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January 8, 2008

Jennifer J. Johnson, Secretary
Board of Governors
Federal Reserve System
20th Street & Constitutional Ave., N.W.
Washington, D.C. 20551

RE: PROPOSED REGULATION Z (AMENDMENTS TO:)
12 CFR PART 226
DOCKET NO. R-1305
TRUTH-IN-LENDING ACT.

A) **MORTGAGE DOCUMENTS SIMPLIFICATION:**

See attached Legal Aid Society LAS No. 1, hereinafter submitted as **Exhibit "A".** Exhibit "A" was used to assist in the training of mortgage counselors by the Legal Aid Society, and at public forums. Mortgage Document Simplification was recommended also by U.S. Treasury Secretary, Henry M. Paulson, Jr. However, the Chairman of the Federal Reserve Board of Governors should also advocate for this reform directly to the 50 State Banking Superintendents.

B) **THE CLOSING AGENT DUTIES:**

See LAS No. 2, 3, 4, 5, 16, and 30. Regulation "Z" should state in some detail, the various "duties" of a mortgage "Closing Agent" and offer some specific fact patterns for guidance. LAS No. 6 should also be referred by the Chairman of the Federal Reserve Board of Governors to the American Bar Association (Chicago) for study and comment within 90 days since local attorneys are frequently present at critical stages of mortgage closing preparations.

C) **PRIX FIXE (FLAT FEE) CLOSING COSTS:**

See LAS No. 7, 74, and 75. This HUD initiative to rein in junk fees would resolve one of the mortgage industries commonly known "unfair, abusive and deceptive practices" and the Chairman of the Federal Reserve Board of Governors should refer to HUD Secretary, Alphonso Jackson, for Secretary Jackson 90 day HUD comment. The FRB should offer also, for a public comment, HUD's own proposed regulation, now in draft form, and written in 2002 as a proposed HUD regulation on flat fee closing costs.

D) INDEPENDENT "COMPLIANCE OFFICERS":

See LAS No. 15, 29, 37, 40, 42, 43, 64, 67, 68, 70 and 71. See also New York State Banking Regulation Part 410(d) attached as **Exhibit "B"** that could in some form be included in Regulation Z.

E) YIELD SPREAD PREMIUMS (YSP) DISCLOSURE: (SEE LAS No. 24, and 49)

The "Yield Spread Premium" is not a consumer friendly word or plain English. It is a most deceptive choice of a financial descriptive title for a supplemental or enhanced mortgage broker's fee or commission, or legal kickback. The borrowers in this nation deserve a better descriptive term. Request the National Consumer Law Center (NCLC) or The Center for Responsible Lending to also suggest a better term for this much discredited and abusive fee or broker commission.

F) UNCLEAN HANDS: WHO CERTIFIES A MORTGAGE BROKER'S COMPLIANCE WITH REGULATION Z AT THE CLOSING TABLE:

A sordid history existed of mortgage broker "closing agents" lack of "timely" and written certification or full compliance by the closing agent, with state and federal "Time Standards" of RESPA Disclosure requirements (see LAS No. 30). Timely disclosure was not present in almost every borrower "complaint" reviewed by the Legal Aid Society. The borrowers themselves, were not aware of "Notice" requirements. A written "check list" with time requirements should be provided by each closing agent to the borrower with the Good Faith Estimate (GFE) of Closing Costs. This "check list" should be drafted by the Federal Reserve Board and included in Regulation "Z".

G) THE TRUTH-IN-LENDING FEDERAL DISCLOSURE STATEMENT:

See LAS No. 32 and 38 which current federal Truth-in-Lending statement was only submitted to the borrowers at the last minute in these three (3) sample ARM closings described in LAS No's 32 and 38. The GFE was concealed in one predatory closing (until closing day) among seventy (70) legal size documents. Though the FRB "proposed" regulations call for disclosure of a schedule of payments three (3) days after applications the final **Federal Disclosure Statement** should also be provided 3 days before closing. It is that important a document and could provide another opportunity for counseling by the borrower. This Federal Disclosure Statement, and the Good Faith Estimate of closing costs should contain an appropriate warning notification given below in paragraph "L", and a Counseling Rights Statement (given below in paragraph "Q-2").

H). DIFFICULTIES ADJOURNING A CLOSING WHEN A BORROWER APPEARS AT THE CLOSING TABLE. THE PSYCHOLOGY USED BY THE MORTGAGE BROKERS TO CLOSE.

This difficulty should be stated in a "Preamble" to the proposed regulations. For example, closing agents in subprime loans come prepared to close in 15 to no more than 30 minutes. These closings in many cases in New York State may involve up to 70 legal size pages of documents for an unrepresented borrower to read, to review, to sign and or to initial. Even an attorney as a borrower, would find this task impossible. In most refinance mortgage closings in New York State, the borrower does not have counsel present and has not previously seen all or any of the closing documents. In one reported case of a first house purchase, the borrower was warned by a knowledgeable person that the mortgage brokers promise of a 30 year "fixed rate" was probably false. The forewarned borrower then called the mortgage broker three (3) times to confirm the terms and was repeatedly assured it was a 30 year "fixed rate". At the **first closing** (with the seller and others present) the borrower was presented with an ARM mortgage which he refused to sign and the closing was adjourned to redraft the mortgage papers to a "fixed rate". At the **second closing** the borrower was again presented a revised ARM rate, not the fixed rate both promised and repeatedly confirmed by telephone. It was only at the **third closing** table that the mortgage broker finally revised the documents to a "fixed rate". These scams were common and a "pattern and practice" in too many closings, because the mortgage broker did not provide the Federal Truth-in-Lending Disclosure Statement before the closing.
See LAS No. 45 on the psychology used at a mortgage closing and LAS No. 77, 78, and 78(b) on the subprime markets "collateral damages" which should also be made note of by Regulation Z in its Preamble.

I) The Preamble to the proposed Truth-in-Lending Regulations (Docket R-1305) should identify and or describe the descriptive terms mortgage brokers used to identify these junk mortgages (see LAS No. 52, 53, 54, and 55).

J) PREPAYMENT PENALTIES A/K/A EXIT FEES:

NEW MORTGAGE: Traditionally these penalties were payable in 3 to 5 years if the borrower refinanced. The New York State Banking Department Regulations had a better idea in limiting them to one year **(see Exhibit "C")**.
OLD MORTGAGE: The mortgage broker in a refinance should also be required to disclose and notify the borrower if a prepayment penalty is due to the prior mortgage holder and when it will expire. This is a "closing cost" rarely fully disclosed until the last minute to avoid a borrower waiting for the old prepayment penalties expiration. It's a deceptive practice that needs to be addressed early by Regulation Z Disclosure in the Good Faith Estimate of Closing Costs.

K) A WALL STREET TASK FORCE:

The Federal Reserve Board of Governors Chairman could request Wall Street Executives, John A. Thain, President, Merrill Lynch and Robert E. Rubin, (Citibank Director) to advocate for a Wall Street "Task Force" to recommend Wall

Street oversight and good business practices and lender due diligence standards before using the bond markets as a conduit for mortgage backed securities. America needs mortgage backed securities and bonds for liquidity in the credit mortgage markets. European and American investors need new Wall Street voluntary good business standards before foreign bank investors will enter this American mortgage backed security market again. The U.S. dollars recovery also depends on a Wall Street initiative. See LAS No. 73, 74, 75 and 80 recommendation for a Wall Street Task Force. The Federal Reserve Board of Governors need to reach out more often in this crisis to other government agencies and private groups. Regulation Z by itself is not enough.

L) All mortgage documents forwarded to a borrower before the closing should state the following in dark print at the top of the page.

Warning: "this document may contain legal and financial terms, or conditions, or disclosures that a layman may not adequately comprehend. You may seek the advice of a private attorney, or a local legal services agency, or your State Banking Superintendent for the names of free pre-closing mortgage counseling agencies in your area"

M) Regulation Z should state that every Mortgage Broker and /or lender should provide the "toll free" number of the local State Banking Superintendent with the first mailing when submitting to the potential borrower the "Good Faith Estimate" of Closing Costs.

N) (HOEPA)HIGHER PRICED MORTGAGE LOANS:

The proposed regulations permitting borrowers to "opt out" of tax and insurance escrows 12 months after a mortgage closing should take into account other factors. The regulations may consider a 24 month "opt out" as a more conservative approach. This 24 month payment period would allow the borrower to experience the monthly mortgage installment and family budgeting, especially where additional home equity funds were taken in cash at the mortgage closing and are being used to pay the initial 12 months of mortgage monthly installments.

O) EARLY DISCLOSURE OF ESTIMATED ESCROW: FOR TAXES AND INSURANCE:

If the borrower voluntarily "requests" an escrow of taxes and insurance this monthly increase based on a good faith estimate of taxes and insurance should be disclosed as early as possible, in writing to the borrower, or a minimum five (5) days before closing. The lender or mortgage broker must discuss this escrow need at the first meeting with the borrower. It should be the lender or mortgage broker's "fair dealing duty" to bring up this topic early in the loan application process.

P) "Time Limit" On Disclosure Requirements:

Under regulations allow an additional day for mailing if placed in a U.S. or Fed Ex Postal Box before 5 p.m., and an additional two (2) days if placed in a U.S. or Fed Ex Postal Mail Box after 5 a.m. If faxing or E-mail is used, Regulation Z should provide that a mailed copy should always follow the faxed or E-mail copy. This mail "back-up" notice standard is always used in the service of a summons, if not previously personally delivered.

Q) Federal and state banks, financial houses, other national and state major mortgage lenders claim they were "clueless" as to the "toxic loans" and "junk fees" that were being sold by mortgage brokers to home purchasers and to homeowners refinancing a prior mortgage.

Recommendation:

1) The U.S. Federal Reserve Board of Governors (FRB) and the U.S. Housing and Urban Development (HUD) and the Federal Trade Commissions (FTC) and even the U. S. Treasury Department have an obligation to set forth a formal written Standard or Code of Good Business Practices for mortgage lenders and mortgage brokers under FRB and HUD regulatory jurisdiction. Note: Even the FTC has a 3 Day Right of Cancellation for home refinances and home Improvement loans. (Please draft within Regulation Z, an inter-agency standard, or code.)

2) Furthermore, the "Consumer Rights" of the home borrower or home purchaser should also be clearly set forth in a borrower's Bill of Rights in order to further empower the borrower, and a copy given to each mortgage borrower with the "Good Faith Estimate" of Closing Costs. Therefore provided the following "Borrower Bill of Rights" to each mortgagee borrower with the GFE of Closing Costs:

You Have The Right To An Honest Lender or Mortgage Broker:

Your mortgage broker and lender may not, at any time, deceive or mislead you in any way about any aspect of the terms of the mortgage on your home, or about any aspect of the financing, and in particular, your mortgage broker must not:

- Deceive or mislead you in any way about the value of the house;
- Deceive or mislead you in any way about the total closing costs for the mortgage;
- Deceive or mislead you in any way about the monthly mortgage installment payments and monthly escrow payments for estimated taxes and insurance;
- Deceive or mislead you in any way about the pre-payment penalties prior or current;
- Deceive or mislead you in any way about the full and complete terms of the mortgage including the interest rate;
- Deceive or mislead you in any way about the nature of any document the mortgage broker or lender asks you to sign, or to read; and/or fail to provide you ample opportunity and time to read;
- Deceive or mislead you in any way about your rights and future responsibilities before, during, or after the closing of the mortgage.

- Deceive or mislead you in any way about your right to outside free mortgage counseling;
- If you suspect your mortgage broker or lender has deceived or mislead you, you may bring legal action against the lender or mortgage broker for recovery or the fees, commissions, points, cost of the mortgage, and/or other losses.

R) COMPULSORY MORTGAGE COUNSELING: **(See Exhibit "D")**
Also it is important to note that:

- A Reverse Mortgage requires outside counseling.
- The U.S. Bankruptcy Law requires outside counseling before filing.
- Counseling in many locales is permitted by telephone and or in person.
- Even Washington Mutual Bank **(Exhibit "E")** has volunteered to call (prior to closing) every Washington Mutual Bank borrower being represented by a mortgage broker to **"ensure the borrower fully understands the terms of the loan their broker is requesting "in addition to the total compensation the borrower will pay to the broker for their broker services".**

S) **Question: Why the RESPA Law failed borrowers, and why the Mortgage Brokers ignored RESPA.**
Answer: There were no civil monetary penalties, fines, or forfeitures for serious violations, (see LAS No. 75 and 79(d)).

Forfeitures might be a good start. May I suggest:

- Broker Yield Spread Premium **Forfeiture**
- Points (Broker Commission) **Forfeitures.** Prepayment Penalty: **Forfeiture.**
- Brokers Attorney fee: **Forfeiture.**
- Brokers Application fee: **Forfeiture.**
- Broker Origination fee: **Forfeiture.**
- Broker Discount fee: **Forfeiture.**
- Broker Underwriting fee: **Forfeiture.**
- Broker Document preparation fee: **Forfeiture.**
- Broker Processing fee: **Forfeiture.**
- Broker Departmental fee: **Forfeiture.**
- Lender Review fee: **Forfeiture.**
- Brokers who falsify a borrower's income or assets or resources: **$10,000.00** fine.

Conclusion:

In the new financial world we now live in, "counseling" should be the rule, not the exception. Furthermore, The Federal Reserve Board of Governors, and Chairman, Ben S. Bernanke should take a more pro-active public relations approach and also reach out to the 50 State Governors , and to other state and federal agencies to consolidate on the record, a more comprehensive unified Consumer Protection, and Disclosure" approach to this crisis. Past strong Truth-in-Lending Legislation, past

Regulation Z rules, past RESPA legislation, and past HOEPA legislation apparently failed in this crisis.

It has been 34 years (1974 to 2008) since the RESPA Act was enacted. RESPA was a good law that was ignored by the new breed of mortgage brokers. The RESPA law enacted in 1974 and placed in the federal Truth-in-Lending Act (TILA) 12 U.S. Code 2601, stated in part:

"Preamble"

§ 2601. (a) The Congress finds that significant reforms in the real estate settlement process are needed to insure that consumers throughout the Nation are provided with greater and more timely information on the nature and costs of the settlement process and are protected from unnecessarily high settlement charges caused by certain abusive practices that have developed in some areas of the country. The Congress also finds that it has been over two years since the Secretary of Housing and Urban Development and the Administrator of Veterans' Affairs submitted their joint report to the Congress on "Mortgage Settlement Costs" and that the time has come for the recommendations for Federal legislative action made in that report to be implemented.

(b) It is the purpose of this chapter to effect certain changes in the settlement process for residential real estate that will result-

(1) in more effective advance disclosure to home buyers and sellers of settlement costs;
(2) in the elimination of kickbacks or referral fees that tend to increase unnecessarily the costs of certain settlement services.

This time The Federal Reserve Board, and Chairman Bernanke in official statements and official speeches, has to reach out to the states with more than Regulation Z to bring this mortgage fraud under control. Even the European Financial Regulators are demanding comprehensive reforms in the U.S. and 50 state mortgage systems. The states have to be partners with the Federal Reserve Board in this reform.

Respectfully submitted,

James P. Carr
Legal Aid Society of Suffolk County

EXHIBIT A

LEGAL AID SOCIETY OF SUFFOLK COUNTY, INC.

SOME REFORM AND/OR DISCUSSION IDEAS FROM THE LEGAL AID SOCIETY TO ADDRESS CERTAIN ABUSIVE LENDING PRACTICES THAT HAVE DEVELOPED IN THE RESIDENTIAL REAL ESTATE MARKET AND THE BOND MARKETS

WHY THE MARKET DOES NOT WORK:

Banks, Lenders, Investment Firms, Mortgage Brokers and the Homeowner

-SOME REFORM AND/OR DISCUSSION IDEAS FROM THE LEGAL AID SOCIETY TO ADDRESS CERTAIN ABUSIVE PRACTICES THAT HAVE DEVELOPED IN THE RESIDENTIAL REAL ESTATE MARKET:

(1) **Mortgage Document Simplification:** An unrepresented client's complaint: she could not read, or comprehend seventy (70) legal size mortgage pages at a mortgage closing. Why not "fax" or mail, or deliver documents to the borrower prior to the closing, so the borrower may read them in their entirety, before the closing day, or seek legal advice on these very confusing legal documents while in the consumers hand. Why not also reduce the size of the documents to simplify them for a lay person. Include all blank and typed documents, and even a sample of the Three (3) Day Right of Cancellation. Mortgage closings involve very large sums of money, and most subprime mortgage customers are not represented by counsel. Secretary of the Treasury, Henry M. Paulson, Jr., recently announced his support for mortgage document simplification.

(2) **The Closing Agent** (in New York State, its generally an attorney) should have a quasi-fiduciary, or "fiduciary duty" or "special duty" to the unrepresented homeowner-borrower both before the closing, and again at the closing. (See also No. 4, below for the Special Duty.)

