BUILDING SUSTAINABLE HOMEOWNERSHIP:
RESPONSIBLE LENDING AND INFORMED CONSUMER CHOICE

PUBLIC HEARING ON THE HOME EQUITY LENDING MARKET

FEDERAL RESERVE BANK OF SAN FRANCISCO
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MR. OLSON: Good morning. I'm Mark Olson, Federal Reserve Board of Governors. We are delighted this is the third in a series of hearings that we have had on HOEPA. It's a repeat of a series of hearings that were held about six years ago that led to at that point implementation of the HOEPA regs and others.

Let me -- let me first of all just outline the day and what the expectations are. We have three panels. Heavy focus on nontraditional products in the mortgage area. By design, we have -- we use the San Francisco, essentially the west coast, hearing to focus on that.

Much of the rest of the country seems to think that the nontraditional products are relatively new. As we will hear today, they're not new products on the west coast, and so your experience here is -- I think will be very valuable for our overall understanding of the -- of the role of the new products in the marketplace, both the positives and some of the issues that are created.

The first panel will go until 10:30. We will then take a break and have the second panel that will go until 12:30. And then break for lunch and then an afternoon panel.

Very importantly, at about 3:00, hopefully precisely 3:00, we will have what we call an open mic time. And that's -- at that time it will be an opportunity for anybody who would like to speak to speak.

And if you would -- if you would care to avail yourself of that opportunity, there will be a sign-up sheet. And that sign-up sheet, it will be -- where will they find the sign-up?

MS. REID: Outside right now but --

MR. OLSON: Just out the door right here. So make sure you've signed up sometime between now and then if you would care to avail yourself.

For the panelists, there will be a -- each of you will be asked if you could summarize your comments in five minutes. We enforce it.

MS. REID: I'm your timekeeper. I'll hold up this "one minute left."

MR. OLSON: And what we've discovered -- we didn't discover it. It's been coming up. So much of the value of these hearings comes out of the dialogue, in the discussion. So I think -- and then we will -- a summary for five minutes and then we will move on from there.

Just to introduce my fellow panelists, Leonard Chanin, Sandy Braunstein, my colleagues from Washington, D.C., and Jack Richards from the San Francisco Fed.

There are three areas of focus for these hearings. Number one has been, of course, the impact of predatory lending and the effectiveness of the HOEPA regs. Second has been a look at this new phenomenon called the nontraditional mortgage products.

And that -- in the intervening six years, some very remarkable things have happened in the marketplace. And what has happened essentially is that we have seen through a combination of technology and secondary market appetite and a highly liquid market, there is a -- whereas the secondary market had for many years focused primarily on the conforming product, the Fannie and Freddie conforming product, the fact that that secondary market now has an appetite for the nontraditional product has had a number of implications, both good -- largely good frankly because of the -- because it has provided a liquid source for more mortgage product, there are more people who have access to mortgage money than ever before, and a wider variety of a range of products.

The difficulty comes because of the fact that sometimes there are products where we -- that we clearly have recognized, where people are put into products that they probably shouldn't be, either -- for whatever reason. And that's part of what we are -- we're going to probe today. The extent to which those products are, in fact -- how they're marketed, how they're used, and the experience that we've had with them.

It is hoped -- the expectation is that there will be four objectives or four goals that will come out of these hearings: Number one, an evaluation of the effectiveness of the HOEPA regs; number two, there is -- we will be at some point looking to review a Reg Z, and some of the input from here will be factored into that review.

Point number three, we at the Federal Reserve think it's part of our responsibility to focus on consumer literacy and financial education. That -- and what we are learning in these processes will help us provide direction for that effort.

And number four, that is also a responsibility of the Fed -- one of the responsibilities that we assume for ourselves is to look for opportunities for further research.

And so those are the four that will hopefully come from here.

In an environment like this, the appropriate use of financial products is a shared responsibility. Certainly the primary responsibility is for the consumer.

A consumer in a free society, in a free market, there's an underlying fundamental presumption that the consumer is responsible for his or her choices and actions. However, it is a shared responsibility, and the second part of that sharing is with the originator, the initiator of those mortgage products.

There is no question of what -- there's an extraordinary knowledge asymmetry, between the knowledge that an individual will have when they are taking, especially sometimes for the first time, a mortgage product and to try to evaluate them in the context of a wide range of products that are available.

I have said before -- and let me say it again because it brings it home. Some of you know my background is banking. I spent 16 years in the banking industry. I never was primarily a mortgage lender, but during those 16 years, I was involved in the closing of a lot of -- of a large number -- I'm thinking it's roughly a hundred -- mortgage loans that I was involved in the closing of.

And yet every time I went to a closing of my own loan, I felt somewhat at a disadvantage in terms of my understanding. So I can imagine what somebody that is approaching that experience for the first time must feel.

So there is that clear shared responsibility, the consumer and the lender.

There is a third group that broadly defined that has -- we are learning more all the time can make a real impact, and that's the community and consumer groups. Financial institutions, not intentionally but by their nature, I think do not get real close to the broad community, especially the low-mod and sometimes the minority communities.

The financial institutions don't have that immediate connection that some of the consumer groups do. And we found the consumer groups that have that access, that have that credibility can bring an education, can bring an understanding, but can also bring to the marketplace -- can help focus what some of those important issues are. And we've heard from some of those groups and we will continue to hear from some of those groups.

Fourth group is the regulators. We are not number one. We're not even number two. We shouldn't be. In a sense, we're the referees. And it is our responsibility to look at the extent to which -- first of all, it is our responsibility to implement the laws that congress gives us, and most of what we do is implementing laws that congress gives us.

But it's also our responsibility to look at the marketplace to see that the -- that the activity in the marketplace is consistent with the expectation of the existing laws and the risk taking and appropriate behavior of the institutions that we regulate.

So that's our opener. We have four people on the panel this morning. I think we will go in -- counterclockwise, Paul, starting with you.

So if each of you would introduce yourselves, your organization, and then give us a brief summary and then we will go -- we'll leave us plenty of time for questions.

So Paul.

MR. LEONARD: Thank you.

MR. OLSON: Anything else I missed? Anything else that we should have --

MS. BRAUNSTEIN: I don't think so.

MR. OLSON: We didn't sing "I Left My Heart in San Francisco," but we're planning to do that at 3:00 when we're getting ready to leave. It's a beautiful city. It is just -- it is just -- we're reminded when we come here what a great place this is.

Paul.

MR. LEONARD: Governor Olson, I hope you meant at 4:00, after the -- after the open mic period. Right?

MR. OLSON: That was -- that must have been Freudian on my part.

MR. LEONARD: Thank you for inviting me to testify here this morning. My name is Paul Leonard. I'm the California director of the Center for Responsible Lending.

The Center for Responsible Lending is a national nonprofit policy and research organization focusing on predatory lending policy and issues. The organization is based in Durham, North Carolina. We also have offices in Washington, D.C. and have recently opened our California office here in Oakland, California.

I want to say that these -- I think these hearings come at an opportune time, as the subprime mortgage market continues to grow and evolve at breakneck speed. Subprime lending totaled more than $600 billion in 2005, more than doubling in total size just since 2003. And adjustable rate ARMs, both -- and interest only ARMs and option varieties now account for well over half of the subprime market.

Having been called to testify at the last minute and replacing a panel member who got sick, and having limited time to prepare, what I thought I would do, which I think will be enlightening, was to walk through this rate sheet which we pulled -- I actually pulled off the web this morning. It's a rate sheet for a standard 2/28 ARM mortgage that's offered by the New Century Mortgage Corporation.

I've provided you all with copies. And I think that the rate sheet, if you'll bear with me quickly, sort of highlights a few of the central problems associated with adjustable rate and other nontraditional loans.

The left half of the page you'll see has a matrix for fully documented loans. The right half of the page has a matrix for stated income loans with you'll notice a 50 to 100 basis point premium for the -- for the option of having a stated income loan, which will speed up the loan processing period but has also been a source of rising abuse I think, at least from what I've heard in the community. The far right column you'll see lists a series of adjustments to rate that might apply to any loan.

