (Sacramento)
California Reinvestment Coalition (San Francisco)
City of Oakland
Civic Center Barrio Housing Corporation (Santa Ana)
Community Financial Resource Center (Los Angeles)
Community Housing Development Corporation (Richmond)
Community Housing Opportunities Corporation (Davis)
Community Legal Services in East Palo Alto, Inc. (East Palo Alto)
Consumer Action (San Francisco)
Daniel M. Leibsohn, Consultant (Oakland)
East Bay Asian Local Development Corporation (Oakland)
East Palo Alto Council of Tenants Education Fund (East Palo Alto)
EPA CAN DO (East Palo Alto)
Esperanza Community Housing Corporation (Los Angeles)
Fair Housing Council of San Diego (San Diego)
Fair Housing Council of the San Fernando Valley (Panorama City)
Fair Housing Law Project (San Jose)
Fair Housing Napa Valley (Napa)
Fair Housing of Marin (San Rafael)
Fair Lending Consortium (San Francisco)
Fresno Housing Alliance (Fresno)
Fresno Interdenominational Refugee Ministries (FIRM) (Fresno)
Housing and Economic Rights Advocates (Oakland)
Housing Rights Center Southern California (Los Angeles)
Ingrid M. Evans, Esq. (San Francisco)
La Raza Centro Legal (San Francisco)
Law Center for Families (Oakland)
Legal Aid Foundation of Los Angeles (Los Angeles)
Legal Aid of Marin (San Rafael)
Lenders for Community Development (San Jose)
Low Income Investment Fund (San Francisco)
Making Connections Oakland (Oakland)
Mercy Housing California (San Francisco)
Mid-Peninsula Housing Coalition (Foster City)

Mission Economic Development Agency (San Francisco)
Monterey County Housing Alliance (Salinas)
Mortgage Brokers Association for Responsible Lending (Burlingame)
Moses Diaz, Esq. (Visalia)
National Economic Development & Law Center (Oakland)
NID-Housing Counseling Agency (Oakland)
Non Profit Housing Association of Northern California (San Francisco)
NORCAL-FDC (Oakland)
North Bay Aging Adult Services (Napa)
Oakland Association of Insurance Agents (Oakland)
Orange County Community Housing Organization (Santa Ana)
Palo Alto Housing Corporation (Palo Alto)
Public Advocates, Inc. (San Francisco)
Public Interest Law Firm (San Jose)
Rural California Housing Corporation (Sacramento)
San Diego Coalition for Fair Banking (San Diego)
San Diego Housing Federation (San Diego)
Sentinel Fair Housing (Oakland)
The Community Housing Council of Fresno (Fresno)
The Fresno Housing Resource Center (Fresno)
Vermont Slauson EDC (Los Angeles)
West Berkeley Neighborhood Development Corporation (Berkeley)
Western Center on Law and Poverty (Los Angeles)