(3) **Lender's attorneys (or any attorney) attending a closing,** should have a new ethical standard or guideline for mortgage closing practices mandated by the State or National Bar Association, separate and apart from the lender's "Closing Agent" Duty of Full and Fair Disclosure. All parties should also have a "Special Duty" to unrepresented borrower as described in paragraph 4 below. The ethical obligation of any attorney is, of course, never to remain silent, in the face of written, or oral misrepresentation, or to be silent where a statutory Duty to Disclose exists. As former **Brooklyn Foreclosure Prevention Project** Director, Raun J. Rasmussen, Esq., in a New York Law Journal article dated February 4, 1998 stated:

> Even silence in the face of misrepresentations by the broker may be actionable, if it can be shown that the attorney (for the broker) "induced" the borrower to rely on his or her advice…
>
> When only the lender has a lawyer, and while the lawyer sits silently while the broker claims that the lawyer can "take care of" both lender and borrower, the lawyer's conduct approaches the illegal "inducement" discussed above.
>
> If the lawyer, instead of sitting silently, smiles and reassures the borrower that "everything will be all right," a claim may be even stronger. When you add an unsophisticated borrower to the mix of a complicated legal transaction, the lender's lawyer would be wise to encourage the borrower to get her own counsel…
>
> Thus, a lender's lawyer should not encourage a borrower to sign documents, or explain the contents of those documents if asked. Those opinions and conversations are usually intended to encourage

the borrower to proceed with the closing, a result beneficial to the lender, but not always to the borrower.

(4). **The Closing Agent Certification:** Both lawyers and non-lawyers acting as closing agents should sign a **Certificate** acknowledging that a fiduciary or quasi-fiduciary duty, or a **special duty,** in the creditor-debtor relationship exists between the lender-broker, and the unrepresented homeowner-mortgagor. The National Consumer Law Center (NCLC) states that the "closing agent's special duty" should encompass a duty of fair and honest disclosure of all facts which might be presumed to influence the borrower in regard to said borrower's actions, including those favorable to the creditor or third party and, especially those **adverse** to the borrower's interest. Source: **The National Consumer Law Center's Legal Advocates Guide: Stop Predatory Lending.** (2002, page 31)

(5) **A Closing Attorney and Conflicts of Interest:** In New York State, the closing attorney for a mortgage broker is generally paid directly at the closing by the mortgage borrower. In many states the closing agent (a non-attorney) may also be similarly paid. The conflict of loyalties and conflict of interests arise in that it may be monetarily in the best interest of the closing "attorney" and closing "agent" to see the closing process completed. However, the many thousands of complaints from borrowers, and the many thousands of defaults that are occurring, seem to indicate that the following **three (3) duties** had <u>not</u> been met:

- Duty of Fair and Honest Disclosure of facts that might influence the borrowers decision.
- Duty of Full and Fair Disclosure of all facts adverse to the borrowers interest.
- Duty of Good Faith and Fair Dealing to a contract based on both common law and New York State Unified Commercial Code.
- Silence by the closing agent in the face of patent or open misrepresentations by the mortgage broker violates the aforesaid three (3) duties.
- In all Predatory Lending closings, failure to postpone the closing until the unsophisticated borrower has had counseling by an independent attorney or mortgage counseling agency may violate the aforesaid three (3) duties.
- In all Subprime Lending closings, the borrower's ability to repay needs to be both discussed and verified by "due diligence" of the mortgage broker.

(6) **Silence of Multiple Attorneys at a Predatory Closing:**

Even attorneys only representing the prior recorded mortgage holder or representing another credit lien holder, when attending a closing to either pick up a check, or to submit a satisfaction of a lien or mortgage satisfaction, must also speak up when faced with an obvious predatory closing. Silence is not an option for any experienced professional in the closing room.

(7) **Closing "Costs" should be "prix fixe" or flat fee closing cost.** Due to technological data advances, the required closing cost disclosure can always be disclosed upfront even before the loan application is signed. Early disclosure also, of the "name" of the person or entity, or company collecting closing fees should be mandatory, and submitted to the borrower before the closing with the Good Faith Estimate (GFE). Many federal banks and state banks today, disclose all closing fees (pre-printed charts) to any "walk-in" customer and recently used guaranteed flat fees. Closing costs can always be forecasted in advance by the size of the estimated mortgage and preprinted as a future consumer handout even before the customer contacts the mortgage broker. Junk fees, duplication fees, and unearned fees masked as closing costs, are not uncommon in mortgage broker consumer complaints. The mortgage broker's industry has never policed itself, and state regulation is needed there.

(8) **Early Disclosure** up front of any **"pre-payment penalty"** in a "refinance" should be required before an application fee is paid. A pre-payment penalty owed to a prior mortgage holder exceeding 1% of the new mortgage should require a referral at the option of the borrower, to an outside budget counseling agency. "Mortgage flipping" resulting in a prepayment penalty is not always in the best interest of those not financially astute. The NCLC states that mortgage loans with pre-payment penalties often include a "yield spread premium" fee payment by the lender to mortgage broker (see paragraph No. 24 below).

(9) A **borrower's "ability to re-pay"** must be paramount and certified by the mortgage broker and by the closing agent, and verified by the mortgage broker's closing attorney in any mortgage closing which was, and is in 2007, the major failure to perform on the part of the subprime mortgage market, subprime brokers, and their employees. It is the major failure of today's mortgage brokers to act ethically, and fairly. Improvident lending, when combined with an adjustable rate mortgage (ARM), is a breach of the Duty of Good Faith and Fair Dealing. The NCLC defines two (2) typical ARM mortgages as follows:

> **Payment Option ARM (adjustable rate mortgage)**
> A mortgage that allows a number of different payment options each month, including very minimal payments. The minimum payment option can be less than the interest accruing on the loan, resulting in negative amortization.
>
> **Exploding ARM (adjustable rate mortgage).**
> A common type of "hybrid" ARM in the subprime market that includes both a fixed and adjustable-interest rate component. A "2/28" hybrid ARM comes with an initial short-term fixed interest rate for two years, followed by rate adjustments, generally in six-month increments for the

remainder of the loan's term. Typically the introductory rate is artificially low, giving homeowners a dramatic increase in housing costs after the introductory period expires.

(10) **ARM Mortgages and the Low Income Borrower:** Low income borrowers should not be given an ARM mortgage without access to voluntary outside third party counseling. The Legal Aid Society recommends possible use of the existing counseling agencies now counseling (without fee or charge) "Reverse Mortgage" applicants, or HUD-certified housing counselors. Reverse mortgages "counseling" is one of the bright lights in our modern mortgage market today. Even federal bankruptcy courts now require counseling as a first step in bankruptcy. These certified third party counselor agencies are always good sources of potential counselors for subprime mortgages. However, the counseling cannot be beneficial or successful unless the borrower has received from the broker, all the mortgage papers, mortgage terms, and closing costs. (see paragraph 32 below).

(11). **<u>Summary:</u> Not all subprime mortgages are predatory, nor are all predatory mortgages subprime.** The key component is, did the lender or mortgage broker, and the mortgage broker's attorney, and the mortgage broker's closing agent consider the borrower's "ability to re-pay", and was "full and fair disclosure" of documents made to the borrower with sufficient time to allow the borrower, if necessary to withdraw. Failure to reveal and accurately disclose the rate of interest, terms of payment, costs of closing, monthly installment amount, and time to adequately review drafted documents for the closing all upfront, are the most common "unfair and deceptive practice complaints" of consumers. Without this information, (see Paragraph 32 below) even third party counseling would be fruitless. Whether procedural or substantive, the duty of "good faith and fair dealings" between parties to a contract is based in common law, and based federal law, and on the New York State Uniform Commercial Code, and other New York State Consumer Laws, all of which should be incorporated into future reforms.

(12) **Some "Good News" for Pooled Mortgaged Backed Securities: (MBS)** Keeping the mortgage principal reasonably intact through Modification Agreements, Work-out Agreements, Forbearance Agreements, and as a last resort, a voluntary Deed- Over with a Sale or Short Sale where the lender agrees to accept the proceeds of the "short sale" in full satisfaction of the mortgage may be in the best interest of the investors, the homeowners, and the financing markets. Foreclosure of a mortgage loan or "writing off", the loan by the lenders and, or selling the "mortgage deficiency" (after a referee sale) to national debt collection agencies, or discounting any part of the defaulted pooled mortgage backed loans is not the most desirable practice. Early resolution with the homeowner is less costly than litigation.

(13) **Various Modification and Work-Out Safety Valves are Available:** Nationwide, there are 350 non-profit legal services offices that the Mortgage "Servicing Agent may, in many cases, refer homeowners in default when the homeowner is more than three (3) months in arrears. FHA/HUD also has used independent foreclosure counseling agencies for years.

(14) **Liability for a Mortgage Brokers Unfair and Deceptive Practices:** Deceptive Practices employed in predatory mortgage lending deceives not only the homeowner, but also the bond markets, and ultimately, its investors. Those closing agents who knowingly "structure" these predatory mortgage closings for deceptive mortgage brokers may also be equally liable as **Aiders and Abettors**, and that may include the mortgage broker attorneys. The US Supreme Court in a pending case in its up coming term may address the factual definition of "Aiders and Abettors".

(15) **Designated Independent "Compliance Officers" are now needed at large Mortgage Broker Offices and Should be Required by State law.**
It is now apparent that mortgage brokers cannot or will not "police" their own work force. Bond companies, security companies, banks, mutual funds, public companies all have "Compliance Officers", yet the first link in this pooled mortgage-backed securities chain, the subprime and prime mortgage brokers, have no Compliance Officers to see that their sales and closing staff are all trained, and adhering to federal and state statutory settlement procedures and the duty of both full and honest disclosure and the duty of good faith and fair dealings. **(see Paragraphs No. 29, No. 43, and No. 68 below)** Small mortgage lenders can subject their operations to bi-annual audits by outside certified Compliance Officers. (Also see No. 37, 40 and 42).

Some Common Sense Reforms:

a) Mortgage Broker Firms may be required to keep statistical records on the individual brokers with the highest percentage of defaults within six (6) months of the closing of the mortgage.
b) Compliance Officers (C.O.'s) should interview the borrowers in a "select percentage" of these defaults to determine if Unfair and Deceptive Mortgage Practices were the cause of the default, and then notify management.
c) Where a borrower may be given sufficient "cash" at the closing to "make up" income for upfront future mortgage payments, then separate statistical records should be maintained on individual brokers with defaults occurring within 12 months and within 24 months.
d) Borrowers in default are rarely if ever "interviewed" by an outside agency or C.O. to determine the reason for the default. Therefore, deceptive practices are rarely if ever "tracked" by government agencies back to the offending staff mortgage broker. This results in <u>repeat</u> offenses against future borrowers.

(16) **The National Bar Association's Dilemma:** The question to ask is, could this subprime meltdown that has so severely damaged U.S. markets, both nationally and internationally, been avoided if The American Bar Association, and/or the respective fifty (50) State Bar Associations had acted sooner, and issued mandated closing settlement "guidelines" to attorneys for these new subprime mortgage closings. Closing statutory procedural practices and mortgage law substantive practices and the "legal forms" used therein, are all the bulwark of an attorneys practice at law. The various Bar Associations in America today should not ignore their responsibility to take remedial steps within their own profession to address this new mortgage marketplace. New rules of conduct by an attorney at a mortgage or home closing are needed in view of the thousands of consumer complaints. Some of these homeowners could not afford even the first payments, others were given enough cash at the closing to make only the first few payments to "mask" the predatory nature of the loan and anticipated early foreclosure.

(17) **Written Authority for Future Modifications of Pooled Mortgages by the Mortgage Serving Agent is Needed.** Securitization of pooled mortgages has been around for conventional mortgage loans for decades, but only became prevalent for subprime mortgage in 1995. Federal and state governments must ask itself, how can the securitizations process be made fairer by future state legislation or state regulations, and by focusing more on a borrower's possible future need for modifications of their mortgages in times of financial hardships, or predatory lending. Warning: Some "Private Trusts" containing pooled mortgage-backed securities allegedly prohibit modification or forbearance agreements unless "in the best interest" of the investors. The "trustee bank" then determines what the mortgage "servicing agent" can or cannot do to modify a mortgage in default. Some of these trusts even limit mortgage modifications to 5% of the trust pool.

Comment: Arbitrary restrictions on a "servicing agents" limited authority to modify may not be in the public's best interest, and in the long term, may not be in the investor's best interest.

Some History: The federal government sponsored Fannie Mae, (Freddie Mac) has for decades, pooled and sold its own, mostly conventional mortgage securities, and some subprime mortgages, and ALT-A mortgages, yet a borrower/homeowner could in times of hardship, seek a Fannie Mae "modification agreement" directly from his mortgage servicing agent, without Fannie Mae direct participation. Let's return New York State to these reasonable and fair modifications procedures, known as "workout agreements" or "forbearance agreements" to prevent foreclosure. Fannie Mae, in writing, always gave its "mortgage loan servers" advance authority to modify and to act on Fannie Mae's behalf. This modification authority is spelled out in writing. Furthermore, HUD/FHA mortgages, and Veterans Administration mortgages (through Ginnie Mae) did the same on its guaranteed mortgages. It was a fair system that always worked well in the United States, and in New York State.

(18) **Appraisers and Conflicts of Interest:**

A federal bank or state bank's "selection" of an appraiser rarely (in the past) resulted in a biased appraisal. Most times it was very conservative. However, since mortgage brokers and real estate agents entered the mortgage field, the house appraisals, especially in cases of "house flipping" have in some cases been inflated, becoming the focal point in some federal and state fraud investigations. This is a possible area for increased state regulation.

(19). **Regulate Pooled Mortgage Backed Securities: (MBS)**

Pooled mortgage-backed securities (MBS) unlike stocks and other bonds are not regulated by the federal or state government. Wall Street firms buy and sell these pooled mortgage backed securities at private trading decks, not at public exchanges.

Asset-Backed Commercial Paper: These are short term asset backed securities are similar to a short term I.O.U. Today commercial paper is mostly held by money market mutual funds and backed by a combination of bonds, residential mortgages, car loans, credit card receivables, and or other loans.

(20). **Rating Firms and Conflicts of Interest:**

Rating firms are paid by Wall Street Investment Banks. Investment banks desire and need good ratings to encourage outside investors to purchase their bond offerings. One in four mortgages sold to these investors were subprime mortgages without numerous independent bond analyst or rating firms setting off alarms. The Wall Street Journal, on August 15, 2007 raised the question of the rating companies (S&P, Moody's, Investors Services, and Fitch Ratings) "collaborations behind the scenes, with the underwriters that were putting securities (mortgage loans) together". The **Exhibit "D"** Wall Street Journal article shows the fees paid to rating firms were very lucrative, and that some mortgage lenders and mortgage brokers should have been more cautious in both their lending "standards", and in not accepting almost every subprime mortgage application that walked in the door. This may not have occurred if the then "explosive" highly rated secondary market into which to "dump" these bad mortgages had not been so easily available. It was a wild ride that any prudent lender, ten (10) years ago would have avoided. The Wall Street Journal article further quotes State Attorney General Marc Dann of the State of Ohio as follows:

> The rating firms had so much to gain by issuing investment-grade ratings that they let their guard down. They had a "symbiotic relationship" with the banks and mortgage companies that create these products, says Mr. Dann, who's office is investigating practices in the mortgage markets and has been talking to rating firms.

(21). **Collaterized Debt Obligations (C.D.O): Once liquid, now illiquid:**

C.D.O.'s were aggressively sold to investors and were composed of a multiple of different rated bonds, some lower rated, some higher rated, which were combined in order to accomplish a better overall rating. CDO's were selected to offer a better fixed interest than corporate bonds with similar ratings. A complex CDO may contain mobile home loans, airplane leases, car loans, credit card receivables, and hospital mortgages. Investor's could not properly evaluate this mix of bonds because of its intentional complex nature. CDO's are not transparent. State and federal regulations should be considered in the future to make CDO's more transparent. Investment firms need to go beyond "Internal Risk Controls" by seeking information from outside consumer protection "agencies" that exclusively deal with mortgage defaults to calculate the market risk.

(22). **Mathematical Risk Models:**

" Statistical Risk Models" or computer driven Quantitative Trading Models and historical data were substituted for costly mortgage bond research, and are still used by some rating agencies (possibly Moody's, or Standard & Poors) but have apparently failed in the current market to identify the proper "assigned risk" of C.D.O's, or pooled mortgage-backed securities. We may again need more of the experienced human analyst's input. One need only have read of the constant consumer complaints and continuous bad news on that mortgage broker's industries unfair and deceptive practices to be put on notice (see paragraph 27 below) of these problems.

(23) **Mortgage Underwriting:**

The use of computer automated data in determining a subprime borrower's "ability to re- pay" appeared to be deficient in subprime loan underwriting. A major overhaul is probably in the works, but why it took so long is a question for future congressional hearings. We still need subprime lending in America, but <u>not</u> the unfair and deceptive mortgage broker tactics of the last six (6) years. **Many Legal Aid and Legal Services Office's have known of this possible mortgage broker subprime "potential meltdown" since early 2002, when only 4 1/2 % of all mortgages were subprime** based in part on the rise of multiple valid consumer complaints. In 2002, the National Consumer Law Center published its first Guide For Legal Advocates, entitled: "Stop Predatory Lending" to address this **blossoming** threat to home ownership in America. Wall Street, the investment firms and the big banks ignored these signals and the warning coming from Predatory Lending Conferences.