These rate sheets are updated every day and provided to brokers who are out there working in the marketplace.

So I wanted to just highlight one example. Assume we have a B credit borrower with a FICO score between 600 and 620, borrowing with an 80 percent loan-to-value and full documentation. The PAR rate for this borrower, which I've highlighted, would be 7.65 percent.

If you look over on the right-hand side of the page, however, you can see that a broker can earn an additional two points, or $6,000, for that -- for closing that loan in a yield spread premium if they're able to sell the loan at 125 basis points above PAR. This would bring the initial rate for that loan in at 8.9 percent.

If our borrower is taking out a $300,000 mortgage, initial payments of PAR would be $2,130 per month. With a broker who is maximizing their yield spread received from the lender, the initial monthly payment would jump to about $2,400. In today's market, most subprime lenders are underwriting these loans only to cover the initial payment of the loan. So it would be for this $2,400.

There are two key issues I think that I wanted to highlight. First was the yield spread premiums and the second really important one is the payment shock component of these loans.

After two years -- the rates are fixed at these rates for the first two years and then are reset-based on a LIBOR index and the lender specified margin. Today LIBOR rates are 5.4 percent. And you can see in the left-hand column the margin for B credit borrowers is 6.7 percent. So the effective rate of two years would rise to 12.1 percent. In that case, it would be a $700 increase. A 30 percent increase in the monthly payment after just two years in the loan.

Now, not many families that I know of are going to be able to afford a 30 percent increase in their mortgage after two years, especially when the loan is underwritten only for the initial payment. If the rates rise by two percentage points, the payment shock will be -- the payment shock will be a 50 percent increase in their payment.

The result, many borrowers will be in mortgages that they may ultimately not be able to afford. In an appreciating market, they may be able to refinance but will clearly lose some equity in covering their closing costs. In a cooling market, we expect that there are going to be substantial -- substantial folks who fall into the foreclosure process.

This isn't just a hypothetical issue. These loans were the standard subprime mortgage in 2004 and 2005. And since that time, we've seen a 400 basis point increase in the interest rates.

MR. OLSON: Paul, can you just wrap up?

MR. LEONARD: Sure.

MR. OLSON: And then we'll move on.

MR. LEONARD: Sure. Let me offer a few suggestions.

MR. OLSON: No, not a few. Or else just give us the topics and then we'll come back to them.

MR. LEONARD: Recommendations for actions: Strengthening the guidance and making it mandatory and in using FDC Act authority to apply that, the same standards to non-depository lenders.

Second, encouraging congress to opt a suitability standard for borrowers to meet the needs in their -- in this increasingly complex marketplace which you just referred to.

And third, we need to fix the incentives that don't reward brokers and the system for increasing the rates that subprime borrowers face.

MR. OLSON: Paul, thank you very much.

Kevin, you're up next.

MR. STEIN: Thanks. Governor Olson, members of the Federal Reserve staff, I want to thank you for coming to San Francisco to hold these important hearings and for giving us this opportunity to comment.

My name is Kevin Stein. I'm the associate director of the California Reinvestment Coalition. We're a statewide advocacy coalition of over 240 nonprofits and public agencies that work to promote access to credit and fight predatory financial practices in underserved neighborhoods throughout California.

The main massage I want to convey today is that we're seeing big problems in the mortgage market in California, and we urge the Fed to act to protect home buyers and homeowners in the state.

We are hearing more and more atrocious stories of abuse. Many groups and individuals have contacted us in anticipation of these hearings, and I hope several of them will be able to come testify during the open mic session today so that you can hear directly from them.

Nontraditional loans are being sold aggressively in California, and this is contributing to the -- to the chaos that we're experiencing. Interest only option ARM and stated income loans are being sold to borrowers who cannot afford homeownership and who did not understand their loan terms.

With hundreds of billions of dollars in loans scheduled to reset in the next few years, we know that many will not be able to make their mortgage payments. As payments dramatically increase, these borrowers will have a difficult time refinancing into new home loans and those that -- those who could refinance will be facing steep prepayment penalties, which in California translates into thousands of dollars.

Stated income loans we feel are a recipe for abuse, where brokers often inflate incomes of unsuspecting borrowers.

Another problem we see is the persistence of loan pricing disparities. In a study that we did based on 2004 HMDA data, amongst many findings of disparity, we note that minority neighborhoods throughout the state were four times as likely to get higher cost home purchase loans. And we estimate that people of color in California are paying millions more per month as a result of higher cost mortgage loans. This dynamic obviously means that many families in the state are facing lost equity and have less resources to support their families.

We are already witnessing an increase in delinquency and foreclosure activity in the state as a result of nontraditional mortgage products. This is alarming as interest rates are expected to rise and as borrowers of nontraditional loans face looming rate increases and resets.

As far as solutions are concerned, we propose six that we hope the Fed would implement to mitigate some of these problems.

One, expand the HOEPA protections by including yield spread premiums and prepayment penalties in the points and fees calculations. We'd also urge that you lower the HOEPA threshold so that the rate trigger is set at six points above treasury and the points and fee trigger set at five percent. The existing thresholds are unreasonable given the high housing costs in California.

Secondly, we'd urge you to promote informed consumer choice by requiring key loan documents to be written in the same language as the language in which the negotiation is conducted. This is a big problem in California where contracts are often negotiated in one language but the loan documents are all in English and often with less favorable terms than the consumer understood.

We have a precedent in California Civil Code Section 1632 which we believe could be the foundation for a broader and more encompassing federal requirement.

Thirdly, we urge the expansion of HMDA reporting requirements so that HMDA can better help us identify discriminatory lending practices as is its stated purpose. And I know the governor has spoken to this issue.

Amongst other things, we'd urge the inclusion of credit score information, the age of the borrower, and, pertinent to this discussion, whether a loan is, in fact, a nontraditional loan.

Fourth, we urge the development of due diligence standards for the secondary market. We're currently conducting research on the secondary market for subprime securities in conjunction with Raphael Bostick, the director of the Master of the Real Estate Development Program at the University of Southern California.

To date, we've reviewed 99 subprime securitized issues from 2005, and we can see the prevalence of nontraditional loan products and other problematic loan terms. CRC believes the secondary market has no regard for whether it is financing predatory loans. Strengthening HOEPA will help and expand importance of liability, but broader standards are necessary.

Fifth, we urge the expansion of CRA obligations. The Federal Reserve in its analysis that accompanied the release of the 2004 HMDA data noted that there were pricing disparities that could not be fully explained, and at the same time noted that these disparities were lesser within banks' CRA assessment areas.

And we think that's an important finding. At the same time the banking regulators continue to hold on to an outdated and overly narrow definition of what constitutes a bank CRA assessment area.

MR. OLSON: We'll ask you to stop there and we'll -- those are important and we'll have -- we'll want to have a full discussion on each of those. But thank you.

Rick.

MR. LIEBER: Good morning. I'm Rick Lieber, EVP of IndyMac, responsible for managing our company's mortgage products. And I thank you for the opportunity to share our perspective on nontraditional mortgages. And I also thank the Mortgage Bankers Association for asking IndyMac to represent them on this very important subject.

For quick background, IndyMac is a $24 billion institution. That makes us the largest in Los Angeles, the ninth largest in the nation, and we're also the seventh largest mortgage originator in the country.

For the opening remarks, which are tied to five minutes, I'd like to make just three key points.

MR. OLSON: Some of them have gone to five minutes and 15 seconds.

MR. LIEBER: I get an extra ten?

MR. OLSON: I just took ten seconds of yours, so you can --

MR. LIEBER: Can I have 12 for that interruption?

First, we think the mortgage products have actually typically lagged the industry in innovation and some of the features and option ARMs that have existed in other consumer products are actually better served in a mortgage product.

Second key point, we think that most mortgage originators originate nontraditional mortgage loans, including option ARMs, in a safe manner, a sound manner that properly address layered risk. We think that solid underwriting has brought about very prudent loan products that have predictable performance, and we think this is born out in the secondary market.

Thirdly, third point, we think some of the recent innovations in option ARMs that have been offered by both IndyMac and other major lenders actually further advance the soundness of the products and their appropriateness for consumers.

On the first point, option ARMs provide borrowers with one very key benefit and that is flexibility in payments. And this allows borrowers who have a reduction in income or a sudden expense to be able to handle their mortgage payments with much lower risk of default and, therefore, much higher odds of not having any risk of losing their homes.

And this is a feature of flexibility that's been with -- that consumers have had access to for several years with different consumer loan products.

We actually think it's more prudent for a borrower to access these additional borrowings against an asset that actually rises in value over time rather than assets that don't have an ongoing value, such as a meal or a vacation that might be on a credit card.

An additional component, interest on a mortgage is deductible, whereas interest on some of the other consumer credit generally is not.

The second key point, IndyMac and we believe actually most national lenders do originate nontraditional mortgages in a prudent manner. And a key to this is lending with guidelines that guard against the potential for layered risk and restrict the lending to borrowers who are, in fact, in a position to handle that flexibility. An option ARM, for instance, we only lend and most national lenders only lend to prime quality borrowers who have a history of responsible use of credit.

And additionally, loan-to-value ratios are typically five percent lower on option ARMs than other products. In fact, the average loan-to-value on an option ARM is approximately 70 percent, and that would mean, with at least our standard product, that the loan balance could grow only to the point where your advance against value is 77 percent, which still leaves a significant amount of equity.

And if you factor in just a reasonable amount of home value appreciation, say three percent, over a three-year period, which is the average life of a mortgage loan, there actually is no loss of net equity.

The concept of addressing risk of one loan feature being compensated with other guidelines applies to all of our core products, the alternative A products. And in a recent exam by the regulators on the regular scheduled exam, they agreed with that premise and concluded that, in fact, our reduced documentation loans, primarily stated income loans, were, in fact, less risky than full documentation loans as a result of those compensating factors.

We and I think most industry participants also work very hard to make sure that borrowers understand the features of the loans that they're taking out. We have a two-page option ARM disclosure that in very plain English outlines the features of the loans and we believe very clearly illustrates the risk of a rising principal balance and the risk for a potential significant increase in minimum payment.

This long history has proved to create a very strong secondary market, which I believe supports the premise that the products are predictable and reasonable.

And then last point on new products, we think recent innovations with option ARMs have advanced the benefit to consumers. For example, we recently released a flex pay product that allows for fixed rate for up to five to seven years, in addition to continuing to provide the payment flexibility. We think -- we've also added features that reduces the potential increase in the payment and in the -- an example, that can reduce the payment by up to a third.

The conclusion that I would like to make is that we should make sure as we add different components to regulation and different restrictions on innovative products we don't forget the fact that many of this innovation does, in fact, bring about additional benefits to the consumers and we don't overact in a way that can stifle that benefit in the long run.

I thank you again for the opportunity and I look forward to questions.

MR. OLSON: My goodness, he didn't even need the last 12 seconds. You finished right on time.

Well, we clearly are seeing the -- from the first three where the focus will be on the advantages versus the risks inherent in these products.

We'll hear from Bruce and then we'll go to some questions.

Bruce Fuller.

MR. FULLER: Thank you, Governor Olson. I'm Bruce Fuller. I work in the financial planning department for World Savings.

World Savings is one of the largest financial institutions in the nation with over $125 billion in assets. We operate savings branches in ten states and originate residential mortgages, almost entirely option ARMs, in 39 states.

We have been making adjustable rate mortgages for 25 years and have never had a default because of loan structure.

And the reason is very simple. We have very, very careful underwriting and our meticulous ongoing service after origination.

Our overall loss rate, even taking into account the deep recession in Southern California in the early '90's, in which we saw rapid price appreciation, followed by the implosion of the defense industry, high unemployment, declines in property values up to 20 percent, has averaged less than five basis points since 1981.

So now some background on adjustables having talked about us a little bit. For some time before ARMs were originated in 1981, we and other major financial institutions in California and throughout the country, together with trade groups and others, studied the various forms of adjustables that were made elsewhere in the world. The research took us to Great Britain and other parts of Europe where ARMs had been used for quite a long period of time.

At the end of the day, when we were deciding which type of adjustable to choose, there were basically two choices, the option ARM that provides protection against payment shock by features such as annual payment caps and the borrower's ability to defer interest or what we term the no neg ARM that does not allow deferred interest and then is, therefore, more likely to result in payment shock for the borrower.

Our experience I think proves the case for the option ARM. Contrary to some beliefs, the option ARM loan was really never offered only to high-income, wealthy professionals. We and other lenders have been offering the option ARM since 1981 to the exact same types of borrowers to whom we and others are offering fixed rate mortgages during the same period of time.

Over that period we funded over a million and a half option ARMs, with an average loan size of 175,000. And our company's delinquency rates are well below industry averages, including those for institutions who offer only fixed rate loans.

And again, indeed, we have never identified a single delinquent loan in our portfolio, much less a foreclosure or loss due to the structure of our option ARM product. Our option ARM because it's designed, priced, and underwritten reasonably is successful by definition.

Now, what's changed recently? Obviously in recent years, the option ARM is being offered by a much wider spectrum of lenders, facilitated by the new securitization market, technology developments, implementation of automated underwriting standards, appraisal monitors, and credit scoring.

While our version of the option ARM has been around a long period of time, these new technologies may not be fully tested, especially with alternative mortgages. And I'm sure we'll get into that more soon.

We're clearly not here to defend all the practices in the marketplace. We have long supported a regulatory regime that encourages lenders to provide full and fair disclosure to customers and prudently manage their lending practices. And that includes the following:

Avoiding lending practices that can be predatory or abusive, providing consumers with clear and timely disclosures, maintaining strong underwriting appraisal compliance and risk management functions, avoiding diluting underwriting standards just to get volume, actively managing, monitoring, and controlling risks of default, and regularly and continually interacting with customers so that they understand what they have and how they should act.

Of course, these sound practices really are relevant to any loan a bank may offer, and we certainly support the reemphasis of these principals in the pending interagency guidance and the marketplace.

As one side note, I would also note that other forms of equity that people -- ways people use equity such as getting fixed rate mortgages and piling equity lines of credit on top of it have some of the same risks as nontraditional products we're discussing with maybe not all of the protections.

In conclusion, we applaud the agency for issuing the close guidance and as in our letter we think the guidance needs to more fully address certain emergent practices that may put customers in jeopardy, particularly loans that are offered with deep initial payment discounts.

We do not support overly prescriptive underwriting rules or mind-numbing stacks of disclosures that no one would ever want to read or need to read or will ever read, but we look forward to working with the Federal Reserve and other agencies to develop appropriate consumer protections.

Thank you.

MR. OLSON: We have 200 people on our staff that would read every single one of those mind-numbing statistics.

MR. FULLER: Unfortunately, Herb and the rest of us would, too. But I'm not sure the consumers will; that's what I'm worried about.

MR. OLSON: Thank you. Thank each of you.

Let me go back and ask a couple of follow-up questions. And I'm sure my other people on our panel would want to do the same.

Paul, the rate sheet that you handed out would show -- obviously the people would want to move into the upper left-hand side I would think of -- in each category, and would certainly rather be on the left-hand side of the page than the right-hand side of the page.

Yet as we look at -- if we look at a distribution where we can get access to distributions of the nontraditional product, particularly as they're sold into the secondary market, we see in many cases -- I don't say that we've seen every, but in a number of cases, we see that the interest only or the low doc loans tend to correlate with higher credit scores and either low or the lowest of the loan-to-value ratios, which would suggest that there's a significant element of consumer choice in that as opposed to steering.