(24) **Mortgage Brokers "Yield Spread Premiums" (YSP) Disclosure:** These fees (2 1/2% of the mortgage) should be made more transparent by separately stating and identifying them on the Good Faith Estimate (GFE) upfront. The Yield Spread Premium is a fee paid by the lender to a mortgage broker when the mortgage broker arranges a mortgage loan with a lender. The interest rate on the loan is generally inflated to an amount higher than the "par rate" to cover the cost of this extra fee paid to the mortgage broker. The "par rate" is the best rate on any given day. Unfortunately, it can also create an incentive for some mortgage brokers to not always seek the most favorable terms for the borrower, but instead, the most favorable terms for the mortgage brokers. Early disclosure is in the best interest of all parties. The lenders have the "power" to demand this disclosure be made by the mortgage broker. In October, 2007 Washington Mutual Bank announced it would "call" each customer of the mortgage brokers before mortgage closing to disclose the YSP and other <u>terms</u> and rates of the <u>proposed</u> mortgage to the borrower. (Also see No. 49).

(25) **A New Third HOEPA RefinanceTrigger: Subprime ARM mortgages:** All Refinance Subprime Mortgages that include Adjustable Rate Mortgage (ARM) should automatically be included under the Home Ownership and Equity Protection Act of 1994, (HOEPA) 15 U.S.C. 1639. HOEPA is a special law that provides added consumer protections when a refinanced mortgage has high interest rates **combined** with high closing fees.

(26) **A New Fourth HOEPA Refinance Trigger:** Mortgage Flipping and the **Pre-payment Penalty.** The "prepayment penalty" in a refinance is one strong indicator of possible mortgage flipping. Any prepayment penalty in excess of the lesser of $3,000.00 or 1% of the loan, should trigger the need for the added consumer protection under the HOEPA statute. Furthermore, states can pass their own HOEPA statutes.

(27) **Early Notice to Wall Street:** Prior to this subprime mortgage meltdown, the perils of unregulated mortgage brokers predatory lending activity were disclosed in some detail by the Federal Trade Commissions (FTC) "Consent Settlements" with many of the nations largest lenders then using independent mortgage brokers. The Federal Trade Commission has a long "list" of these settlements, i.e., Associates First Capital, (Citigroup) Ameriquest Mortgage, etc. It is difficult in 2007 for analysis rating firms, and mortgage underwriters to not have anticipated the subprime mortgage market melt down unless they were ignoring all the consumer complaints so widely reported in the New York Times, The Boston Globe, etc., and in Legal Aid Society litigation It appears to be not a question of if it would occur, but only when it would occur. An ethical mortgage management officer and President of a mortgage brokers office in Huntingon, New York State, recently was quoted in the Long Island Press (August 9-15, 2007) with respect to the subprime mortgage market meltdown that the "get what you can" trend of mortgage brokers is to blame. He further stated "basically, if you have someone (mortgage broker) "sitting behind a desk trying to get a client, he doesn't care if the borrower can make the payment. He doesn't care about the person. He just wants to make the sale and this leads to a fallout". This statement comes from a senior mortgage broker in business for many years.

28) **State Licensing, Re-Educating and Retraining:**

Rehiring the thousands of mortgage brokers, now out of work is an important job now facing this industry. However, retraining these mortgage brokers into a 'new lending culture" of placing the best interests of their clients (homeowner, borrower) at the forefront of every new mortgage application process will require much work, training and supervision. The Federal Reserve Board and the State Banking Superintendents can encourage the lenders to demand of the mortgage brokers, to whom the lenders give lines of credit, to install the necessary safeguards to ensure that mortgage applicants receive fair and honest counseling and disclosure before the mortgage closing.

(29) **Compliance Officers are Office Inspector Generals:**

The hiring of qualified mortgage brokerage office Compliance Officers, is the 'key" to restoring the Global and National reputation of both the American Mortgage Brokerage Industry and other American Investment Banks. This Compliance Officer should have a minimum of ten (10) years experience representing and defending and/or negotiating homeowners as victims of foreclosure schemes. He or she should have a superior knowledge of both prime and subprime mortgage brokerage scams and unfair and deceptive mortgage Industry Practices and experience with the,

*HOEPA Act	15 USC 1639
*RESPA Act	12 USC 2601
*TILA Act	15 USC 1601
*FHA Act	42 USC 3601
*ECOA Act	15 USC 1691
*State UDAP Acts	

(30) **Unclean Hands: An Industry Wide Practice.**

The NCLC in its book "Stop Predatory Lending" concludes that: "predatory lending is rampant in the subprime market; recent lending without regard to a borrower's ability to repay is having serious repercussions.
The NCLC then explains on page 78 how this may be accomplished by the mortgage broker and/or the lender who comes to the closing with "unclean hands" as follows:

> Lenders will often try to argue that borrowers were complicit in any fraud in the loan application process, whether by providing a falsified income or an inflated appraisal. Lenders frequently base this argument on the various **certifications** borrowers sign at closing, and particularly at the signing of the loan application. The borrowers are often <u>never</u> given an opportunity to review the documents prepared by the lender and the broker. When borrowers do ask questions, they may be told, "this is how it is always done."

It is noted by Legal Aid in actual "case histories" that on the closing day the borrower is signing "certification" after certification" by being told "sign here or sign there". The closing agent is not signing any certification stating the borrower has had three (3) days to review the terms and/or all the documents or that fair disclosure has been timely made or that pre-closing third party counseling has been recommended by the lender and refused by the borrower. The question of who has "clean hands" and who has made misrepresentations and who has relied on these misrepresentations is obvious from the predatory nature of the consumer complaints being received across this state and nation.

The NCLC states (page 60) on HOEPA'S federal additional loan "disclosure notice" requirements:

> Although the (disclosure notice) <u>timing requirements</u> appear straightforward, it is common practice for predatory lenders to rush the consumer to complete a loan quickly, before the consumer understands the nature of the scam or can obtain advice from a lawyer, friend, or relative.

Lenders may be tempted to "fudge" the date on the "notice" because (timely) complying with this (disclosure notice) requirement gums up the bureaucratic operation (of the lender).

(31) **Standards vs. Standards: Whose standards?**

The "Federal" standards the industry is now allegedly "tightening" do not and will not address the existing mandated "statutory standards" discussed in paragraphs above. There are all types of "standards" that relate to mortgage closing and each professional group involved must not only look internally but also externally at the other 'links' in the mortgage chain, and demand from the "links" below them, fairness, and demand disclosure, and demand Truth–in-Lending, and demand pre-closing counseling.

(32) The Truth-in-Lending Federal Disclosure Statement (See also Paragraph No. 38)

This "Federal Disclosure Statement" (attached) should be delivered **into the hands** of the borrower three (3) days before any prime or subprime mortgage closing and it now provides complete easy to understand adjustable rate mortgage disclosure or balloon payment disclosure. Had this early disclosure been required, many homes now in foreclosure may have been saved from foreclosure

(33) The Defrauded One-Third:

Does the mortgage industry and Wall Street now accept the research reported by Americans for Fairness in Lending that "one third of those offered subprime mortgages are qualified for less costly prime mortgages". Furthermore, are the investors also put at foreclosure risk by this predatory practice of raising the interest rate for otherwise prime mortgage applicants and involuntarily subjecting them to abusive ARM 2/28 mortgages?.

(34) A Subprime "2/28 hybrid" Arm Mortgage given to a new Homeowner was a Formula for Disaster:

First time homeowners receiving subprime mortgages generally incur some early expensive major repairs and/or purchase a refrigerator or stove on the installment plan or automobile, and certainly some needed furniture expenditures. Even a "2/28" hybrid ARM mortgage for first time homebuyers was in many cases not fiscally wise, or common sense, as other debts were anticipated in the first few years.
An improved "5/25" ARM Mortgage (at the option of the "prime" borrower) may have been reasonable for a prime eligible mortgage borrower but subprime first time homeowner should always be given a fixed rate.

(35) **"Liar Loans" A/K/A "No Document" Loans:**

During 2005 and 2006 in the then heated subprime mortgage market, these subprime "no income documentation" mortgage loans quickly went from **problematic to predatory to fraudulent.** It is now obvious that is why some mortgage lenders referred to them as **Neutron Loans**. The "sky was falling", but many lenders and banks did not require of mortgage brokers due diligence in the application process.

(36) **The Hard Facts:**

- Moody's Economy.com, a research firm in West Chester, Pa., projects that lenders will acquire about 760,000 homes through foreclosure this year and 935,000 in 2008, up from an average of about 440,000 a year from 2000 through 2006.
- According to Inside Mortgage Finance, U.S. lenders originated about $600 billion of subprime home loans in 2006, or 20% of all home mortgages.
- According to the Durham, N.C. Center for Responsible Lending about 56% of those subprime loans were 2/28 mortgages, and some of these subprime ARM mortgage were interest only in the first 2 years.
- According to RealtyTrac Inc, (Irving, Calif) foreclosures are up 93% and on track to top two million homes for the year since 2006.

(37) **Therefore, Future Mortgages with Nontraditional Mortgage Terms Deserve Three Safety Valves:**

(a) Independent voluntary or involuntary credit counseling and,
(b) early disclosure of the TILA Federal Disclosure Statement, and,
(c) independent Compliance Officer reviews, and where necessary, future staff consumer rights training for all mortgage originators.

(38) **The Federal (TILA) Disclosure Statement Box:**

4. Truth in Lending Act (TILA) Statement Box **Enhancements:**

By federal and state law, **add to this Disclosure Box** the following information:

- the actual dollar amount of any prepayment penalty, to a **prior** mortgage holder or **current** mortgage and,
- a statement that the borrower may seek mortgage counseling and, budgeting, and
- **the names and telephone number of 3 local mortgage counseling agencies.**

(see below)

☒ INITIAL ☐ FINAL

FEDERAL TRUTH-IN-LENDING DISCLOSURE

(38)

Creditor

No.1

Borrower(s)

- 3 MORTGAGES (ARM)
- 3 COMPLAINTS.
- 2006 Subprime FORECLOSURE.

Loan No.
Processor
Date of Disclosure 01/25/2006
Est. Settlement Date (Date of Closing) 02/13/2006

Mailing
Address

ANNUAL PERCENTAGE RATE The cost of your credit as a yearly rate.	FINANCE CHARGE The dollar amount the credit will cost you.	AMOUNT FINANCED The amount of credit provided to you or on your behalf.	TOTAL OF PAYMENTS The amount you will have paid after you have made all payments as scheduled.
10.988 'e' %	$ 842,510.73 'e'	$ 321,797.82 'e'	$ 1,164,308.55 'e'

wow!

10.988 %

Your MONTHLY PAYMENT SCHEDULE will be:

# Payments	$ Payment	Beginning On	# Payments	$ Payment	Beginning On	# Payments	$ Payment	Beginning On
36	$2,488.86	4/1/2006						
6	$3,191.70	4/1/2009						
317	$3,319.36	10/1/2009						
1	$3,321.55	3/1/2036						

No.2

FEDERAL TRUTH-IN-LENDING DISCLOSURE STATEMENT
(THIS IS NEITHER A CONTRACT NOR A COMMITMENT TO LEND)
For use with Adjustable Rate Mortgage Loans

Lender:
Borrowers:

Property Location:

Date: April 10, 2006
Application #:

ANNUAL PERCENTAGE RATE The cost of your credit as a yearly rate.	FINANCE CHARGE The dollar amount the credit will cost you.	Amount Financed The amount of credit provided to you or on your behalf.	Total of Payments The amount you will have paid after you have made all payments as scheduled.
11.665 %	$ 754,956.15	$ 274,883.43	$ 1,029,839.58

wow!

Disclosures are estimates based on an anticipated funding date of 4/14/06

Your payment schedule will be: e means an estimate

No. of Payments	Amount of Payments	When Payments are Due
24	$ 2,252.29	Monthly, beginning June 1, 2006
6	$ 2,657.77	Monthly, beginning June 1, 2008
330	$ 2,908.60	Monthly, beginning December 1, 2008

TRUTH-IN-LENDING DISCLOSURE STATEMENT
(THIS IS NEITHER A CONTRACT NOR A COMMITMENT TO LEND)

LENDER OR LENDER'S AGENT:

No. 3

☒ Preliminary
DATE: 12/11/2006
LOAN NO.
Type of Loan: Conventional

BORROWERS:

ADDRESS:
PROPERTY:

ANNUAL PERCENTAGE RATE The cost of your credit as a yearly rate.	FINANCE CHARGE The dollar amount the credit will cost you.	Amount Financed The amount of credit provided to you or on your behalf.	Total of Payments The amount you will have paid after you have made all payments as scheduled.
10.650 %	$ 1,134,868.94	$ 384,519.41	$ 1,519,388.35

wow!

PAYMENT SCHEDULE:

NUMBER OF PAYMENTS	AMOUNT OF PAYMENTS	PAYMENTS ARE DUE BEGINNING	NUMBER OF PAYMENTS	AMOUNT OF PAYMENTS	PAYMENTS ARE DUE BEGINNING
24	$3,372.44	Monthly beginning 02/01/2007			
335	$3,504.19	Monthly beginning 02/01/2009			
1	$264,546.14	Monthly beginning 01/01/2037			

BALLOON PAYMENT AFTER 30 YEARS IS $264,546 14/100.

DEMAND FEATURE: ☒ This loan does not have a Demand Feature. ☐ This loan has a Demand Feature as follows:

VARIABLE RATE FEATURE:
☒ This Loan has a Variable Rate Feature. Variable Rate Disclosures have been provided to you earlier.

39) **Pooled Mortgage "Buy Back Agreements".**

As stated in Paragraph No. 17, above, the amount of delinquent mortgage loans that can be "modified" by mortgage "Servicing Agents" , is limited to 5% . These "Servicing Agents" seek to keep loans performing, but may "modify" some mortgage loans up to 5% of the pool to prevent them from becoming nonperforming loans. "Servicing Agents" collect fees for the performing loans only, not loans in default. However, mortgage originators may offer investors "buy back" agreements, in order to more easily sell these pooled mortgage securities to investors. These "buy back" agreements are not common and are not a secured guarantee as the funds needed to perform under the "buy back" agreement are not held in escrow, and are subject to the cash flow of the originators.

40) **Annual Audits or Reviews by Independent Compliance Officers (C.O's) May Be Introduced into the other "Links in the Mortgage Chain" for Investor Confidence.**

- Asset-Backed Commercial Paper (C.O. audits/reviews annually).
- Rating Firms (C.O. audits/reviews).
- Pooled mortgage backed securities (C.O. audits/reviews)
- Mortgage Underwriters (C.O. audits/reviews)

41) **Will State Registration and Regulatory Oversight of Mortgage Brokers by the States provide Adequate Consumer Protection?**

The short answer is "NO"!

42) **Some Common Sense Reforms:**

a) Mortgage Broker Firms may be required to keep statistical records on the individual brokers with the highest percentage of defaults within six (6) months of the closing of the mortgage.
b) Compliance Officers (C.O.'s) should interview the borrowers in a "select percentage" of these defaults to determine if Unfair and Deceptive Mortgage Practices were the cause of the default, and then notify management.

c) Where a borrower may be given sufficient "cash" at the closing to "make up" income for upfront future mortgage payments, then separate statistical records should be maintained on individual brokers with defaults occurring within 12 months and within 24 months.

d) Borrowers in default are rarely if ever "interviewed" by an outside agency or C.O. to determine the reason for the default. Therefore, deceptive practices are rarely if ever "tracked" by government agencies back to the offending staff mortgage broker. This results in repeat offenses against future borrowers.

43) **"Costs" of Compliance Officer (CO) Reviews and Audits:**

The costs are not great as these internal reviews can be completed expeditiously. These are not financial audits, but "fact finding" audits.

The federal laws and the Congressional hearings (see paragraph 29 above) of the 1960's, 1970's, 1980's, and 1990's have not effectively regulated these mortgage origination abuses, frauds, and deceptive practices, but Compliance Officer audits, and C.O reviews and C.O. in house training may be the best reform.

44) **Job Losses/Job Retention/Job Training:**

The Wall Street Journal reported mortgage firms have cut 70,000 jobs, and more jobs by October, 2007. Expect more mortgage firm and construction company job cuts to come. These former mortgage broker employees need more than just new management "guidelines" when they are rehired. They need to know there are "enforcement standards" that will be executed, and reviewed at their "office level" by independent Compliance Officers (C.O). Hiding behind the corporate veil should no longer be possible for these mortgage salesmen.

45) **The Psychology of Mortgage Commitments and Consumer Commitments:**

Today's mortgage broker is a very experienced salesman. Even **before** the terms and details of the lenders refinance loan commitment are disclosed to the consumer the mortgage broker will encourage the consumer to notify other pressing creditors of this new financing. The mortgage broker will even offer to accept confirmation telephone calls from a consumer's creditor. This assistance psychologically "locks in" the consumer and increases the consumers need to "close" even if the refinance mortgage terms drastically change, at the last minute, from very fair to predatory. In the purchase of a home the friendly seller of the home is sitting across the table at the closing, which causes the purchaser to feel obligated to close on the mortgage The more anxious the consumer to close the more onerous the unfavorable mortgage terms may become. It is not a case of "buyer beware", it is a known practice of marketing and deception by either an experienced broker salesman, or lender's closing agent.