And yet, as I listened to you, it sounds as if you are suggesting that the differences in price may work exclusively disadvantageously to the less informed borrower.

Would you just clarify that?

MR. LEONARD: Well, I think both can be true actually. I mean, I think it is, on the one hand, true that more informed borrowers are making savvy decisions about managing their own finances, selecting the products that are best for them.

I think our concerns are really about the less informed borrowers, folks who don't really understand the complexities of the process, and particularly in the role of brokers in selling these products, that the products may not meet the best needs of the least informed borrowers, that they may be least informed and least able to negotiate products that might be available but that they are not aware of, and that there are -- that these can be presented in ways that appear to be advantageous to the borrowers but, in fact, may not represent their best financial interests.

MR. OLSON: You -- I interrupted you as you were about to make some suggestions. You talked about using the unfair and deceptive authority. You talked about suitability. You talked about changing of incentives to brokers. Were there others that you -- other suggestions you --

MR. LEONARD: No, those were the three primary ones.

MR. OLSON: Those were the three. I suspect we'll have a chance to get back to those.

MR. LEONARD: Okay. Good.

MR. OLSON: I don't know if the FTC has held a similar hearing. That's where we -- a lot of the activity that takes place is an -- a lot of the mortgage activities and institutions that are primarily regulated, not exclusively but by the FTC.

Kevin --

MR. LEONARD: Just as a point of clarification, FTC did host a forum in late May on these products.

MR. OLSON: They did. Okay. Good.

MR. LEONARD: They did, in Washington I believe.

MR. OLSON: Okay. Kevin, let's come back to one point that you -- as you pointed out, we had some discussion when I testified at -- on Monday on this issue about expanding HMDA reporting. And let me state my concern. And then I would be interested -- or our concern. And then would be interested in your response.

I think as everybody here knows, HMDA -- the HMDA reportable data is -- has been the location of the property, the dollar amount of the loan, the date of the loan -- actually not the date of the loan. It includes income of the borrower and now it is expanded also -- and the race of the borrower. Now expanded to include loan pricing.

In research that we have done, the Fed has done, 90 percent of the mortgages issued are unique, which is to say it's the only loan of that dollar amount made in that geo-code area, probably a census tract, that year, by that institution. So it would be relatively easy to through cross-references with public records find out the name of the person.

If we were to add other personal data to it, there is an enormous privacy issue that is raised, number one. Number two, credit scores are a purchase product and increasingly financial institutions are using proprietary credit scores. So there is an apples and oranges issue there.

But I -- and then even so you -- in our experience, in order to make a decision on whether or not a loan is being made in equal terms, you need probably as many as 30 data points. And you can get those only from a credit file. You cannot get them from HMDA data. You cannot even get them from a downloading typically of the front end system of a mortgage originator.

So I know that you folks have thought this through, the trade-off between what information you put in the public domain and the important privacy implications.

MR. STEIN: Okay. Thank you for the question. And if I may, I just wanted to add a bit to the prior question just quickly.

This idea that we have savvy consumers that are choosing these new products, just three things I'd say. One is you may know the Consumer Federation of America did a study recently where they called into question whether the nontraditional products are really going to folks with higher incomes and higher credit scores.

And secondly, we've seen such an explosion of these products -- and I don't know if -- I mean, are we to assume that we just have an exposition of more informed consumers that are seeing the need for this product?

I think the product is being pushed more heavily, and that I think is -- and to the third point, we're seeing anecdotally a lot more evidence of people who have these loan products and have no idea what they're getting. So we see a lot of -- we see a big -- kind of a mess in this market.

On the point about HMDA, I appreciate the concerns about privacy. And I guess I would say just generally that it's interesting and a bit frustrating because the Fed has been good about requiring more data to be included, and while we keep getting more and more data, in a way what we hear from the industry is that the data is somehow less and less meaningful, which is -- which doesn't make sense.

If we have a HMDA statute and a reporting requirement and the idea is to help us identify discrimination, then we should make sure that the HMDA regulations and reporting requirements get us to that paint.

If there are -- and I think the folks at the Fed are probably a lot smarter about this than I would be. But if there is no way to require -- to require more data and maintain the privacy of consumers, perhaps there's a way to require the data to be reported and to have -- and not necessarily have all of it be made public.

MR. OLSON: That's exactly -- that's exactly what happens now. And that's exactly what we examined for. And so -- but what the -- the difference is it happens in the examination process but not in the information that's publicly available.

MR. STEIN: Well, I note that in the analysis that was put out with the release of the 2004 HMDA data, maybe there's some analogy that the researchers did look at the what we think of as the other CRC data, which is that private database. And we had some questions about the validity of doing that, to look at a private database to try to overlay some of the additional information that's not available through HMDA.

And perhaps if there was public reporting -- if there was a reporting requirement that applied to all financial institutions where the government was the receiver of the information and we could have government researchers looking at that, at that information, that would I think be a better -- a better way to go than what we saw in 2004.

MR. OLSON: Rick, the -- talk about these experiences -- these issues again. And the next two are both lenders and it will be very interesting. How -- you folks as lenders are clearly aware of these issues. The way -- the additional complexity puts an extra burden on a responsible lender.

Let's get the fundamental issue on the table. There's some bad actors out there. There's no question about that. We didn't invite any of them to speak here.

MR. LIEBER: They probably wouldn't have shown up.

MR. OLSON: But there are.

So in your case, you look at that information asymmetry if you will. And it starts either -- it starts either when you're working with -- through brokers if you're doing so or when people come in the door and then -- and then let's -- at some point let's compare your sale, for example, to what we're hearing about the -- you must be picking up anecdotally what's happening with the push marketers who are operating in quite a different way. So would be interested in hearing your perspective.

MR. LIEBER: Well, one of the key things that I think works to the benefit of IndyMac for the consumer is that we only have one origination process that handles both non-prime, prime, and our alternative products. So that a loan that comes to us goes through actually our automated engine and the engine determines the best product and all products available to that consumer. So I think that's a major benefit for us.

MR. OLSON: Say that again because I think that that's -- it sounds like you're -- that you are -- that your process automatically or in an automated fashion generates that analysis.

MR. LIEBER: Correct.

MR. OLSON: So describe the -- describe it again.

MR. LIEBER: Sure. It's an automated engine. And whoever our customer is, whether that would be a consumer directly or a mortgage banker or broker, will submit the loan request. We'll actually pull the credit report and, based on that information, give the borrower the best product and the best pricing available.

Or stated another way, you can't say, "Hey, I want a non-prime price because I think, as the broker, I will get more money as a result of that." So if a borrower has prime characteristics, they will get a prime loan through our system. And I think that's a key advantage that we've got in our methodology.

And we certainly are in the mortgage business for the long-term, as is World and other major players, and we don't want to make loans to borrowers that they won't have the -- that won't serve their best interests. But I agree with you there are some bad actors in the industry that are causing problems for everybody.

MR. OLSON: Bruce, you -- World is known as a portfolio lender.

MR. FULLER: Right.

MR. OLSON: Not -- are you exclusively still a --

MR. FULLER: Yeah, 99 percent.

MR. OLSON: Okay. And for those -- what that means in broader terms is that when you -- when you make a loan, you take full responsibility for it for as long as that loan is in your portfolio.

MR. FULLER: Right.

MR. OLSON: So you also said that you have been doing option ARMs, if I understand, since 1981?

MR. FULLER: Right.

MR. OLSON: One of the -- one of the criteria that we use -- that the regulators use to evaluate credit risk exposure is we ask them to test it through the cycle. What that would mean would be through a cycle, typically an economic downturn through the full cycle and through an interest rate cycle.

FULLER: Right.

MR. OLSON: Well, you -- since 1981 you have been through several --

MR. FULLER: Right.

MR. OLSON: -- cycles. So could you describe what your experience is through interest rate upturns over that period of time, recognizing, I'm sure, that you are dealing with much smaller numbers in prior cycles.