46) Mortgage Application Fees:

If a mortgage commitment is not obtained from the mortgage broker, or the mortgage "closing" for a house purchase is not finalized, and closed for any reason for either the lenders fault or at the borrower's request , the 'borrowers application fee" should be refunded. In a mortgage refinance, after closing, borrowers should not be penalized for exercising their statutory Right to Cancel. Invariably it is the mortgage broker's lack of upfront early disclosure of closing costs, and/or mortgage terms, interest rates and/or fees that result in a borrower's cancellation. Consumers need to be informed upfront, that the "Right to Cancel" is an honorable option to prevent possible fraud and deception. A "Right to Cancel" is a written document provided at a mortgage refinance "closing" and this document should also instruct the consumers (in large print) as to where said consumer may seek counseling or legal advice. For example, a family attorney or the local **named** legal services office, or the State Attorney General's office, and or the Federal Trade Commission. This pre-printed notice should be inserted onto the "Right to Cancel" because the three (3) day time limit is very brief. Note: This "Right" only exists in refinance mortgages after the closing, not in a home purchase mortgage after it closes. A home purchase mortgage borrower's "cancellation" must come before the closing.

47) Advertising Mortgages: Television, Newspapers, Magazines, Radio, Direct Mailing, the Internet, Realty Offices, Banks and Financial Office Solicitation:

According to the New York Times article **Scrutiny for Mortgage Ads,** August 25, 2007, both the State Attorney Generals of Ohio and New York and the Federal Trade Commission have ongoing reviews of unfair and deceptive mortgage ads. Unfortunately, because of the many thousands of lenders and the millions of mortgage ads each year it is now impossible for federal and state "regulators" to adequately rein in this predatory ad activity. It is recommended that advertising ad reviews be a mandatory duty or obligation of the Compliance Officers (C.O.) annual or semi-annual audit.
Law Professor Patricia McCoy (University of Connecticut) stated in the above New York Times article:

> The advertising was a drumbeat to consumers, saying: "Don't worry, you can qualify for a loan. We will approve it. "It was "push marketing" to reach out to these people on the sidelines who have doubts about their ability to pay a mortgage and lure them in."

Even when consumers do find out about higher rates before closing on a house, by that time they are often "psychologically committed" to buying.

48) **The Expose of a Predatory Lender**: (see Exhibit "A")

New York Times financial reporter, Gretchen Morgenson, in her Investigative Report dated August 26,2007 describes in some detail the inner workings and the Unfair and Deceptive Practices of one of the top mortgage originator in the United States, Countrywide Financial Corporation . This Investigative Report exposes the improper sales tactics, the use of "fixed" software, the predatory commissions fees, the unfair sales incentives paid to unethical salesmen, and the early concealment from the consumer of mortgage interest rates and mortgage points and the excessive closing costs or unearned fees demanded at the mortgage closing, along with the questionable loan terms and other multiple deceptions. The facts in the Federal Trade Commission's settlement in the case of the predatory mortgage lender, Associates First Capital (now owned by Citigroup, Inc.), has some similarity to the predatory Countrywide Financial Corporation "facts". Countrywide's biggest stock investor may be Bank of America in the near future. Bank of America is known for its "higher standards" and "no closing cost" mortgages. Bank of America would, no doubt, clean house at Countrywide if it takes control. Unfortunately, Bank of America's serious participation is now just a rumor.
The former Chief Executive Officer of Citibank/ Citigroup, Inc. Charles Prince, to his credit, removed thousands of independent mortgage brokerage firms from the Associates First Capital approved brokers "lists" to hopefully bring Associates First Capital in line with Citigroup, Inc. ethical corporate business standards. However, these furlonged independent brokers, no doubt, then went to work for other lenders and their shoddy "work product" was pooled into MBS and sold to big banks and investment houses. Unfortunately, as the old adage implies 'what goes around, comes around", and these deceptive mortgages severely damaged our credit markets!.

49) **Incentives and Commissions fees for Mortgage Brokers:**

"Volume Based Compensation" fees and 'Yield Spread Premiums" fees paid for mortgage broker referrals should not be based on "predatory or ARM interest rate inflation schemes". Nor should demands for "pre payment penalties" result in extra commissions to a salesman or broker. Frequently the unjust interest rate "inflated" loans are targeted toward those not represented by private counsel.

Note: (see Exhibit "A") New York Times Reporter, **Gretchen Morgenson's** Investigative Reporting on Countrywide Mortgage **should be read by** every member of the U.S. Congress, both Senate and House, and the U.S. Credit market firms and banks.

50. **Structured Investment Vehicles (SIV) and Short Term Debt "Conduits"**.

Conduits: These are commercial bank and investment bank IOU's or paper entities that are asset-backed commercial paper debt portfolio's which contain short term and/or medium term debt obligation issued to investors. Some mature in 3 to 9 months some mature in 30 to 90 days some mature in a week or more, and others in days. SIV's may be the longer term instrument and along with the shorter term "Conduit" vehicles both operate "off the books" and or "off the balance sheet" of the parent bank. The purpose is to raise money in the commercial paper market for future investment in high yielding assets and pooled mortgage backed securities by bundling mortgages, credit card debt, business loans and auto loans. Conduits or SIV's are not easily transparent to the stockholders of the parent bank or transparent to the public. However, the new entity on the block was the so called "liquidity put" which gave purchasers of C.D.O's, the right to reverse the sale and return the C.D.O to the seller if no market existed. To the purchaser and the public, all of the above could not have been more complicated and less transparent.

51. **Many Brokers Encourage a Borrower's Irrational Exuberance.**

Too often many brokers encourage a borrower to take on excessive financial risk by stating that the Fair Market Value of the house can only appreciate during the early term of an Adjustable Rate Mortgage (RAM). This sales pitch was used to convince many borrowers that the home equity increase would far out-weight the debt risk. It was a sales tactic that would bring too many borrowers to the closing table without the benefit of honest or ethical financial counseling.

52. **The Mortgage Broker Industry's "Blind-Eye" Predatory Culture has created many In-House New Labels to Identify their Brokerage Firms Predatory Loans:**

*Toxic mortgage
* Junk Mortgage
*Teaser Rate Mortgages
*Exotic Mortgages
*Dicey Mortgages
*"Upside Down" Mortgages (borrower owes more than FMV of the house)
* Ninja Mortgages (No Income, No Job, No Assets=Ninja)
* Liar Loans
*Take my word for it mortgages
*Shark Loans
*Stated Income Mortgages
*Pulse Mortgages (some lenders encourage mortgage brokers to throw funds at anyone with a pulse)
*Neutron Loans (see above paragraph 35)

53. **"Payment Option Mortgages": The One Percent (1%) Mortgage.**

This particular radio ad and/or paper leaflets, and/ or teaser ads bring in low income borrowers. However, the one per cent (1%) interest rate is only applied to the first day of the mortgage loan. The interest rate on the second day might increase to 8.13% and then 8.77%, but with this unpaid higher interest applied to the mortgage principal. (Take my word for it mortgage.) Under this mortgage scheme, the borrower loses ground each month up to a trigger point where the ballooning principal then kicks in with a 8.77% interest or more rate on the now substantially inflated principal. In New York City, <u>The Foreclosure Prevention Project</u>, South Brooklyn Legal Services, reported an avalanche of these consumer complaints.

54. " **The Scratch and Dent" Mortgage Backed Bonds:**

The rating firms own designation of "scratch and dent", applies to mortgage loans that:

- Exceed loan-to-value thresholds and,
- do not include documentation of borrowers income and,
- are subject to close monitoring to determine if they fail to perform in the first few months after the loan is disbursed.

The rating firms (i.e. Fimalac SA's Fitch Ratings, etc) will continue to periodically scrutinize these bonds for actual performance from the day they are bundled and sold to investors as pooled mortgage backed securities.

55. **Near-Prime Mortgages:**

These are mortgages the originators "claim" are one step up from subprime, as these mortgages allegedly were based on a borrowers credit score above the subprime benchmark. For example, the borrower has a fair credit score, but the borrower did also provide verifiable documentation of assets and/or salary. Many of these mortgage loans may be near the borderline of ALT-A loans and should be subjected to periodic monitoring, and if necessary, future downgrading by rating firms. The rating firm may put this bond on a watch list as a "scratch and dent" mortgage backed bond.

56. **Acquisition Bridge Loans:**

These are not the old fashion bridge loan (pre-mortgage loan) needed to provide funds to a homeowner who is building his home where said loans will be converted upon house completion to a conventional mortgage. Acquisition Bridge Loans are actually Merger Loans. Today, Wall Street firms and commercial banks financed mergers and acquisitions then will "layoff" these Acquisition Bridge Loans as bonds or securities. Acquisition Bridge Loans are generally "off the books" as short term debt which the bank or the investment firm never intended to hold as an asset. These merger loans were intended merely to generate fees for the lender.

57. **"Table Funded" Mortgages:**

The name of the investor buyer of the proposed mortgage is confirmed in advance before the mortgage closing in a "table funded" mortgage loan. The borrower at the "closing table" simultaneously assigns the mortgage loan to the entity or person actually putting the funds on the table.

58. Exit Fees a/ka/ Prepayment Penalties Frequently "Close the Back Door" to Refinancing by a Homeowner.

"Exit fees" are prepayment penalties that mortgage brokers are aware may "close the back door" by making it too costly for a borrower to get out early from an abusive ARM mortgage. The fee may result in a 3 to 5 year interest penalty. However, most adjustable rate mortgages (2/28) adjust to a higher rate ultimately after 2 years, while the exit fee may not expire for 3 or more years. The variance above in "years" seems to favor the lender and the mortgage brokers commission. Many subprime borrowers don't understand either the "term" or gravity of a prepayment penalty and having to wait out the prepayment penalty' s 36 months may not always be an option for the homeowner. One recent homeowner complaint received by Legal Aid, identified a $17,000.00 prepayment penalties that was paid by the homeowners when refinancing his home. New York State limits the prepayment penalty to the first year of the loan which is a better approach.

59. **Moral Hazard: The "Bad Behavior" Bailout:**

Moral Hazard is a market economic term used to describe an expost financial bailout, or expost financial assistance or other expost guarantees that rewards risky behavior. It is a term used to criticize the "hazardous downside" of either the U.S. Federal Reserve or Foreign Central Banking Systems in releasing liquidity or cash into a credit market's financial system to help stabilize credit markets for that market's past bad behavior.

60. **Financial Armageddon: Monitoring the Risk:**

The diffusion of mortgage risk among many thousands of investors worldwide, makes it difficult to know who bears the risk, and what the risk is. This was most pronounced with the advent of risk hedging derivatives, commercial paper, bonds and securitization or pooling of securities, and debt paper. Today, with the worldwide markets seeking investments in the United States, this current 2007 embarrassing meltdown of U.S. mortgages has delivered a "black eye" to our U.S. financial risk monitoring system and government. It is embarrassing when foreign governments demand to be invited to the U.S. to monitor our U.S. financial "offerings" on an equal basis with our U.S. regulators and our self regulators, our stock exchanges, our rating firms, and our bank and security firms Compliance Officers.

61. **"Sliced and Diced" into a pooled Mortgage Backed Bond Portfolio:**

To obtain a rating firm's top AAA rating, the packaging firm for the pooled mortgage backed bond could combine with investment grade mortgages, those speculative grade mortgages up from the nether region of junk mortgages. These combined mortgages were in effect "sliced and diced" to mix the good with the bad.

62. "Liquidity Back Stop Agreements" in Commercial Paper.

Banks issuing Conduits and Structured Investment Vehicles (SIV's) may agree to provide limited assurances (resembling guarantees) that these IOU security vehicles will be repaid at due date even if the Conduit or SIV cannot be rolled over or sold in the credit market. The "Liquidity Back Stop Agreement" may be a guarantee limited, in whole or in part, by one bank or a consortium of three to five banks. It may vary within the commercial paper or within a Conduit. Conduits are more protected than possibly the SIV's, and, as stated above, Conduits and SIV's are different, yet similar.

63. **The "Risk Distribution" in Various Collateralized Debt Obligations.** (CDO's)

Collateralized Debt Obligation (CDO's) are a form of asset-backed bundled security in which risk is distributed so investors can decide how much risk the investor wants to buy into. It is not for the inexperienced investor, as "Risk Distribution" is not clear, or foolproof.

64. **2007 Will Always be the Year of the <u>first</u> American Banking Upheaval of the 21st Century.**

George Washington Plunkitt, a political leader in the scandal plagued Tammany Hall (1850 to 1930) stated:

> There is a difference between honest graft and dishonest graft.

The laws in the United States today, still draw a distinction between criminal mortgage fraud and civil mortgage fraud. Consumer Civil Fraud is codified, to a degree in state statutes known as The Unfair and Deceptive Practices Acts (UDPA). Unfortunately most Mortgage Broker UDPA violations will not cease without independent "internal controls" within the mortgage broker offices. New government rules, new regulations and new statutes will not suffice without internal quality management controls, backed by independent quality audits. The modern mortgage broker is paid by commission which is an inherent incentive "to produce and to close" on the mortgage. Internal controls may be verified by an experienced Compliance Officer that has access to consumer complaints files, and foreclosure and mortgage default files.

65. **In 2007, there was a Mortgage Market "Tailspin" that "Humans" not Computers Could Easily Have Predicted as Early as 2005.**

Alan Greenspan, now a private citizen now admits that in late 2005, Mr. Greenspan knew the 2/28 subprime adjustable rate mortgages (ARMS) were vulnerable to causing credit and mortgage markets gyrations. Earlier UDPA "warnings" were coming from The Center for Responsible Lending (CRL), The Consumer Federations of America (CFA), The National Consumer Law Center (NCLC), The Association of Community Organizations for Reform Now (ACORN), Non-profit Counseling Agencies, and many Law Services groups nationwide. However, no alarms were coming from the private money sectors, the investment banks, the analysis, the rating firms nor the Federal Reserve System in 2005, 2006, or early 2007.

66. There are ARM Mortgages, and then there are ARM Mortgages.

Most ARM mortgages will "adjust" using a mathematical formula based on a particular Index. The most common Index being the 1-year U.S. Treasury Bill, plus a margin. Currently, rates on most ARM's are set 2 or 3 percentage points above the Treasury Bill. There are a variety of ARMS as follows:
The abusive subprime lenders in 2004, 2005, and 2006 most frequently used the 2/28 ARM with a "pre-payment penalty" clause. This ARM had the highest foreclosure, and default rate. However, other ARMS may be a one year, no closing cost introductory ARM, or Option ARM, where the homeowner choose the amount of interest they want to pay, tacking the unpaid amount into the principal, a/k/a negative amortization. Furthermore, there is a 3/27 ARM, a 5/25 ARM, a 7/23 ARM, or a 10/20 ARM, etc. Lenders, in describing these 30 year mortgages, also use the labels 3/1, 5/1, 7/1 or 10/1 (to describe the foregoing) to indicate an ARM rate adjustment each year after the initial low mortgage terms. All adjustable rate mortgages have a lifetime rate "ceiling", or cap. Still other ARMS may have a periodic rate ceiling, or cap which periodically limits the rate increase for each yearly rate adjustment. The lender's combination of 30 year or 40 ARMS can be both unlimited, and creative. A "sample" of various recent Adjustable Rate Arms from a reputable New York State private sector Credit Union (dated September 24, 2007) is printed below:

66. There are ARM Mortgages, and then there are ARM Mortgages.

terms

- 30-year jumbo mortgage
- 30-year jumbo mortgage
- 40-year fixed mortgage
- 40-year mortgage
- 5/1 ARM
- 5/1 interest-only ARM
- 5/1 interest-only jumbo refinance ARM
- 5/1 interest-only refinance ARM
- 5/1 jumbo ARM
- 5/1 jumbo interest-only ARM
- 5/1 jumbo mortgage
- 50-year mortgage
- 6 month LIBOR rate
- 7/1 ARM
- 7/1 ARM (interest only)

Adjustable Rate Mortgages

INTRODUCTORY ARM (30 YR TERM) (2) to $1,700,000			5/1 TREASURY INDEXED ARM (30 YR TERM) (4) to $1,700,000		
30 YEAR	RATE	APR	30 YEAR	RATE	APR
0 Points	5.500%	6.616%	0 Points	5.875%	6.416%
1 Point	5.125%	6.679%	1 Point	5.500%	6.363%
2 Points	4.875%	6.754%	2 Points	5.250%	6.360%
3/3 ARM to $1,700,000 (30 YR TERM) (3)			7/1 TREASURY INDEXED ARM (30 YR TERM) (4) to $1,700,000		
30 YEAR	RATE	APR	30 YEAR	RATE	APR
0 Points	6.250%	6.516%	0 Points	6.250%	6.516%
1 Point	5.875%	6.516%	1 Point	5.875%	6.419%
2 Points	5.625%	6.549%	2 Points	5.625%	6.386%
3/1 TREASURY INDEXED ARM (30 YR TERM) (4) to $1,700,000			10/1 TREASURY INDEXED ARM (30 YR TERM) (4) to $1,700,000		
30 YEAR	RATE	APR	30 YEAR	RATE	APR
0 Points	5.750%	6.492%	0 Points	6.625%	6.707%
1 Point	5.375%	6.492%	1 Point	6.250%	6.554%
2 Points	5.125%	6.524%	2 Points	6.000%	6.485%

ADJUSTMENTS	RATE
ARM loan amount greater than $800,000	0.125%
ARM loans with 90.01-95% LTV or CLTV	0.125%
2nd Home fixed	0.125%
FICO score fixed rate < 680 (jumbo < 700)	0.125%
Fixed loan amount > $800,000	0.125%
Plus Fixed loan amount > $1,000,000	0.125%

All applicable Adjustments are cumulative 1-800-628-7070 www.bethpagefcu.com

67. The Time for Credit Market Excesses Has Past:

The November 2007 new mortgage default predictions are worse. Mark Zandi, Chief Economist of Moodeys Economy.Com (West Chester, PA.) expects **defaults on about three million mortgage loans in 2007 and in 2008 combined, and Mr. Zandi predicts that two million of these defaults will force homeowners from their homes.** The mea culpa's, the excuses, the comments, apology's, rationalizations, and explanations from the Mortgage Industry, the U. S. Treasury, the Congress, the Federal Reserve Systems, (both former and current senior personnel) for the implosion of the U.S. credit markets, is not helpful to the foreclosed homeowner. The simple solution is to first require "oversight audits" on the subprime but non-bank mortgage market issuers, brokers and dealers. Many of these non-bank mortgage issuers, brokers and dealers had no professional interest in prudent lending but only in the fees that they immediately earned. These closing broker in-house "fee incentives" cannot always be regulated or prohibited in the future, but must be put on a "watch list" to prevent continuing myopic behavior. The mortgage broker will always be rewarded for how many loans he or she originates. These mortgage broker fee compensation structures however, can be self-regulated by mortgage brokers management "in-house" behavior reviews. In-house behavior however, requires continuous in-house "sales closing behavior audits" and training by outside non-government Compliance Officers (CO"S) similar to accounting audits, but less expensive and less time consuming.