MR. FULLER: Right. Sure. Thank you.

So on your first point, as far as a portfolio lender, you're right. One of the major differences with us is we basically obviously have a large skin in the game.

So it's -- I think a lot of what we hear or some of what we hear the problem is is essentially someone trying to put someone in a loan that the goal is that they can't make the payment.

If we do that or any portfolio lender does that, we lose also. So obviously we have to be in a situation where we -- it works for the borrower before it works for us. And we spend a lot of time making sure that that happens.

As far as the cycles go, you're right that we have been through -- as a portfolio lender doing it for 25 years, we've been through a number of cycles. And basically what we found is if you structure the product correctly -- and we can have discussions of what we think that is -- what happens is the product works so that when rates go up, the person's payment goes up some but they're allowed to defer some interest to essentially not have a payment shock, to be able to ride it out.

And then generally because there are cycles, interest rates move back down and that's when they pay the loan back down. And obviously individual consumers choose different methods. Some will pay more at other times than others.

But generally what we're looking for is a product that we know there's cycles and it will work through the cycles and we won't have a product where there is short periods of time, like you're referring to, Paul, where, hey, over a two-year period, if it's going to blow up, that doesn't work for someone.

You have to have a product that's going to work for the customer over a long period of time when rates have gone up and down. And that's the way our product has worked in both rising and falling interest rate environments in the past.

MR. OLSON: Then what -- my father, I remember the first time I -- second time I took out a mortgage loan, he reminded me that I was -- any increase in equity through appreciation of the house was speculation, that equity in a house came through reduction of principal.

What do you find -- what happens to reduction of principal for the interest only product or the all -- the alternative payment products relative to the -- to the fixed amortization products?

MR. FULLER: Right.

MR. OLSON: Rick, I'd be interested in your comment. Either -- both of you, please. Not at the same time.

MR. LIEBER: Might be challenging.

I think the first point, Governor, is the average loan is actually outstanding today for only about three years. And borrowers refinance for a variety of reasons, other than they move or they refinance for other features that they want to change in the loan. It could be lower interest rate, it could be other payment flexibility.

So the point of that is on a conventional mortgage loan, the amount of amortization that is seen in its normal life is very modest, is on -- on a typical three-year loan, it actually works out to be a little less than three percent at today's interest rates. So the equity appreciation through amortization is really quite modest in the average loan life today.

And I think we -- we all acknowledge that in the history of the United States, or certainly the recent history, home prices have gone up dramatically. But even if you look back at a much longer period of time, home prices have had a nice consistent growth that probably exceeds three percent.

So the equity that would be gained in home price appreciation would typically exceed the equity gained through the amortization.

MR. FULLER: I would just add to that I think that what we've seen recently at least is that people -- consumers want to use their equity and what they're looking for is what's the way they're going to use it. Some people use it through their equity line of credit, some people use it through deferred interest mortgage. And so it's kind of how they want to use it.

Now, what we also see is every borrower is individual obviously. We have some borrowers who -- we have programs that pay down your equity even faster than normal and some borrowers choose those or choose more -- to make more than the minimum payment. Other borrowers want to use their equity, whether it's through an equity line of credit or through a mortgage.

And I think what we try to emphasize is the availability to do that but also a product structure with a payment discount that's not too deep that if someone does pay the minimum, they're still okay, that that buildup won't be too fast to where they're going to run into a payment shock.

MR. OLSON: Jack, Sandy, or Leonard, questions?

MS. BRAUNSTEIN: Yeah, I have a couple questions.

One of the things, you know, that we've heard over and over again about these products and that we see are the complexity of the products. And I know, you know, even looking at them myself, it gets rather daunting and confusing because of constant change in terms and payments and interest rates can rise and then if you're interest only you might end up with negative am on some of these products.

So I was wondering what do you do -- okay. To add on to this, which is pointing a finger at ourselves, frankly our TILA disclosures are not the most enlightening products in the world for a consumer. So besides the TILA disclosures that I'm sure you're giving regularly to be in compliance with the law, what do you do to make sure consumers that are getting these really understand the implications of these products, you know, where their payments could go, the kind of payment shock issues and other things? What do you do? Do you have something supplemental to that?

And then I would ask -- and I'm asking the lenders that for their products. But then I would ask Kevin and Paul what they're seeing from consumers.

MR. LIEBER: One of the things we've done is develop what we think is a very solid disclosure, particularly for option ARMs.

And we first acknowledge mortgages can be quite complex. The basic concept is simple, somebody is lending money in return for somebody paying it back over a period of time with an interest rate. That's the very simple part.

But I acknowledge it gets very complex, very quickly, and there are lots of features. Most of those features -- I think actually all the features are designed with the best intent to help consumers gain flexibility and have more opportunity. But they are complex.

In the case of option ARMs, one of the potentially more complex products, we've developed what we think is a very solid, plain English disclosure that goes through the key terms of the product and makes it very clear at the outset that in -- in the case of an option ARM, the reason a borrower would take that product is solely for the payment flexibility.

And then make it very clear that your loan balance can rise, and will rise, if you make that minimum payment, and that at the end of the loan, certain loan terms, if you reach the maximum of the amount the balance is allowed to increase or certain time-based periods, you will have an increase in the payment.

So we work very hard to make that clear. We've gone beyond just the legalese or the simple -- not simple but the requirements regulated so that the borrower can be educated. And we've tried to make it simple and --

MS. BRAUNSTEIN: Is this something you give to them in addition to the required TILA disclosures?

MR. LIEBER: We do. We give it to them after -- soon after the application process.

MS. BRAUNSTEIN: After their application?

MR. LIEBER: Correct. Before they close the loan. And before they're at the closing table as well where it may be too late.

MR. FULLER: So we have what we referred to as deferred interest disclosure, which is similar to what Rick talked about, where we're laying out what the terms are, what kind of deferred interest they should have and things like that. And we follow through with that with the borrower also and have gone through those steps.

Now, obviously, as we've discussed, I think another disclosure goes so far -- another key point is is the lender reputable? Is the product good? You know, is it something we're going to make sure works for the borrower?

You know, so we do a strong job in trying to make sure the disclosures are accurate and are clear and concise and highlighted and they know the key points, making sure they don't get buried in the paper.

But I think, in general, in the market we also have to try and figure out for lenders who may not want to do that how are we going to deal with this?

MR. LEONARD: I think I have four things on this one. One is -- I mean, I would go back and not -- I mean, I think that the great -- perfect disclosures would be great and are never going to happen, number one.

Number two, I think it's really about the role of regulators in determining reasonable and responsible underwriting standards, which I know you are taking a look at now, and applying them in a rigorous way across the entire lending industry, through FDC authority or -- and we would hope that you would issue mandatory regulations rather than voluntary guidance on these matters, or in addition to voluntary guidance I should say.

Third, there has to be some establishment of real fiduciary responsibility of brokers, that brokers are right now not accountable enough in this process. And we've seen it time and time again in a number of instances across the country where -- particularly an example recently in Montgomery county of the discussion about implementation of a local fair lending law that was to take effect and where we saw that retail lenders were staying in -- were staying in Montgomery county at imposition of this new fair lending law, but lenders were pulling out -- who were relying on their brokers were pulling out of Montgomery county.

So the brokers are not really accountable in this process. And they're the ones who are really sort of at the front lines of what, Governor, you referred to as this knowledge asymmetry. And I think unless there's a clear fiduciary responsibility that's established that there will always be knowledge asymmetries.

MR. OLSON: Let's stick with that. But they're also at the front edge of the push marketing.

MR. LEONARD: Uh-huh.

MR. OLSON: And there is a limit as -- there are limits to regulations, in particular, or laws that can catch up with a rapidly moving marketplace.

MR. LEONARD: Yes.

MR. OLSON: And especially when you see overwhelmingly societal value -- I would -- if you care to challenge this presumption you can -- overwhelmingly societal value in more money being made available to more borrowers.