68. **Compliance Officer (CO) Reviews Need Not Always be Annual if a Waiver is Granted.**

As previously stated not all subprime loans are predatory, and subprime loans are beneficial to many Americans seeking homeownership. Ethical mortgage brokers are numerous, as are many large lending institutions and federal and state banks. An initial Compliance Officer (CO) review may result in a long term waiver (3 years, or 5 years) between CO reviews. However, for the initial review the mortgage default and mortgage foreclosure files need to be reviewed along with all loan documentation. Furthermore, the ethical training program of mortgage brokers requires certification by a CO at the time of the CO audit.

69. **Bank Traditional "Risk Transfer Products" Did Not Work: Risk Controlled Safeguards Were Ignored:**

Lending banks in the past controlled "Risk" by fair and accurate underwriting and making its own loans from "in house capital or deposit funds" then transferring, not holding risk, to informed buyers or informed investors or to Fannie Mae, Freddie Mac and Ginnie Mae for cash or credit. However, today the investment arms of banks have defeated these prudent and conservative "Risk Transfer Strategies" by investing in Hedge Funds with sub-prime mortgage exposure and in holding bonds in the securitized markets such as Mortgage Backed Securities (MBS) and in aggressively purchasing variable interest entities and/or other special purpose entities (SIV's and CDO's, etc.) that brought risk back to the parent bank. Now the bank is holding most of the risk for these losses. The original idea of lowering the risk of high default rates by diversifying loans from different sources was defeated by seeking out high interest sub-prime loans for their high cash flow. Lenders and banks in response to demand for mortgages encouraged the creation of a whole new class of independent (off company premises) mortgage brokers in order to substantially decrease office employees and new hires and still expand business. It was both foreseeable and inevitable that the new credit industry structured debt market would, lacking verification of lending standards, eventually go to junk.

70. **The Rating Agencies: Was the Investor and Wall Street in the Dark:**

Rating Agencies in the past rarely shared all the information it relied on to the investment market as a whole and/or to prospective purchasers in particular. Some "day light" or sunlight requirements are needed if the average buyer or investor is to put his money into a "financial product" that even the professional seller has had great difficulty or lack of data for making adequate disclosure or clear informed disclosure. These convoluted risky or complex pooled securities and bonds that may be composed of corporate debt, loans to hospitals, automobile loans, and prime and sub-prime pooled mortgages, are a "crazy quilt" that rating agencies in the past should have devised a better system of full disclosure. The Rating Agencies need periodic audits by an outside Compliance Officer (CO) and/or reviews to determine if their system of disclosure is adequate, fair and timely. The State Attorney General Offices in the United States today have devised a system of full disclosure in condominium "sales" that is universally recognized as both fair and adequate. Taking a "page" from the State Attorney General's condominium "book" would be a good start for the securitized bond market.

71. **Mortgage "Loan Server" Companies, a formerly most profitable business, are not properly Monitored by State or Federal Regulators or Audited by outside Compliance Officers (CO).**

A Loan Server generally receives a fee of 0.25 percent on a prime mortgage and 0.50 percent on a subprime mortgage. However, subprime loans are big cash providers to

Loan Servers, as Loan Servers keep all the late fees, and other exaggerated default fees. In 2006, Countrywide Mortgage collected 285 million dollars in "late fees" alone. In addition, Loan Servers can also collect other very high additional junk fees, especially if a subprime borrower seeks bankruptcy protection. Loan Servicing can be a cash cow without serious risk in a good market. It can make money either way if the loan goes good or bad. However, in a very bad market Loan Servers should substantially increase its number of employees to adjust or modify mortgages. Our 2007 mortgage crisis has proved the reluctance of Loan Servers nationwide to quickly hire these needed extra staff, and home retention specialist, further adding to the nations credit market downturn. A 2007 Report on mortgage foreclosures by Law Professor Katherine Porter, found lucrative, but questionable loan servicing fees and improper accounting frauds and improper profiting by Loan Servicers appearing in foreclosures. Some of these junk fees are labeled "pay-off" fees and "monthly" inspection fees. Furthermore large Loan Servicers would charge a borrower in bankruptcy many times the actual Loan Servers reasonable cost. While other Loan Servers have failed to give the borrower, in loan default, credit for mortgage payments received by either miscalculations and/or concealment of itemized payment records. Outside investors in pooled mortgage backed securities, will not benefit from , or receive any of this excess income as an "offset" to their pooled losses, and the settlement costs to loan servers in a bad market, like 2007, may indirectly be passed on to investors. But an inherent "conflict of interest" may also exist, if a loan server in a modification agreement with a borrower, refuses to move a prime borrower out of a subprime loan. Admitting that a prime borrower was incorrectly labeled "subprime" may reduce the servicing fee from 0.50% to 0.25%. In some instances, contractually, Loan Servers may be dismissed by mortgage owners, if the Loan Servers too oftem acts in the borrowers best interest.

72. **The Mortgage Electronic Registration System (MERS)**

The MERS home loan registration system is frequently a named plaintiff in thousands of court foreclosure actions in the United States today. This system is jointly owned by FANNIE MAE and Countrywide Mortgage and other large lenders. It oversees more than 20 million mortgages in the U. S. The MERS system has been accused in civil court of charging exaggerated fees and enhanced charges in foreclosure actions. A recent class action lawsuit accused the MERS Systems of retaining foreclosure attorneys for a "fix legal fee" and then demanding from the borrowers three to four times for that same legal services disbursement. The outside investors in pooled mortgage backed securities did not benefit from or receive these excessive fees as an "offset" to their pooled losses.

73.. **The proposed federal law The Mortgage Reform and Anti-Predatory Lending Act of 2007 although a good start, will not, by itself, rein in the abuses of independent mortgage brokers affiliated with lenders of record.**

In the year 2000, predatory mortgage lending once again became a major issue in civil legal defense offices across the United States. In years before 2000, Legal Aid saw a rise in independent mortgage broker subprime loans becoming more fashionable among banks, among investment entities, and in Wall Street.
For instance, in 1997, independent mortgage brokers passed the half way "mark" in U.S. mortgage processing. Volume Based Compensation (VBC) or Yield Spread Premiums (YSP) from lenders was encouraging more independent mortgage brokers to bring in "inflated" interest rates on First mortgages from 10.5% to 15%, and up. Many second mortgages were 15% to 24%. The Federal Reserve Board labeled a mortgage a "high cost" loan based on the "rate spread" or APR interest rate on the loan over the

Treasury rate as follows: a high cost label or subprime label occurs when the spread is 3% above the Treasury rate for a first mortgage and 4% above for a second mortgage. The Legal Aid experience is that even "padded" interest rates, and "padded" closing costs today, had become the norm among too many mortgage brokers. By 2007, the mortgage market was approximately $8.5 **trillion Dollars, of which, the subprime portion is 1.2 trillion. It is interesting to note the U.S. Treasury debt is also 9 trillion dollars.**

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Legal Aid Society Question: **Why the pessimism by this writer?** During the past 30 years of federal and state legislation, and mandatory disclosure reforms and regulatory corrections, that this writer has witnessed, all said legislation when seeking to correct the lack of disclosure to the potential homeowner/mortgagor, these federal and state laws have been by-passed or ignored by too large a percentage of the independent mortgage broker industry. In other words mere licensing and mere legislation or mere regulations cannot rein in even civil unfair and deceptive practices by the independent mortgage broker firms that choose otherwise. Today (2007) the credit markets and **Wall Street**, and the investment houses, and the big banks have the clout to act now to rein in this abuse, and save this profitable Wall Street credit market. A private industry **"Task Force"** should be formed in Wall Street to "preserve" what is still Wall Street's most profitable market the national homeowners mortgage Market of 8.5 trillion dollars, both prime and subprime.

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Independent mortgage brokers good and bad, are here to stay, **but they can continue to by-pass or ignore rules and regulations.** What mortgage brokers cannot ignore is the inherent power of the money market managers, the big banks, and the investment houses, if said credit markets demanded and implemented accountability and oversight before "packaging' or selling debt. Fraud Risk Management had always been a bi-word of large corporate business concerns. Protection of their own mortgage credit markets should be placed at the top of their investment industries "agenda" in 2007. Therefore, Legal Aid offers this recommendation below:

74. **Due Diligence by Wall Street: A private non-governmental credit market industry-wide "Task Force" composed of some of the best Wall Street Risk Managers, should be impaneled to lobby the lenders to voluntarily rewrite the disclosure procedures and the process used to approve mortgages.**

The current bills before Congress will not stop fraud and deceptive practices. We will always see those cases. Mortgage brokers were aware of the complete lack of civil penalties when they ignored the disclosure requirement in the past. It is was not, in most civil frauds cases, a crime to lie to a borrower. Unfair and deceptive practices are generally civil in nature, not criminal. However, Mortgage Brokers were not the only cause of the 2007 mortgage collapse. There were other obvious signs of trouble on the horizon, going back to the year 2000, and earlier such as:

*Real Estate Broker's offices expansion into a profitable mortgage market for possible lucrative referrals to mortgage brokers for additional commissions (1% or more). An additional needless cost to the borrower and investors on top of the mortgage brokers commissions (points), and the lenders discount fee. These business arrangements may not necessarily be illegal, but are unethical in too many instances if proper disclosure is not given. Furthermore, some real estate companies have their own affiliates or "in house" mortgage broker subsidiaries, (i.e. Century 21 Real Estate and Coldwell Bank Real Estate). This is almost a legal double dipping arrangement.

*Mortgage brokers seeking unconscionable additional broker fees from lenders on top of origination, or points, or commissions such as an add on of a Yield Spread Premium (YSP) This was an additional needless increase in cost to the borrower and investors.

*Mortgage brokers seeking to "profit" from "Exaggerated Closing Costs" allegedly paid by the borrower, but actually paid by the investor in the long run. These Mortgage Brokers sought to add to the mortgage mix, a "higher-than-prime-loan for services fee" not performed. Furthermore, adding prepayment penalties to hinder the ability of borrowers to timely refinance and escape out of an unfair adjustable rate mortgage (ARM). An additional needless increase in cost to the borrower and investors.

*Some small mortgage brokers were retaining friends and relatives and partners as "closing agents" with high legal fees and high legal documents preparation costs but with the prices being set solely by the mortgage broker. An additional needless increase in costs to the borrower, and the investors.

*Large mortgage brokers were augmenting their income with lucrative separate and distinct in-house **ancillary firms** that would charge (higher than market) non-negotiated fees and charges.

*Title Search fees
*Title Examination fee
*Loan Servicing fees
*Notary fee ($350.00)
*Courier fee
*Appraisals fees
*Tax Certification fees
*Flood Certificate
*Fire Insurance premiums
* Flood Insurance premiums
*Title Insurance premiums
*Legal fees
*Mortgage Insurance charge
*Mortgage Insurance charge
*Tax Search fee
*Broker Processing fee
*Tax Services fees
*Lien release fees
*Pay off service fees
*Document preparation fees
*Fax fees messenger fees
*Attorney fee
*Application fees
*appraisal fee
*Origination fees, etc

(For additional fees, see attached Exhibit)

* Of course, none of the above additional charges were negotiated in an arm's length transaction with the borrower, or at cost but could be inflated 2x's and 3x's and/or 5x's and 10x's a reasonable and fair cost reimbursement rate. When assessing fees, the "sky was the limit". These were additional needless costs to the borrower, and future investors. **All the above fees were added to the mortgage "principle" that the ultimate Wall Street investor indirectly would pay a higher than anticipated price for, because high mortgage "principle debt" and low values of the home results in a negative recover if the house is foreclosed.** In the past, closing costs used to be paid for by the borrower, upfront with a down payment now the closing costs are added to the mortgage principle. That was an invitation to mortgage brokers to charge excessive fees, and to set up a cottage industry of ancillary firms.

75. **Did "Risk Taking" alone bring down the credit markets in 2007. A better analysis would be, ignorance by the credit markets on how the new mortgage system worked.**

Former U.S. Senator William Proxmire who wrote the Real Estate Settlement Procedures Act (RESPA) in 1974 , with input from the nations Legal Aid Society offices, and the author herein, **sought to prohibit ancillary business, or insiders controlled business arrangements** as a conflict of interest, and conflict of business ethics, and furthermore, this RESPA Act compelled real full and fair disclosure to borrowers. It also prohibited fee splitting, unearned fees and kickbacks. However, the mortgage broker industry and the **Real Estate Associations** have since lobbied the Congress and the U.S. Housing and Urban Development Department (HUD) to relax rules on ancillary business and to prevent reasonable HUD Regulatory controls on closing costs. Furthermore, the sharp increase in mortgage broker firms was in proportion to the decease in RESPA disclosure to borrowers.

A private "Task Force" of banking industry and **Wall Street** professionals who were also mislead, or victimized, (along with their clients and investors) could enforce the RESPA standards requiring disclosure and lobby for "fixed price" closing costs. The RESPA requirements of 1974 were relaxed in the 1990's, but a better word is ignored by the new group of many thousands of mortgage brokers that entered the finance field. RESPA worked well during its first 20 years (1974-1994) because the big banks enforced its statutory Standard of Disclosure. Today, a proposed "Task Force" should also look at why the warnings (lectures and symposiums) by the federally funded National Consumer Law Center (NCLC), were ignored by Wall Street. In 2002, the NCLC published a separate 300 page book entitled "Stop Predatory Lending" to warn the public and the country. The general opinion is few if any Wall Street or big bank executives or risk managers subscribed to this 2002 manual.
The RESPA law enacted in 1974 and placed in the federal Truth-in-Lending Act (TILA) 12 U.S. Code 2601, state in part:

§ 2601. (a) The Congress finds that significant reforms in the real estate settlement process are needed to insure that consumers throughout the Nation are provided with greater and more timely information on the nature and costs of the settlement process and are protected from unnecessarily high settlement charges caused by certain abusive practices that have developed in some areas of the country. The Congress also finds that it has been over two years since the Secretary of Housing and Urban Development and the Administrator of Veterans' Affairs submitted their joint report to the Congress on "Mortgage Settlement Costs" and that the time has come for the recommendations for Federal legislative action made in that report to be implemented.
(b) It is the purpose of this chapter to effect certain changes in the settlement process for residential real estate that will result-

(1) in more effective advance disclosure to home buyers and sellers of settlement costs;
(2) in the elimination of kickbacks or referral fees that tend to increase unnecessarily the costs of certain settlement services.

76. **The new 2007 <u>Bank Stabilization Fund</u> will not, by itself, provide a safe platform on which to build new and improved structured investment vehicle entity that the mortgage and real estate markets needs <u>now</u> to provide liquidity to the credit markets and to pooled mortgage backed securities (MBS) The nation and the credit markets still need prime and sub-prime mortgages with the ability to repay.**

    a. We do not need a new "business model" to replace MBS. A proposed Wall Street "Task Force' need first look only at the mortgage "origination", or underwriting process <u>before</u> the Wall Street pooled bond sale process and why the mortgage origination both failed the American homeowner, and failed the credit markets. The reasons given above in this discussion paper, may answer some questions and also provide direction on how to save this MBS credit market for future generations of home borrowers.
    b. The question of Hedge Funds investment in a MBS for the sole purpose of seeking higher income, higher returns, and/or higher yields, was not all wrong. Where Hedge Funds went wrong, was leveraging these MBS, and by pledging these securities to buy more debt thus multiplying the risk many fold. That's merely a Risk Management issue that doesn't require much study.

77. **Collateral Damage Resulting from Foreclosures: Tenants**

Many, many thousands of family's who "rent" ARM homes from owners and, while said renters are up to date in their rent, they will be evicted in a lenders foreclosure action against the landlord-owner. Even school districts will be effected as a large mass of "relocations" take place across the United States due to loss of homes, and jobs related to the mortgage industry.

78. **Collateral Damage Resulting from Foreclosures: The Homebuilders Industry.**

Many of our largest home builders have been forced to sell land or cease construction with the loss of many thousands of construction jobs. All of the big public home builders have been hit hard by the credit market turmoil. Some of the biggest names experiencing market set backs and slowdowns are Levitt & Sons., D.R. Horton, Lennar Corp., Standard Pacific Corp., Hovnanian Enterprises, Toll Brothers, WCI, KB Homes, Tousa, etc. Did all of our national <u>Corporate Boards of Directors</u> totally lack an understanding of the term "predatory lending", and the insiders "joking mortgage titles" created or adopted again with greater frequency in the early years, from 2000 on, (see paragraph No. 52). These mortgage titles, or labels or terms were as well known in the mortgage industry as was the term, "Liars Poker", known to the Bond business. The difference was that the mortgage terms and mortgage broker behavior were more egregious, and in clear violation of the RESPA Act of 1974..

78(b) Collateral Damage to City, and State Budgets:

A 2005 study by the Homeownership Preservation Foundation (Minneapolis), identified twenty-six (26) monetary costs incurred by local city government agencies and city taxpayers resulting from neighborhood foreclosures.

These costs have to be absorbed either by local city taxpayers or by the cities cutting city services for its taxpayers in general. Additional state costs are reported each day as our national foreclosures increase.

78(c) A Mortgage "Due Diligence Company or Private Firm " performs the last "audit"/review of the now complete mortgage file prior packaging the various mortgages in a bond or security and prior to obtaining a credit rating by the rating firms.

A "conflict of interest" may exist because the due diligence company is paid by the lender $350.00 per mortgage file reviewed and the due diligence company is then responsible for identifying the weaker subprime loans known as "Exception Loans". These "Exception Loans" were the most hazardous of the subprime loans and would have to be sold or packaged at a substantial "discount" by the lender. However, due diligence audits were only performed on a limited percentage of these and other mortgages before packaging which doesn't appear to be a vigorous or complete audit system.

79 (d) The borrowers financial statement stating the borrowers income, assets, and resources should contain a separate "signed disclaimer" by the mortgage broker that the mortgage broker has not instructed or coached the borrower to misrepresent the borrowers income, assets or resources.

Regulation Z should require that a copy of the final written borrower's financial statement and the written "mortgage broker's disclaimer" be given to the borrower at least 3 days before the closing. The National Consumer Law Center (NCLC) in its book Stop- Predatory Lending page 78 stated with respect to falsified loan applications:

> Lenders will often try to argue that borrowers were complicit in any fraud In the loan application process, whether by providing a falsified income or an inflated appraisal. Lenders frequently base this argument on the various certifications borrowers sign at closing, and particularly at the signing of the loan application. The best response ids grounded in educating the judge about how loans are made and the relative sophistication or lack thereof of the parties. **The borrowers are often never given an opportunity to review the documents prepared by the lender and the broker. When borrowers do ask questions, they may be told, "This is how it is always done".**

Please note: A second foreclosure case, October, 27, 2007 at The Legal Aid Society of Suffolk County where different mortgage brokers raised different clients income from approximately under $3,000.00 per month to $9,000.00 per month, both clients were retired senior citizens on Social Security. The mortgage brokers closing agent also exclaimed "this is how it's always done". It almost appears to be an "industrywide" practice in subprime loans.

78(e) Super SIV- the US Treasury Departments has indorsed Master Liquidity Enhancement Conduits as a short term fix.

Wall Street created the Collateral Debt Obligations (CDO) and the Collateral Mortgage Obligations (CMO) and Structured Investment Vehicles (SIV) and the Mortgage Backed Securities (MBS) all of which are in trouble.

The US Treasury Department is seeking to solicit Wall Street Banks and Investment Firms to back up these troubled deteriorating debt obligations with this emergency backup Super SIV. The private management fees for Super SIV's will be paid by the banks and Wall Street at a proposed rate of 0.1% up to 0.2%. This Super SIV will first separate out and exclude the riskier SIV's and Subprime or ALT-A mortgages. Only the good SIV's will be given Super SIV status and then a discount incentive of up to 8% will be offered the investors of Super SIV's.

Note: Legal Aid Society reforms are annexed hereto for discussion purposes.

79. **How Long can Freddie Mac Continue to "Support" the Mortgage Market Liquidity While Possibly Suffering Billons of Dollars in Future Default Loses of it's Own.**

For all purposes the current prime "purchaser" and/or the prime "insurer" of Mortgages in the U.S. is the federally chartered Fannie Mae, and Freddie Mac and, in addition, the US governments insurers of mortgages the Federal Housing Administration (FHA) and the US Veterans Administration. The non-profit federally chartered twelve (12) **Regional Federal Home Loan Banks,** although not government owned, they are also substantial sources of cash "advances" to lenders which are secured by mortgage loans. Fannie Mae and Freddie Mac together hold 4.8 trillion US mortgages or half of the nation's mortgages prime and subprime, yet Joshua Rosner, Research Analysis at Graham Fisher & Co. stated: "we are seeing unprecedented foreclosures and declines in house prices not seen since the Great Depression". Today we are seeing that the independent mortgage broker's unfair and deceptive practices, not only "targeted" the consumer but also "targeted" Fannie Mae and Freddie Mac. It is predicted that by May of 2008, the U.S may see 42 billion dollars in ARM mortgages "reset" to higher interest rates. Goldman Sachs recently took a pessimistic view predicting 400 billion in MBS losses with other mortgage losses, and/or foreclosure expenses along with a drop in home Fair Market Values (FMV) (possibly 15%) over the next 3 years. Home values are now down 5%. The European Organization For Economic Cooperation and Development predict 300 billion in U.S. mortgage "write offs". Some news and media organizations using various studies, predict that at least 150,000 ARM mortgages will "reset" each month. The most certain prediction is that defaults, delinquencies, resets, losses and 'possible" recession will become the "economic topic" of this decade. Some key congressional dates to remember are:

- 1932- Federal Home Loan Bank Board created by Congress as a non-profit.
- 1934 – U.S. Federal Housing Administration Created.
- 1934 – U.S. Federal Deposit Insurance Corporation.
- 1938 - Fannie Mae chartered.
- 1974 - Real Estate Settlement Procedures Act (RESPA) enacted by Congress with national Legal Aid Society input.
- 1978 - Neighbor-Works American chartered by Congress as a non-profit organization, but its mortgage affiliate is Neighborhood Housing Services.

* * * * * * * * * * * * * *

80. Conclusion: **If, as Paragraph No. 52 implies, these subprime mortgages were "designed to fail", new underwriting standards alone will not suffice. Private industry enforcement procedures are now needed. A credit industry-wide Task Force should be empanelled by private industry to see how Big Cap American Corporations were so easily fooled, and what can be done in the future to correct it. American Credit and Investment Corporations cannot leave this task to Congress alone. The European Banking and Credit Markets are watching America for private sector input and leadership. As a consumer, American citizens expect the American Credit, Investment and Banking concerns to also take action to restore market confidence.**

EXHIBIT

Real Estate Frauds and Mortgage Schemes and Scams

EXHIBIT

- Fraud/UDAP (where the assignee is involved in some way),
- Corporate/familial relationships between the parties;
- Civil conspiracy between or among parties;
- Aiding and abetting;
- Knowledge of fraud and acceptance of the "fruits";
- Knowledge of insolvency of seller;
- Licensing violation or other illegality in contract which renders it void;
- No holder in due course status;
- RESPA violation if referral fees were paid or fees were split for the provision of settlement services in the mortgage loan context;
- RICO;
- Padded recording fees
- Back-dating of documents
- Adding insincere co-signers
- Charging for duplicative services
- Requiring high cost credit insurance
- Mandatory arbitration clauses
- Making an unaffordable loan based on the value of the property
- Equity-skimming schemes
- Steering to high rate lenders
- Shifting unsecured debt into high rate mortgages
- Breach of Duty of Good Faith
- Breach of Duty of Fair Dealing
- Please refer to exhibits annexed hereto for scheme explanations.
- Real Property flipping schemes (the sale or resale of the property to increase cost)
- Mortgage flipping schemes (i.e. multiple refinancing to increase fees)
- Homesaver schemes (a/k/a deed equity transfers resulting in loss of deed)
- Reverse redlining schemes
- Taking of a home due to abusive loan terms.
- These experienced attorneys at a closing, can see the "warning signs or red flags" of a predatory mortgage loan such as:
- Excessive interest
- High fees and padded or inflated closing costs
- Paying off low rate mortgages
- Balloon payments
- Negative amortization
- Multiple and excessive closing costs and fees to third parties
- Lending without regard to ability of borrower to repay
- Falsely alleging a borrower has rental income, when the borrower's income is too low.
- Inflated appraisals:

  Inflated appraisals usually occur when the unsuspecting borrower is purchasing a home and the real estate agent then ties this purchase in with a "flipping" of property, i.e., the repeated sale and resale of property, usually by an investor, or even a real estate agent as an owner to inflate the asking price. The appraiser, real estate agent, and lender are often in cahoots. The appraiser may receive a kickback from the real estate agent or lender. The real estate agent's fee is a percentage of the sales price or profits. Similarly, the lender charges high "points" which are percentage-based fees. For both the real estate agent and the lender, they seek a higher sales price, to facilitate higher fees or hidden profits.

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Mortgage Broker or Loan Originator Misconduct

Too often the lender's risky products are combined with little or no oversight of loan originators, whether in-house or third-party mortgage brokers. The lack of sufficient oversight is characterized by:

- Total or near-total reliance on third-party mortgage brokers to originate loans without adequate oversight or monitoring of those brokers and without meaningful protection against fraudulent loan applications.
- False assurances by some mortgage originators and brokers, made orally, that contradict and are inconsistent with the loan documents. These assurances include promises that the lender will refinance the loan when the "teaser" rate expires.
- Brokers and lenders sometimes asked borrowers to execute blank forms, facilitating application fraud and undermining lending disclosure laws.
- False assurances by brokers that the loan offered is the best rate available and that the broker has shopped around for the best rate available to the borrower, without disclosing the financial incentives that may be driving the broker's loan selection.
- Fees payable to mortgage brokers for putting consumers into higher-priced loans than those for which they are eligible.
- Loan products with terms that are difficult for the consumers to understand, resulting in heavy reliance on brokers to represent their clients' interests.

MORTGAGE BROKERS AND SOME DIRECT LENDERS Marketed loan products to borrowers with a variety of risky features, which when combined posed an exceedingly high risk that the loans, predictably, would result in foreclosure. These risky features included:

- 100%financing, typically through an arrangement that provided one loan for 80% and a second, "piggyback loan" for 20% of the purchase price and;
- The use of Adjustable Rate Mortgages (ARM) consisting of a lower fixed rate for a short-term period, followed by an increase to a higher, adjustable rate which then would increase every six months for the remaining years of the loan. These loans were known as 2/28 loans (2 year fixed/28 year adjustable rate) and;
- Borrowers were qualified for ARM loans based on only the initial "teaser rate" without regard to their ability to pay **beyond** that teaser rate. Mortgage brokers often promised borrowers they could simply refinance before the ARM adjustment, without disclosing that such refinancing was entirely dependent on continued house price appreciation and subjecting borrower to heavy pre-payment penalties and;
- Offering "Stated Income", "No-Doc or Low-Doc loans where the borrowers need only to state their income, without providing any supporting documents to obtain a loan and;
- Affixing "Substantial prepayment penalties (three to five years) that sometimes lasted beyond the introductory fixed rate period, thereby penalizing borrowers who refinance their loans once the introductory rate adjusts (Note: New York State limits prepayment penalties to one year but pooled mortgages may not by composed of exclusively N.Y.S. mortgages) and;
- Lenders were encouraging these unfair and deceptive practices by rewarding mortgage brokers who sell risky loan products and specifically, paying mortgage brokers compensation A/K/A Yield Spread Premium (YSP) to place some prime borrowers into loans with sub-prime interest rates higher than those for which they qualified and;
- No current law prevents Mortgage brokers from arranging or processing loans that are not in the borrower's interest, and/or prohibit brokers from brokering loans if the broker's financial interest conflicts with the borrower's interest and;
- No current law prevents mortgage lenders from steering borrowers to loan products that are more costly than those that the borrower qualifies for, and /or prohibits lenders from discriminating between similarly qualifies borrowers and;
- No current law prevents lenders and mortgage brokers engaging in general unfair or in deceptive loan servicing conduct, which led to unnecessary fees and/or foreclosures for borrowers and;

- No current law prevents lenders or their agents from "closing on" these exceedingly risky loan products that mortgage brokers and/or lenders knew or should have known were designed to fail, including loan products that combined 100% financing, no "stated income", and adjustable rates which when combined were a scam on the homeowner and;
- Thereafter, selling those loans through third party investment firms and providing financial incentives to those firms to handle high cost products, but lenders failing to meaningfully disclose or monitor or control or regulate the product was a possible civil fraud on investors.

EXHIBIT B

New York State Banking Department Issues Amendments Affecting Mortgage Bankers and Brokers

The New York State Banking Department has adopted final amendments to Part 410 ("Part 410") of the Department's regulations regarding mortgage bankers and mortgage brokers, effective as of September 22, 2004. The revision to Part 410, among other things, affects (i) bonding requirements for mortgage bankers and mortgage brokers; (ii) record keeping requirements for mortgage bankers and mortgage brokers; and (iii) consultants, employees and independent contractors of mortgage bankers and mortgage brokers.

The Superintendent has the discretion to require twice the amount of bond or deposit based on consumer complaints against the mortgage broker.

c. Surety Bonds and Deposit Agreements for Mortgage Bankers and Mortgage Brokers.

Revised Part 410 specifies for mortgage bankers and mortgage brokers language to be contained in a corporate surety bond and the form of deposit agreement to be filed with the Superintendent in connection with a pledge of assets. It also requires mortgage bankers and mortgage brokers to maintain statements and withdrawal requests related to any pledge of assets.

d. Record Keeping Requirements – Mortgage Bankers and Mortgage Brokers.

RECORD KEEPING

Revised Part 410 specifies additional record keeping requirements for mortgage bankers and mortgage brokers as follows:

- Each mortgage banker and mortgage broker must maintain a centralized application log for the principal office and all branch offices, updated daily. Branches must report activity to the principal office not later than noon on the fifth business day after the activity takes place.
- Each mortgage banker must maintain all documents relating to credit, underwriting and pricing on a loan application, whether or not an application is denied, approved or withdrawn.
- Each mortgage broker must maintain a copy of the HUD-1 in each loan file.
- Each mortgage banker must establish and maintain, if overages are charged, lending policies and procedures regarding imposition of overages. This requires inclusion of the rate sheet in the file or information sufficient to identify the rate sheet used to price the loan.
- Each mortgage banker must establish and maintain lending policies and procedures for (i) charging of discount or origination points or (ii) payment of premium pricing to mortgage brokers.
- Except in the case of loans for federally related mortgage loan programs including, but not limited to, any loan purchased by the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation, securitized by the Government National Mortgage Association or insured by the Federal Housing Administration, the Veterans' Administration or the Farmers' Home Administration or loans that are prime no documentation/low documentation or alternative documentation loans, each mortgage banker must establish and maintain lending policies and procedures on (i) loan pricing and exceptions to such loan pricing, (ii) pricing matrices; and (iii) credit grades.
- Each mortgage banker must maintain a mortgage loan commitment pipeline by state and in the aggregate which is updated on a monthly basis. The report must include number of loans, type of loans, number and amount of loans with locked and unlocked interest rate and date of commitment along with fees collected from the borrower. These reports must be maintained for one year.

- Each mortgage banker must maintain, for loans where the applicant entered into a lock-in agreement for the interest rate, a report updated monthly showing the lock-in date and fees collected. These reports must be maintained for one year.

- Each mortgage banker must maintain a report of lines of credit, updated weekly, showing advances on the outstanding lines.

- Each mortgage banker must maintain a list, by state, of closing agents and their name, address and telephone number.

- Within 45 days of the end of each fiscal quarter, each mortgage banker must file with the Department (i) unaudited financial statements including a balance sheet, income statement, cash flow and net worth; and (ii) the number and dollar amount of unfunded and unclosed commitments.
- Each mortgage banker must employ a compliance officer or retain an unaffiliated third party to provide such services.

COMPLIANCE OFFICER

- Within ten days of receipt, each mortgage banker certified by Fannie Mae or Freddie Mac (collectively, the "Agencies") must file with the Department (i) copies of financial reports filed with the Agencies, (ii) copies of audit letters and certifications by the Agencies and (iii) copies of letters withdrawing certification by the Agencies.

- Within ten days of receipt, each mortgage banker must file with the Department a certified copy of a report of audit of the mortgage banker or its affiliate by any lender, investor, party to a loan purchase agreement or any federal agency.

- Each mortgage banker exempt from HMDA reporting requirements pursuant to Section 203.3 of Regulation C must maintain the same data as required by Regulation C for review by the Superintendent.

(e.) Consultants, Employees and Independent Contractors of Mortgage Bankers and Mortgage Brokers.