MR. LEONARD: Correct.

MR. OLSON: So number one, how -- what are you folks doing also to help bridge that information gap or to alert people to some of the risks of being in that marketplace in the front end?

MR. LEONARD: I think two other points. Suitability standard to make sure that there is some screen that applies, that is in federal law that applies, to make sure that -- as in the securities industry -- that a product is reasonably advantageous to the borrower. That would help.

And finally, I can imagine some kind of a third-party mechanism and structure being put in place that borrowers can reasonably turn to to sort of -- who have more informed -- more knowledge and have no skin in the game, as it were, to turn to -- to get assistance and guidance through the process.

And right now we have a -- we have a federal housing counseling program under-funded, not utilized, certainly not utilized for the vast proportion of loans that are made, and I could imagine the creation of some substantial expansion, public interest campaign, 1-800 numbers for people to know that they can call and review the characteristics of a loan with somebody who is seasoned and understands the dynamics of the mortgage marketplace and can give them an independent third-party review as to whether that loan is a suitable loan for them.

MR. CHANIN: Paul, let me follow up on that and then we'll let you get off the hot seat if you will.

And the suitability issue or fiduciary obligation, et cetera, is something that has come up at some of the other hearings as well. And my question is when ARMs came out I guess a couple of decades ago, there was certainly concern. The agencies adopted a number of regulations, disclosures to address those. There was great concern on the part of consumer groups. There was fear the consumers would not understand these.

But now it seems that with these products, there has been a shift away from trying to, if you will, educate consumers, trying to improve disclosures, and saying that there's something, at least implicitly, something fundamentally different about these, so that people have suggested imposing a suitability requirement.

And is there a fundamentally different market in place now than, for example, a decade ago or why -- why is there that push now to --

MR. LEONARD: Well, I think that what you've seen in the mortgage market is a much greater awareness of predatory lending as a systemic problem that has played itself out. The large wave of state laws has only happened since the late 1990's. In North Carolina, home of my organization, we were involved in passing that law in 1999.

I think the second thing that's important to point out is by and large, and certainly here in California, the introduction of new and innovative products into a marketplace that has not been tested through the cycle. We've been in a largely up-cycle over the last -- over the entire period in which most of these products have emerged.

So I think there is some differences in the marketplace. And I think the pace -- the pace and the introduction of these products, the increasing aggressive and corporate as larger national chains who are -- institutions who are involved in this, more aggressive push marketing systemically, I think all of those things raise the stakes for borrowers who are least able to and least well-informed in the mortgage marketplace.

MR. RICHARDS: Rick, you mentioned relatively short life of a mortgage loan. I wanted to ask the panel at large about prepayment penalties, how frequently they're imposed, how complex they may be, whether you see them more often with certain types of loans, and what risks might be involved.

MR. LEONARD: I'll take that one.

MR. LIEBER: All right, Paul.

MR. LEONARD: We have worked very hard to substantially limit or eliminate prepayment penalties for subprime mortgages. We're particularly concerned in this context where there isn't asymmetry between the payment reset date and where the prepayment penalties will extend beyond the initial prepayment reset date, where borrowers are trapped either way, that is, they -- if they refinance before the reset date, they're having to pay a substantial prepayment penalty. And if they -- otherwise they're faced -- facing a payment shock that they can't really afford. So they're losing out either way.

They are extremely prevalent particularly here in California where we see roughly 70 percent of the subprime market having prepayment penalties. They're particularly problematic here in California because they are tied -- they're tied to the interest rate of the loan. And they're usually six months -- six-month penalty on 80 percent of the unpaid balance.

The correlation with the interest rate means that the borrowers who are paying the highest rates also pay the highest penalties. And we think that is -- that is really problematic.

MR. LIEBER: And we certainly believe prepayment penalties have to be reasonable and fair, and we're certainly very much against a penalty that would go longer than the period of time as the fixed rate period.

I think there's also just a reality here in that -- as a practical matter, there is no free lunch. A lender makes a commitment to lend money to somebody for 30 years, for a full 30 years. The borrower has the choice of paying it back either faster or slower. It happens to be the average is three.

And to get some of the features that exist in a product such as a no-cost mortgage so that the lender will actually pay for much of the cost to get that low mortgage originated, appraisal fees, closing fees, doc fees, et cetera, the only way to be able to do that economically is say, "Tell me I will have the loan for at least two or three years."

And if we eliminated prepayment penalties, the practical matter is interest rates would have to go up to cover the fact that -- or interest rates would go up or the elimination of the no-cost mortgage would occur, so the borrower would have to come up with the costs at the outset.

MR. OLSON: There's secondary market implication to the prepayment also -- there's -- through dynamic hedging, if you're hedging against a prepayment risk, that has a pricing implication to it.

Now, does the -- I was -- my wife has an MBA, so she's not -- not an uninformed consumer. But I was trying to tell her the link between a prepayment penalty and pricing. And I was unable to do it. And I know a little bit about dynamic hedging, but it was -- it was very difficult for me to try to explain why that could be -- why that could impact pricing. But it does, does it not?

And most of the -- isn't the significant amount of the subprime product actually going into the secondary market now? Does anybody know the answer to that?

MR. LIEBER: I believe the vast majority.

I'd like to make a point on that in general. We do actually sell most of our loans into the secondary market. And I do certainly respect portfolio lenders. But it really means for us is that we have customers on both sides. We have customers in our borrowers and we also have customers in the people we sell the loans to.

So it's very critical for us that those loans perform to the expectations of the people we sell them to. And although we may not have direct skin in the game on that loan today, we clearly have skin in the game that the loans that we sell to those investors perform over the long-term.

And performance comes in two key measures, the credit performance so that the borrowers -- we put borrowers into loans where they can make the payments. But the other piece of it is that the loan stays outstanding for the length of time expected.

And if I could try to make it very simple -- and maybe I'll oversimplify -- most people who lend money lend money at variable rates. So they borrow their money. Say, "Hey, if I'm borrowing money to buy a loan, my interest rate is going to go up and down every day. But I've got a borrower on the other side who I've made a commitment to that their interest rate won't go up for two years, three years, ten years, or 30 years."

So giving that disparity costs money. And the way to cover that cost is to say, "Hey, guarantee me the loan will be outstanding for two or three years so I can enter into those transactions for hedging, et cetera, so that I can deal with the mismatch between borrowing on a variable rate and lending on a fixed rate."

Now, I either made that very simple or overly complex or made no point at all.

MR. STEIN: Well, I think I understand that and can appreciate that, but I also think that this is part of the problem, that -- as you were talking about with World, and I think as you expressed it, Governor, so you have -- you have concern for what those loans look like because you're holding them. You have to take responsibility for them.

With the fact that the vast majority of subprime loans are sold to the secondary market, there's a diminution of the sense of responsibility. And, in fact, we think all of the incentives are kind of running the wrong way, running towards the investor and away from the consumer on all levels.

I mean, we were talking about disclosure before.

It's not in the interest of those on the ground who are selling the loans to make sure people completely understand what they're looking at. And that's why we urge yield spread premiums to be included in the HOEPA trigger. We talked about prepayment penalties. We urge them to be included in the HOEPA trigger.

I mean, I don't know how anyone could say seriously that consumers are bargaining for the prepayment penalties so that subprime borrowers to a much, much greater degree, 70, maybe 80 percent of the subprime loans, have prepayment penalties. In the prime market it's a single digit percentage. I'm not sure exactly what it is. There's a huge disparity. People are not bargaining for this.

We conducted a study a few years ago where we actually talked to over a hundred consumers of subprime loans in California, and for a significant number of them, they had this dynamic that Paul described, which I think is significant, where you had the prepayment penalty extending beyond the initial interest rate of the loan.

And sounds like three of -- three of us who have spoken to this agree that that's a problem.

MR. FULLER: Four.