Revised Part 410 contains definitions for consultants, employees and independent contractors of mortgage bankers and mortgage brokers.

Applicants to become a mortgage banker or mortgage broker must provide a list of its consultants at the time of application. A mortgage banker or mortgage broker must also file a list of consultants with the Superintendent within ten days of retaining a consultant. Finally, a mortgage banker or mortgage broker must notify the Superintendent within ten days of termination of any consultant.

A mortgage banker or mortgage broker must file with the Superintendent an undertaking of accountability for each independent contractor within ten days of retaining the independent contractor. A mortgage banker or mortgage broker must also give the Superintendent notice of termination of an independent contractor within 10 days of termination.

(f.) Filings by Mortgage Bankers and Mortgage Brokers.

All filings under revised Part 410 may be submitted electronically in a format acceptable to the Superintendent.

EXHIBIT C

Section 5-501 New York State General Obligation Law

Pre-payment Penalty (one year)

Sec. 5-501(3)(b)

§ 5-501. Rate of interest; usury forbidden. 1. The rate of interest, as computed pursuant to this title, upon the loan or forbearance of any money, goods, or things in action, except as provided in subdivisions five and six of this section or as otherwise provided by law, shall be six per centum per annum unless a different rate is prescribed in section fourteen-a of the banking law.

2. No person or corporation shall, directly or indirectly, charge, take or receive any money, goods or things in action as interest on the loan or forbearance of any money, goods or things in action at a rate exceeding the rate above prescribed. The amount charged, taken or received as interest shall include any and all amounts paid or payable, directly or indirectly, by any person, to or for the account of the lender in consideration for making the loan or forbearance as defined by the banking board pursuant to subdivision three of section fourteen-a of the banking law except such fee as may be fixed by the commissioner of taxation and finance as the cost of servicing loans made by the property and liability insurance security fund.

3. If the rate of interest charged, taken or received on any loan or forbearance secured primarily by either (i) an interest in real property improved by a one to six family residence occupied by the owner or (ii) certificates of stock or other evidence of an ownership interest in a corporation or partnership formed for the purpose of the cooperative ownership of real estate taken as security for a loan under subdivision five of section one hundred three of the banking law, subdivision eight-a of section two hundred thirty-five of such law or subdivision two-a of section three hundred eighty of such law, exceeds six per centum per annum,

a. in the case of a loan referred to by clause (i) of this subdivision, the term of such loan or forbearance may extend five years beyond the maximum maturity of such loan otherwise prescribed by law, ~~and~~

b. notwithstanding any other provision of law, the unpaid balance of the loan or forbearance may be prepaid, in whole or in part, at any time. If prepayment is made on or after one year from the date the loan or forbearance is made, no penalty may be imposed. If prepayment is made prior to such time, no penalty may be imposed unless provision therefor is expressly made in the loan contract. In all cases, the right of prepayment shall be stated in the instrument evidencing the loan or forbearance, provided, however, that the provisions of this subdivision shall not apply to the extent such provisions are inconsistent with any federal law or regulation.

4. Except as otherwise provided by law, interest shall not be charged, taken or received on any loan or forbearance at a rate exceeding such rate of interest as may be authorized by law at the time the loan or forbearance is made, whether or not the loan or forbearance is made pursuant to a prior contract or commitment providing for a greater rate of interest, provided, however, that no change in the rate of interest prescribed in section fourteen-a of the banking law shall affect (a) the validity of a loan or forbearance made before the date such rate becomes effective, or (b) the enforceability of such loan or forbearance in accordance with its terms, except that if any loan or forbearance provides for an increase in the rate of interest during the term of such loan or forbearance, the increased rate shall not exceed such rate of interest as may have been authorized by law at the time such loan or forbearance was made.

4-a. Notwithstanding the provisions of subdivision four of this section, a loan or forbearance repayable on demand may provide for changes, reflecting variations in lending rates, from time to time in

EXHIBIT D

PART 41 N.Y.S. REGS. OF BANKING BOARD

"CONSUMER CAUTION AND HOME OWNERSHIP COUNSELING NOTICE

If you obtain this loan, which pursuant to New York State Law is a High-Cost Home Loan, the lender will have a mortgage on your home. You could lose your home, and any money you have put into it, if you do not meet your obligations under the loan.

You should shop around and compare loan rates and fees. Mortgage loan rates and closing costs and fees vary based on many factors, including your particular credit and financial circumstances, your earnings history, the loan-to-value requested, and the type of property that will secure your loan. The loan rate and fees could vary based on which lender or mortgage broker you select. Higher rates and fees may be related to the individual circumstances of a particular consumer's application.

You should consider consulting a qualified independent credit counselor or other experienced financial adviser regarding the rate, fees, and provisions of this mortgage loan before you proceed. The enclosed list of counselors is provided by the New York State Banking Department.

You are not required to complete any loan agreement merely because you have received these disclosures or have signed a loan application. If you proceed with this mortgage loan, you should also remember that you may face serious financial risks if you use this loan to pay off credit card debts and other debts in connection with this transaction and then subsequently incur significant new credit card charges or other debts. If you continue to accumulate debt after this loan is closed and then experience financial difficulties, you could lose your home and any equity you have in it if you do not meet your mortgage loan obligations.

Property taxes and homeowner's insurance are your responsibility. Not all lenders provide escrow services for these payments. You should ask your lender about these services.

Your payments on existing debts contribute to your credit ratings. You should not accept any advice to ignore your regular payments to your existing creditors. Accordingly, it is important that you make regular payments to your existing creditors."

If the notice required by this paragraph is given to the borrower separately from counseling notice required by paragraph (1) of this subdivision, then the list of counselors so enclosed in the counseling notice disclosure shall be enclosed also with this disclosure notice. Such disclosure shall be on a separate form. In order to utilize an electronic transmission, the lender or broker must first obtain either written or electronically transmitted permission from the borrower.

N.Y.S. BANKING Board

A list of approved counselors, available from the New York State Banking Department, shall be provided to the borrower by the lender or the mortgage broker at the time that this disclosure is given. The lender or mortgage broker may provide to the borrower the entire list of counselors or those portions of the list which pertain to both the geographic area in which the borrower resides and any adjacent area or areas.

2. Within three days after determining that the loan is a high cost home loan, but no less than ten days before closing, a lender or mortgage broker shall not make or arrange a high cost home loan unless either the lender or the mortgage broker has delivered to the borrower in writing, either placed in the mail, faxed or electronically transmitted, the following notice in at least twelve-point type:

EXHIBIT E

Company Release - 10/01/2007 09:00

WaMu Implements Industry Leading Standard for Mortgage Brokers, Launches Direct Call Program
New Processes Aimed at Building Consumer Knowledge and Strengthening Mortgage Industry

SEATTLE--(BUSINESS WIRE)--

Washington Mutual (NYSE:WM) today unveiled a new, industry-leading standard for mortgage brokers with whom it does business to help ensure that borrowers fully understand the terms of the loan their brokers are requesting in addition to the total compensation the borrower will pay to the broker for their services.

As part of its new broker standard, WaMu will require evidence that the broker has made certain disclosures to the borrower early in the application process, including:

-- key terms of the loan requested by the broker such as loan amount, loan term, whether the interest rate and mortgage payments may change, and whether the borrower's pricing package carries a prepayment fee, and

-- the amount of all compensation the borrower will pay the broker for their services, including broker points, or administrative or processing fees, and whether the broker has requested a yield spread premium.

In addition, a WaMu representative will attempt to call every borrower who is represented by a broker prior to closing to review the key loan terms directly with the customer.

"We believe our mortgage broker standard and direct call program should become the new industry benchmark for brokers and lenders across the nation," said Kerry Killinger, WaMu Chairman and CEO. "By adopting these standards, together we can increase consumer knowledge of the home loan process and bring about positive, meaningful change to the mortgage industry."

"Our wholesale business is an important component of our lending strategy and we value our relationships with the high-quality and customer-focused brokers we do business with," said David Schneider, WaMu's Home Loans President. "We believe that brokers will embrace this standard because an educated and informed consumer is the best customer for both WaMu and brokers alike."

WaMu has a long history of taking a leadership role in addressing the credit needs of its communities and setting the highest standards for responsible lending. In 2001, WaMu established its Responsible Mortgage Lending Principles, becoming one of the first lenders to create specific principles to guide its mortgage lending activity.

Since that time, the company has continued to take proactive steps to respond to the needs of borrowers. These industry innovations include the commitment to refinance up to $2 billion in subprime loans, announced in April, to assist current borrowers feeling the effects of this challenging environment. WaMu also led the industry in implementing subprime lending standards that eliminated subprime stated-income loans and subprime adjustable rate mortgage loans with initial fixed-rate terms of less then five years (effectively the 2/28 and 3/27 products). The standards also require tax and insurance escrow accounts with all new subprime loans WaMu originates and a WaMu conversation with the borrower before loan documents are prepared.

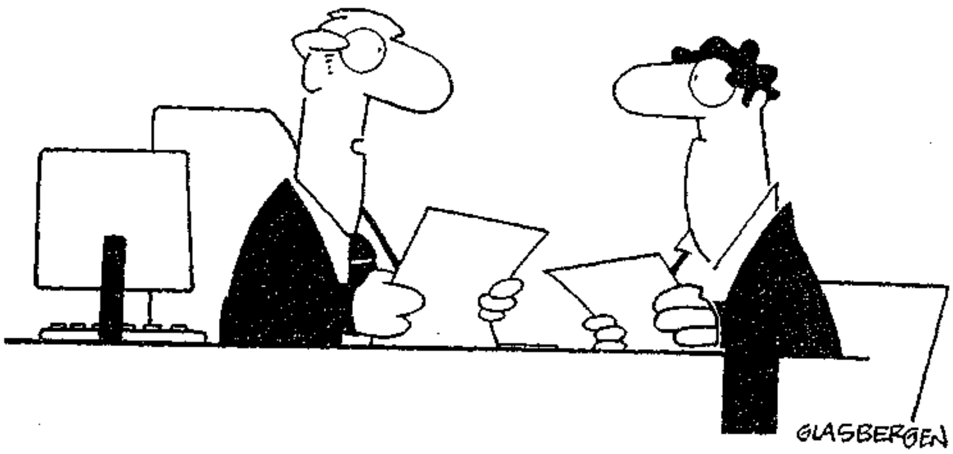
(Note to editor: A copy of the new broker disclosure form is available upon request.)

About WaMu

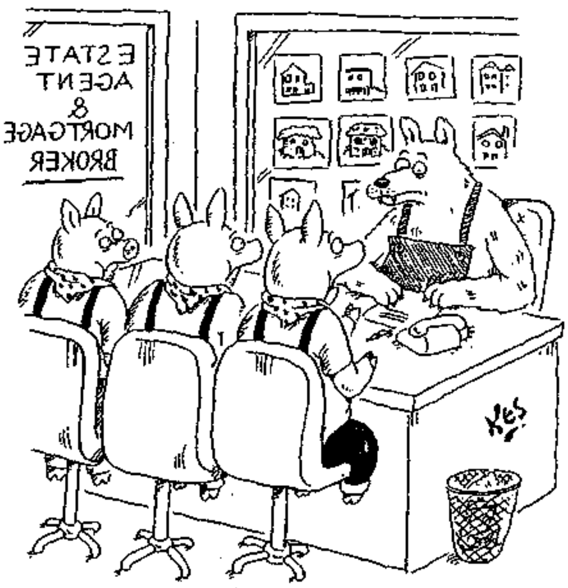
WaMu, through its subsidiaries, is one of the nation's leading consumer and small business banks. At June 30, 2007, WaMu and its subsidiaries had assets of $312.22 billion. The company has a history dating back to 1889 and its subsidiary banks currently operate more than 2,700 consumer and small business banking stores throughout the nation. WaMu's press releases are available at http://newsroom.wamu.com

Source: Washington Mutual

*"They did to me what a man with a gun in a dark alley couldn't do.
They stole my house."*



"It's an adjustable mortgage. If interest rates go up, your payment increases. If interest rates go down, your payment increases."



" So what happens if we can't meet our monthly mortgage repayments?"

Top Subprime Lenders, Before the Bust

Many of the lenders that did the most subprime lending have either gone out of business or scaled back.

Top subprime lenders	New loans, in billions, for 2006
HSBC	$52.8
New Century Financial	51.6
Countrywide Financial	40.6
CitiMortgage	38.0
WMC Mortgage	33.2
Fremont Investment & Loan	32.3
Ameriquest Mortgage	29.5
Option One Mortgage	28.8
Wells Fargo	27.9
First Franklin Financial	27.7
Washington Mutual	26.6
Residential Funding	21.2
Aegis Mortgage	17.0
Accredited Home Lenders	15.8
American General Finance	15.1
BNC Mortgage	13.7
Chase Home Finance	11.6
Equifirst	10.8
NovaStar Financial	10.2
Ownit Mortgage Solutions	9.5

Source: Inside Mortgage Finance THE NEW YORK TIMES

The Top Ten

Top issuers of collateralized debt obligations

	Issuance Jan.-Jun. 2007 *in billions*	Growth Since Jan.-Jun. 2006
Merrill Lynch	$33.4	46%
Citigroup	28.0	45
Barclays Capital	24.7	187
ABN Amro	18.0	1,130
Deutsche Bank	17.0	30
Goldman Sachs	16.9	6
Wachovia	15.8	66
UBS	15.0	75
JPMorgan Chase	13.5	93
Bank of America	12.8	20
TOTAL *all banks*	**286.0**	**44**

Source: Asset-Backed Alert

THE NEW YORK TIMES

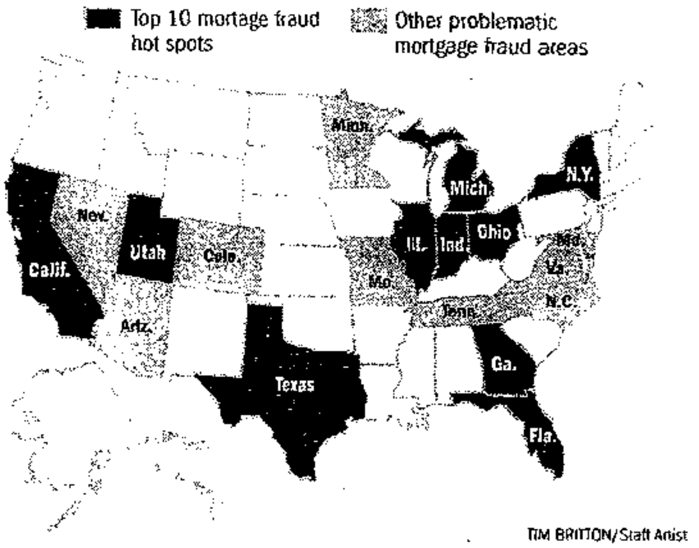
Top five mortgage originators in 2006 with a breakout of their subprime lending, in billions of dollars

	Subprime originations	Total originations
Countrywide Financial	$40.6	$462.5
Wells Fargo Home Mortgage	$27.9	$397.6
Washington Mutual	$26.6	$195.7
CitiMortgage	$38.0	$183.5
Chase Home Finance	$11.6	$172.9

Sources: Inside Mortgage Finance; Inside B&C Lending BLOOMBERG NEWS

Mortgage fraud on the map

As mortgage fraud has grown, Florida has emerged as one of the nation's trouble spots, the FBI says.



TIM BRITTON/Staff Artist

Florida tops nation in mortgage fraud

Florida ranked No. 1 in mortgage fraud in 2006, according to a study by Mortgage Asset Research Institute LLC of Reston, Va. The rankings are based on the number of loans where lenders suspect or find fraud.

Ranking/State (2005 Rank)

1. Florida..........4
2. California.......8
3. Michigan 2
4. Georgia 1
5. Utah 7
6. New York 11
7. Illinois............3
8. Minnesota ...10
9. Colorado 5
10. Nevada......14

Source: Mortgage Asset Research Institute LLC

Top 10

Lenders with the most foreclosures in New York City and Westchester:

1. Freemont Bank
2. WMC
3. New Century
4. Argent
5. Option One
6. Countrywide
7. Wells Fargo
8. First Franklin
9. Alliance
10. Washington Mutual

Source: Sen. Jeffrey Klein

Top mortgage advertisers
Jan.-June '07

		IN MILLIONS
1	GMAC	$46.2
2	Quicken Loans	37.0
3	Countrywide	23.0
4	Capital One	12.5
5	Greenlight	6.9
6	National Mortgage	5.2
7	American Equity	5.2
8	Lenox Financial	4.7
9	Paramount Equity	4.5
10	Indymac	4.4

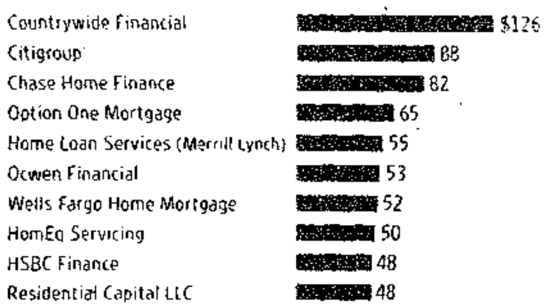
*Does not include online

Source: Nielsen Monitor-Plus, Nielsen//NetRatings

THE NEW YORK TIMES

Messy Work

Top 10 subprime-mortgage servicers for first six months of 2007, by size of portfolio, in billions



This total combines AMC, which wasn't purchased until 9/1/07, with CitiMortgage

Source: Inside Mortgage Finance Publications Inc

(PART 1 OF
2 SERIES)

THE NEW YORK TIMES, SUNDAY, AUGUST 26, 2007

Inside the Countrywide Lending Spree

By GRETCHEN MORGENSON

ON its way to becoming the nation's largest mortgage lender, the **Countrywide Financial Corporation** encouraged its sales force to court customers over the telephone with a seductive pitch that seldom varied. "I want to be sure you are getting the best loan possible," the sales representatives would say.

But providing "the best loan possible" to customers wasn't always the bank's main goal, say some former employees. Instead, potential borrowers were often led to high-cost and sometimes unfavorable loans that resulted in richer commissions for Countrywide's smooth-talking sales force, outsize fees to company affiliates providing services on the loans, and a roaring stock price that made Countrywide executives among the highest paid in America.

Countrywide's entire operation, from its computer system to its incentive pay structure and financing arrangements, is intended to wring maximum profits out of the mortgage lending boom no matter what it costs borrowers, according to interviews with former employees and brokers who worked in different units of the company and internal documents they provided. One document, for instance, shows that until last September the computer system in the company's subprime unit excluded borrowers' cash reserves, which had the effect of steering them away from lower-cost loans to those that were more expensive to homeowners and more profitable to Countrywide.

Now, with the entire mortgage business on tenterhooks and industry practices under scrutiny by securities regulators and banking industry overseers, Countrywide's money machine is sputtering. So far this year, fearful investors have cut its stock in half. About two weeks ago, the company was forced to draw down its entire $11.5 billion credit line from a consortium of banks because it could no longer sell or borrow against home loans it has made. And last week, **Bank of America** invested $2 billion for a 16 percent stake in Countrywide, a move that came amid speculation that Countrywide's survival was in question and that it had become a takeover target — notions that Countrywide publicly disputed.

Inside the Countrywide Lending Spree

Homeowners, meanwhile, drawn in by Countrywide sales scripts assuring "the best loan possible," are behind on their mortgages in record numbers. As of June 30, almost one in four subprime loans that Countrywide services was delinquent, up from 15 percent in the same period last year, according to company filings. Almost 10 percent were delinquent by 90 days or more, compared with last year's rate of 5.35 percent.

Many of these loans had interest rates that recently reset from low teaser levels to double digits; others carry prohibitive prepayment penalties that have made refinancing impossibly expensive, even before this month's upheaval in the mortgage markets.

To be sure, Countrywide was not the only lender that sold questionable loans with enormous fees during the housing bubble. And as real estate prices soared, borrowers themselves proved all too eager to participate, even if it meant paying high costs or signing up for a loan with an interest rate that would jump in coming years.

But few companies benefited more from the mortgage mania than Countrywide, among the most aggressive home lenders in the nation. As such, the company is Exhibit A for the lax and, until recently, highly lucrative lending that has turned a once-hot business ice cold and has touched off a housing crisis of historic proportions.

"In terms of being unresponsive to what was happening, to sticking it out the longest, and continuing to justify the garbage they were selling, Countrywide was the worst lender," said Ira Rheingold, executive director of the National Association of Consumer Advocates. "And anytime states tried to pass responsible lending laws, Countrywide was fighting it tooth and nail."

Started as Countrywide Credit Industries in New York 38 years ago by Angelo R. Mozilo, a butcher's son from the Bronx, and David Loeb, a founder of a mortgage banking firm in New York, who died in 2003, the company has become a $500 billion home loan machine with 62,000 employees, 900 offices and assets of $200 billion. Countrywide's stock price was up 561 percent over the 10 years ended last December.

Mr. Mozilo has ridden this remarkable wave to immense riches, thanks to generous annual stock option grants. Rarely a buyer of Countrywide shares — he has not bought a share since 1987, according to Securities and Exchange Commission filings — he has been a huge seller in recent years. Since the company listed its shares on the New York Stock Exchange in 1984, he has reaped $406 million selling Countrywide stock.

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As the subprime mortgage debacle began to unfold this year, Mr. Mozilo's selling accelerated. Filings show that he made $129 million from stock sales during the last 12 months, or almost one-third of the entire amount he has reaped over the last 23 years. He still holds 1.4 million shares in Countrywide, a 0.24 percent stake that is worth $29.4 million.

"Mr. Mozilo has stated publicly that his current plan recognizes his personal need to diversify some of his assets as he approaches retirement," said Rick Simon, a Countrywide spokesman. "His personal wealth remains heavily weighted in Countrywide shares, and he is, by far, the leading individual shareholder in the company."

Mr. Simon said that Mr. Mozilo and other top Countrywide executives were not available for interviews. The spokesman declined to answer a list of questions, saying that he and his staff were too busy.

A former sales representative and several brokers interviewed for this article were granted anonymity because they feared retribution from Countrywide.

AMONG Countrywide's operations are a bank, overseen by the Office of Thrift Supervision; a broker-dealer that trades United States government securities and sells mortgage-backed securities; a mortgage servicing arm; a real estate closing services company; an insurance company; and three special-purpose vehicles that issue short-term commercial paper backed by Countrywide mortgages.

Last year, Countrywide had revenue of $11.4 billion and pretax income of $4.3 billion. Mortgage banking contributed mightily in 2006, generating $2.06 billion before taxes. In the last 12 months, Countrywide financed almost $500 billion in loans, or around $41 billion a month. It financed 177,000 to 240,000 loans a month during the last 12 months.

Countrywide lends to both prime borrowers — those with sterling credit — and so-called subprime, or riskier, borrowers. Among the $470 billion in loans that Countrywide made last year, 45 percent were conventional nonconforming loans, those that are too big to be sold to government-sponsored enterprises like Fannie Mae or Freddie Mac. Home equity lines of credit given to prime borrowers accounted for 10.2 percent of the total, while subprime loans were 8.7 percent.

Regulatory filings show that, as of last year, 45 percent of Countrywide's loans carried adjustable rates — the kind of loans that are set to reprice this fall and later, and which are causing so much anxiety among borrowers and investors alike. Countrywide has a huge presence in California: 46 percent of the loans it holds on its books were made there, and 28 percent of the loans it services are there. Countrywide packages most of its loans into securities pools that it sells to investors.

Another big business for Countrywide is loan servicing, the collection of monthly principal and interest payments from borrowers and the disbursement of them to investors. Countrywide serviced 8.2 million loans as of the end of the year; in June the portfolio totaled $1.4 trillion. In addition to the enormous profits this business generates — $660 million in 2006, or 25 percent of its overall earnings — customers of the Countrywide servicing unit are a huge source of leads for its mortgage sales staff, say former employees.

In a mid-March interview on CNBC, Mr. Mozilo said Countrywide was poised to benefit from the spreading crisis in the mortgage lending industry. "This will be great for Countrywide," he said, "because at the end of the day, all of the irrational competitors will be gone."

But Countrywide documents show that it, too, was a lax lender. For example, it wasn't until March 16 that Countrywide eliminated so-called piggyback loans from its product list, loans that permitted borrowers to buy a house without putting down any of their own money. And Countrywide waited until

Feb. 23 to stop peddling another risky product, loans that were worth more than 95 percent of a home's appraised value and required no documentation of a borrower's income.

As recently as July 27, Countrywide's product list showed that it would lend $500,000 to a borrower rated C-minus, the second-riskiest grade. As long as the loan represented no more than 70 percent of the underlying property's value, Countrywide would lend to a borrower even if the person had a credit score as low as 500. (The top score is 850.)

Build an 'oasis of rapport' with potential borrowers, a company manual says.

The company would lend even if the borrower had been 90 days late on a current mortgage payment twice in the last 12 months, if the borrower had filed for personal bankruptcy protection, or if the borrower had faced foreclosure or default notices on his or her property.

Such loans were made, former employees say, because they were so lucrative — to Countrywide. The company harvested a steady stream of fees or payments on such loans and busily repackaged them as securities to sell to investors. As long as housing prices kept rising, everyone — borrowers, lenders and investors — appeared to be winners.

One former employee provided documents indicating Countrywide's minimum profit margins on subprime loans of different sizes. These ranged from 5 percent on small loans of $100,000 to $200,000 to 3 percent on loans of $350,000 to $500,000. But on subprime loans that imposed heavy burdens on borrowers, like high prepayment penalties that persisted for three years, Countrywide's margins could reach 15 percent of the loan, the former employee said.

Regulatory filings show how much more profitable subprime loans are for Countrywide than higher-quality prime loans. Last year, for example, the profit margins Countrywide generated on subprime loans that it sold to investors were 1.84 percent, versus 1.07 percent on prime loans. A year earlier, when the subprime machine was really cranking, sales of these mortgages produced profits of 2 percent, versus 0.82 percent from prime mortgages. And in 2004, subprime loans produced gains of 3.64 percent, versus 0.93 percent for prime loans.

One reason these loans were so lucrative for Countrywide is that investors who bought securities backed by the mortgages were willing to pay more for loans with prepayment penalties and those whose interest rates were going to reset at higher levels. Investors ponied up because pools of subprime loans were likely to generate a larger cash flow than prime loans that carried lower fixed rates.

As a result, former employees said, the company's commission structure rewarded sales representatives for making risky, high-cost loans. For example, according to another mortgage sales representative affiliated with Countrywide, adding a three-year prepayment penalty to a loan would generate an extra 1 percent of the loan's value in a commission. While mortgage brokers' commissions would vary on loans that reset after a short period with a low teaser rate, the higher the rate at reset, the greater the commission earned, these people said.

Persuading someone to add a home equity line of credit to a loan carried extra commissions of 0.25 percent, according to a former sales representative.

"The whole commission structure in both prime and subprime was designed to reward salespeople for pushing whatever programs Countrywide made the most money on in the secondary market," the former sales representative said.

CONSIDER an example provided by a former mortgage broker. Say that a borrower was persuaded to take on a $1 million adjustable-rate loan that required the person to pay only a tiny fraction of the real interest rate and no principal during the first year — a loan known in the trade as a pay option adjustable-rate mortgage. If the loan carried a three-year prepayment penalty requiring the borrower to pay six months' worth of interest at the much higher reset rate of 3 percentage points over the prevailing market rate, Countrywide would pay the broker a $30,000 commission.

When borrowers tried to reduce their mortgage debt, Countrywide cashed in: prepayment penalties generated significant revenue for the company — $268 million last year, up from $212 million in 2005. When borrowers had difficulty making payments, Countrywide cashed in again: late charges produced even more in 2006 — some $285 million.

The company's incentive system also encouraged brokers and sales representatives to move borrowers into the

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Countrywide

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subprime category, even if their financial position meant that they belonged higher up the loan spectrum. Brokers who peddled subprime loans received commissions of 0.50 percent of the loan's value, versus 0.20 percent on loans one step up the quality ladder, known as Alternate-A, former brokers said. For years, a software system in Countrywide's subprime unit that sales representatives used to calculate the loan type that a borrower qualified for did not allow the input of a borrower's cash reserves, a former employee said.

A borrower who has more assets poses less risk to a lender, and will typically get a better rate on a loan as a result. But, this sales representative said, Countrywide's software prevented the input of cash reserves so borrowers would have to be pitched on pricier loans. It was not until last September that the company changed this practice, as part of what was called in an internal memo the "Do the Right Thing" campaign.

According to the former sales representative, Countrywide's big subprime unit also avoided offering borrowers Federal Housing Administration loans, which are backed by the United States government and are less risky. But these loans, well suited to low-income or first-time home buyers, do not generate the high fees that Countrywide encouraged its sales force to pursue.

A few weeks ago, the former sales representative priced a $275,000 loan with a 30-year term and a fixed rate for a borrower putting down 10 percent, with fully documented income, and a credit score of 620. While a F.H.A. loan on the same terms would have carried a 7 percent rate and 0.125 percentage points, Countrywide's subprime loan for the same borrower carried a rate of 9.875 percent and three additional percentage points.

The monthly payment on the F.H.A. loan would have been $1,829, while Countrywide's subprime loan generated a $2,387 monthly payment. That amounts to a difference of $558 a month, or $6,696 a year — no small sum for a low-income homeowner.

"F.H.A. loans are the best source of financing for low-income borrowers," the former sales representative said. So Countrywide's subprime lending program "is not living up to the promise of providing the best loan programs to its clients," he said.

Mr. Simon of Countrywide said that Federal Housing Administration loans were becoming a bigger part of the company's business.

"While they are very useful to some borrowers, F.H.A./V.A. mortgages are extremely difficult to originate in markets with above-average home prices, because the maximum loan amount is so low," he said. "Countrywide believes F.H.A./V.A. loans are an increasingly important part of its product menu, particularly for the homeownership hopes of low- to moderate-income and minority borrowers we have concentrated on reaching and serving."

LUCAS JACKSON/REUTERS

Angelo R. Mozilo, chief executive of the Countrywide Financial Corporation, remains undaunted as the mortgage market has cooled.

WORKDAYS at Countrywide's mortgage lending units centered on an intense telemarketing effort, former employees said. It involved chasing down sales leads and hewing to carefully prepared scripts during telephone calls with prospects.

One marketing manual used in Countrywide's subprime unit during 2005, for example, walks sales representatives through the steps of a successful call. "Step 3, Borrower Information, is where the Account Executive gets on the Oasis of Rapport," the manual states. "The Oasis of Rapport is the time spent with the client building rapport and gathering information. At this point in the sales cycle, rates, points, and fees are not discussed. The immediate objective is for the Account Executive to get to know the client and look for points of common interest. Use first names with clients as it facilitates a friendly, helpful tone."

If clients proved to be uninterested, the script provided ways for sales representatives to be more persuasive. Account executives encountering prospective customers who said their mortgage had been paid off, for instance, were advised to ask about a home equity loan. "Don't you want the equity in your home to work for you?" the script said. "You can use your equity for your advantage and pay bills or get cash out. How does that sound?"

Other documents from the subprime unit also show that Countrywide was willing to underwrite loans that left little disposable income for borrowers' food, clothing and other living expenses. A different manual states that loans could be written for borrowers even if, in a family of four, they had just $1,000 in disposable income after paying their mortgage bill. A loan to a single borrower could be made even if the person had just $550 left each month to live on, the

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manual said.

Independent brokers who have worked with Countrywide also say the company does not provide records of their compensation to the Internal Revenue Service on a Form 1099, as the law requires. These brokers say that all other home lenders they have worked with submitted 1099s disclosing income earned from their associations.

One broker who worked with Countrywide for seven years said she never got a 1099.

"When I got ready to do my first year's taxes I had received 1099s from everybody but Countrywide," she said. "I called my rep and he said, 'We're too big. There's too many. We don't do it.' "

A different broker supplied an e-mail message from a Countrywide official stating that it was not company practice to submit 1099s. It is unclear why Countrywide apparently chooses not to provide the documents. Countrywide boasts that it is the No. 1 lender to minorities, providing those borrowers with their piece of the American homeownership dream. But it has run into problems with state regulators in New York, who contended that the company overcharged such borrowers for loans. Last December, Countrywide struck an agreement with Eliot Spitzer, then the state attorney general, to compensate black and Latino borrowers to whom it had improperly given high-cost loans in 2004. Under the agreement, Countrywide, which cooperated with the attorney general, agreed to improve its fair-lending monitoring activities and set up a $3 million consumer education program.

But few borrowers of any sort, even the most creditworthy, appear to escape Countrywide's fee machine. When borrowers close on their loans, they pay fees for flood and tax certifications, appraisals, document preparation, even charges associated with e-mailing documents or using FedEx to send or receive paperwork, according to Countrywide documents. It's a big business: During the last 12 months, Countrywide did 3.5 million flood certifications, conducted 10.8 million credit checks and 1.3 million appraisals, its filings show. Many of the fees go to its loan closing services subsidiary, LandSafe Inc.

According to dozens of loan documents, LandSafe routinely charges tax service fees of $60, far above what other lenders charge, for information about any outstanding tax obligations of the borrowers. Credit checks can cost $36 at LandSafe, double what others levy. Some Countrywide loans even included fees of $100 to e-mail documents or $45 to ship them overnight. LandSafe also charges borrowers $26 for flood certifications, for which other companies typically charge $12 to $14, according to sales representatives and brokers familiar with the fees.

LAST April, Countrywide customers in Los Angeles filed suit against the company in California state court, contending that it overcharged borrowers by collecting unearned fees in relation to tax service fees and flood certification charges. These markups were not disclosed to borrowers, the lawsuit said.

Appraisals are another profit center for Countrywide, brokers said, because it often requires more than one appraisal on properties, especially if borrowers initially choose not to use the company's own internal firm. Appraisal fees at Countrywide totaled $137 million in 2006, up from $110 million in the previous year. Credit report fees were $74 million last year, down slightly from 2005.

All of those fees may soon be part of what Countrywide comes to consider the good old days. The mortgage market has cooled, and so have the company's fortunes. Mr. Mozilo remains undaunted, however.

In an interview with CNBC on Thursday, he conceded that Countrywide's balance sheet had to be strengthened. "But at the end of the day we could be doing very substantial volumes for high-quality loans," he said, "because there is nobody else in town." □