MR. STEIN: So that's -- meanwhile, we believe most lenders don't agree. So I guess I'm glad that we're sitting -- you did get the good guys. So thank you.

We think that's a big problem, that the initial interest rate and the prepayment penalty must be tied together, especially given the fact that people do not understand these new -- these newer nontraditional loans that are being pushed.

And three years it's expected that they're going to roll over. WE see these new 50-year products. And it all kind of predicated on the idea that everyone knows people are in trouble and they're going to have to refinance. And how many of those folks are going to have prepayment penalties? And in our study nobody understood that their prepayment penalty extended beyond the initial interest rate of the loan. And that's why we think yield spread premiums, prepayment penalties need to be included.

And the point about counseling -- so I had six recommendations. I got through five. I thought we had six minutes to present. But six is we need to support home loan counselors, who, as you said in your opening remarks, Governor, are part of this -- are part of the dynamic and are part of the solution and really can help people understand, especially --

I mean, we support the idea of more disclosure, more information, but we also think we need to have regulation. And if there's some way we could tie counseling to HOEPA and to these problematic questionable nontraditional products, we think that would go a long way towards people understanding and less abuse occurring.

MR. LEONARD: I'm going to just make -- one more point about prepayment penalties. My organization has done a substantial amount of research on prepayment penalties, one of which we used proprietary database to look at and see that, in fact, when you look out across a huge scale of subprime loans, there is not the interest rate disparity that you would expect to see.

I mean, again, the argument is you're getting an interest rate benefit from having a prepayment penalty. And when we did a carefully controlled regression analysis to look at that question, we did not see -- find the results that you would expect to see, which is that there would be a substantial lower interest rates for folks who had -- who had taken out prepayment penalties on their loans.

That and the fact that we've also looked at the differing effects of state laws and found that state laws, strong state laws, have worked very effectively to eliminate the penalties that -- eliminate the kinds of predatory products that we're concerned about and which they were intended to do, without having any deleterious effect in terms of the availability of credit or in terms of rate -- of substantial rate impacts.

And that includes a number of states that have substantially scaled back and limited the availability of prepayment penalties on subprime loans.

MR. LIEBER: One point. I'd be very curious to see the analysis, Paul. And hopefully you can share it.

MR. LEONARD: Absolutely.

MR. LIEBER: My guess is that you'll find an analysis and certainly what we've seen is prepayment penalties aren't impacting interest rate as much as they are impacting the cost of closing the loan, so that you get the prepayment penalty that says I will get the lender, whether it's us directly or World directly or a securities investor, we'll get that interest rate for three years, or expect to. Then, in exchange, the borrower doesn't have to then pay many of the costs up front that can be several thousand dollars for the loan. So I would say the trade-off is most likely going to show up in cost to close the loan rather than the direct interest rate.

MR. CHANIN: Following Kevin, I want to talk a little bit about disclosures. My sense is you'd go through Dante's inferno and you'd have one disclosure, abandon hope all ye who enter here. Or my wife works for a spy museum and has a hat that says "trust no one." Either of those would work.

But I guess my question is -- and you can break it up for purchase money or refinancings if it makes sense. But we're going to begin reviewing the truth in lending Regulation Z disclosures presumably next year and really step back and take a look at all the disclosures, the ARMs brochure, et cetera. Is there simply -- are these products too complex to describe them to consumers?

I mean, they're out there and consumers are making choices, for better or worse, on these. And an integral part of this is consumers, you know, decide one way or the other what to get. I mean, is there no real role for disclosures or --

MR. STEIN: I think there's certainly a role for disclosures. And to the extent they can be simplified as it sounds like the panelists are trying to do, that's important. At the same time I think we have to appreciate the limitations of disclosure.

And the Governor noted -- and I believe that there's virtually nobody that completely understands their home loan documents and the home loan process. And what determines how much trouble you get into is really more a function of who is on the other side of the closing table from you.

And for most folks it doesn't -- it's not a problem that they don't understand everything or they haven't read the disclosures, which many people don't, because they're dealing with a reputable lender.

But unfortunately, we think in California and other places, if you live in the certain neighborhoods, you're more likely to be dealt with someone who is not reputable where you're going to suffer for not knowing.

And it's frustrating for people then to use disclosure and consumer education as kind of a sword to say, you know, it's your fault because you didn't do what nobody does, fully appreciate what your loans are.

So having said that -- still some people read the disclosures. Everyone should read them. To simplify them is important. I certainly wouldn't urge the reduction in disclosure.

And to follow up on an earlier point, in California, and perhaps in other places, English is not the language spoken by everyone. It's not the main language. And certainly when the contract is negotiated in another language, we think it's very important that disclosures like TILA, like the promissory note, like the HUD1 and the GFB, it be required that those be required in the language of the negotiation.

And then again, I think it kind of circles back to counseling as being the last stop gap measure to make sure people understand what they're getting, especially if these are kind of questionable, problematic loans.

MR. LEONARD: I have to admit I'm not the disclosure expert in our organization. I will also say I was struck by the Ameriquest settlement with the 49 attorneys general. And in reading that settlement, I was struck at the need for the attorneys general to have to specify in a settlement at this level plain language recitation, literally scripted recitations between representatives of the company and the borrowers about what the terms of the loan were, whether or not there was a prepayment.

I mean, it was quite striking to me that what I would consider to be an absolute bare-bones necessity is something that had to be included and specified in an attorneys general settlement with at the time the largest subprime lender in the country.

MS. BRAUNSTEIN: To follow up for a second on the issue of housing counseling, we talked about this a little bit in the Chicago hearing with people, but I'd like to hear your -- all your views on this.

You know, it's -- that's been a burning issue for a number of years. And even going back six years ago when we first did -- when we did the last set of HOEPA hearings it came up. And from time to time people would raise to us that they thought one of the things that we should have required for HOEPA loans and when we changed our regulations was the requirement that people have housing counseling before entering one of these products.

And I'd just like to get some of your views on this.

I hear, you know, about strengthening the housing counseling market, and I don't disagree with that. I think, you know, it's kind of like Mom and apple pie; it would be hard to disagree with that.

But one of the concerns we always have about this is that, you know, there are some bad actors out there. And how would you handle things like quality control? If you've got a bad actor out there that's making a loan to a vulnerable consumer, they could, you know, have business cards printed up saying they were also a housing counselor and that met that requirement. Or maybe that's a little stretch but they have a friend, you know, here, let me refer you to somebody who had business cards printed up that said a housing counselor on it and they met that, you know, criteria.

Plus, as we know, those of us who have been in this industry a long time, there's housing counseling and there's housing counseling. There's the, you know, 45-minute phone conversation with somebody that some people call counseling and then there's very rigorous counseling where people go for months. Literally sometimes it could be 18 months, even to straighten out credit reports, you know, learn how to budget, actually start saving money towards down payment, learning how to deal with after purchase issues, post-purchase issues.

So where do you -- you know, how do you sort all this out to make it meaningful and helpful to consumers?

MR. STEIN: I mean, I think all those issues are important. The issue of capacity, I mean, are there enough of the counselors who are qualified? Issues about integrity. Are they affiliated with lenders who might be bad actors or getting financing from lenders who might be bad actors?

But at the same time -- I mean, we do have a good, I think, example in the HUD certification process. So there you have an independent -- you know, you have HUD, government agency that will certify certain counseling agencies, and that maybe could be a model. And I just lost my train of thought, so maybe I'll leave it there. But certainly there are challenges, but it -- what we have now is a big problem.

And so in terms of how long the counseling would need to be, I mean, that's maybe a question for others to think more about. But what we're -- I think what we're focusing on today is how do we ensure that borrowers understand their loan terms so that they're getting loans that they know are in their interest. And that might require a certain amount of counseling.

We also don't want the counseling to extend so long that it frustrates the loan transaction. We appreciate that that's a time-sensitive matter for the lenders and for the consumers. But there has to be a better way than what we have now, and we think that that ties into and depends upon somehow building the capacity of counseling through funding.

And we would support the idea of requiring it for HOEPA and these nontraditional loan products as well.

MR. LEONARD: I think there are some precedents of mandatory counseling. There is a precedent for -- in the reverse mortgage program, which you'll hear more about this afternoon.

Again, I think it's explicitly established because it was relatively new product, being introduced at a much broader scale, very complex. And in that case there was a specific requirement at the federal level that all folks who would go through that process in an FHA insured, in a HECM reverse mortgage would receive a mandatory counseling.

I mean, I think the other thing to think about beyond that -- I mean, beyond the idea of building on the HUD-certified system of housing counseling, I mean, in -- what I think about is some sort of a third-party independent review mechanism that isn't necessarily even the extensive kind of counseling, you know, educational function but rather some -- a third party to which a borrower could easily and quickly go, have their documents reviewed and say, "Does this loan make sense for me? Are there some features that I -- that are problematic? Are there some changes that I should be seeking based on a current knowledge of the marketplace?"

And that's a -- it's a different model. I do not claim to have any idea about how to build the capacity to do it. But I think I would echo what Kevin said, is that this is really a large problem and we shouldn't be put off from the idea of attempting to address it simply because we don't have the existing capacity to do it today.

MR. LIEBER: Like I said, we fully support the consumers understand the loans products they're getting into, whether that be through forced counseling, which I personally don't think makes sense, or just ongoing access to information.

And I think much of what has changed in not just the lending business but the entire commerce in the last several years with the Internet is that access to information has expanded tremendously. And I think much of the technology that is available -- and I mentioned ours but we're not alone in it -- will allow borrowers to say -- to computer model, "Here's who I am. Pull my credit score. Tell me what loan type is available to me and what price I should pay." I think that access to information is the key.

And I personally would be very skeptical of any forced counseling. And then how do you confirm that the counseling itself is appropriate? And who is going to decide what is appropriate for a borrower? Because I personally would not want to decide who should or should not be able to have a certain loan type. I don't know how I would make that decision on some of the tougher cases.

MR. LEONARD: One other thing I would point out -- and I think it's actually also really important in the subprime part of the marketplace -- is that shopping and transparency are not nearly as available as it is in the prime sector of the marketplace. I had to look long and hard to find this rate sheet on their web site. Largely a web site advertised as being for brokers only.

You know, but if I'm a prime borrower, you and I can go to Mortgage.Com and pull up 50 different quotes based on the specific -- our specific circumstances. If you're a subprime borrower, the ability to do that shopping is not nearly as transparent.

MR. OLSON: Would those of you who would care to comment on differences you see if the mortgage -- the end product is a purchase mortgage product as opposed to a refi, if that makes a difference in terms of the abuses that you see or the -- or the counseling needs or whatever? Are the fundamental issues that we're discussing, are they different for a refi product as opposed to a purchase product?

MR. STEIN: Well, I don't know that there is. And I guess all I'd say on this is that we are seeing more problems in the home purchase market than we did before. And I know in a way it kind of calls into question -- and so HOEPA is what we have for anti-predatory lending regulation, which is focused on refinance, probably for good reason.

But I think we're seeing things shift so that we do see more of these products being sold, nontraditional and subprime, and more problems reported from borrowers in the home purchase side.

So I don't know about the differentiation, but I'm glad that you raised the question and I think we need to look to both.

MR. LEONARD: I would just say that in -- I'm familiar with data from 2004, purchase data from 2004, in the state of California and nationally, and what we know is that in the subprime marketplace, huge proportions of folks are using interest only, especially here in California where you have unbelievably high housing costs. Huge proportions are using interest only and option ARMs.

And so it seems to me that to the extent that you have folks who are stretching to get into homeownership, some appropriately, some not I suspect, using these alternative kinds of products, I suspect you're going to have increasing concerns about protecting folks in the purchase market in addition to the historical ones that have clearly been a problem in the refi market.

MR. CHANIN: So can we follow up on the purchase money issue? Then there may be, depending on what you view as the problem, different solutions. I mean, one is these people should not be purchasing homes. Or a second solution, if you will, depending on the problem, is that these individuals got the wrong product, that is, their credit score was such that they shouldn't have gotten this product. Or perhaps that they could have gotten a product more suitable for them.

So what exactly is the problem? Are people being stretched or is it all of those? And if you could address those issues.

MR. FULLER: So, you know, I'll start. I think one thing you also have to realize on the purchase market is I'm not sure it's the product. I think another thing we hear at least is you have a high incidence of very high LTVs, which aren't option ARMs. You know, it's people getting 100 percent financing. So there's kind of a whole different dynamic there that you factor into.

Now, what the solution of that is I don't know. We're not in that market certainly, so we don't have any great solutions. But I think it's -- the issue around purchase may not just be, you know, what product to use or something. It's -- there's a lot of 100 percent financing and other things maybe you're getting people into loans that maybe they're not comfortable with.

MR. OLSON: Jack may know more about what I'm about to talk about than I do or somebody else here from the San Francisco Fed maybe.

Ten years ago or so, I was involved in a -- in looking at a circumstance in Hawaii, in Oahu, where we were looking at the mortgage loan business. And Hawaii at that time, Honolulu basically, had some of the highest property values in the country, and certainly if you consider the ratio of property values to income, disposable income. But people still bought homes, and at a fairly high rate.

But what happened is that the lenders had to rethink the front end and back end ratios that were used in approving those loan products but those loans continued to perform.

Now, the only thing you can -- one of the things that you can clearly deduce from that is that people made lifestyle choices, to become house poor in that market because the house was important to them and discretionary purchases were not made in order to be in the house.

That could be happening in California as well, that there is some stretching to get into a house for that reason, but there will be -- that there will be an adjustment in lifestyle so that more discretionary income will go to that house.

And I'm wondering -- what I'd be interested to know is -- my point is that if the ratios are different from what they may have been historically or that values are higher than historically that that may not necessarily translate into problem credits and, therefore, borrowers in difficulty.

And as we look at -- this is now -- I don't think I've looked at first quarter '06 figures yet but I have through fourth quarter of '05. And in the banking industry, we have not seen an increase in delinquencies in the residential mortgage portfolio. As a matter of fact, it's been extraordinarily strong with the exception of some pockets in the subprime market.

There clearly are some prime -- and we're looking at those carefully because there's -- we are starting to see that there may be some evidence of predatory lending in some isolated markets. Well, we know it's there but it's reflecting now in delinquencies.

But I wonder if you could take into consideration what some of those fundamental lifestyle choices -- how that might affect -- and the incidence of homeownership and the value that homeownership has been given and how that might affect some of the other judgments that have been made thus far.

MR. LEONARD: Clearly the underwriting standards and the debt-to-income ratios that are reasonably and normally used are -- have gone up considerably. My sense is particularly in a place like California where prices have been -- are high and appreciating, there hasn't been -- there hasn't been any -- we haven't seen -- clearly people have stretched. Clearly a lot of people have benefited. We haven't seen what happens through a full cycle yet.

And I think that, you know, as I made reference to pretty clearly in my opening remarks, the issue of payment shock, looming payment shocks, particularly at the -- deep in the subprime market and for lower income households who don't have many choices, you know, I think the story isn't over yet, and I don't think we really know whether or not it was a responsible stretching and lifestyle changes or whether the payment shocks are going to force folks into mortgage payments that are going to exceed the commonly used income -- debt-to-income ratios and other ratios and have some significant negative consequences yet.

Again, interest rates were at all-time low in 2004. Vast proportion of subprime loans were moving to the -- 70 percent of the loans initiated in the subprime market in 2004 were the standard 2/28 mortgages. We've seen a huge amount of refinancing in those mortgages before they reach their two-year time frame. So there's something else going on there as well.

But within the next few years, and especially as housing prices slow down, I think we'll see whether or not -- you know, there's innovation and there's individual -- individuals have made prudent decisions about getting into and building wealth in their housing investments or whether or not, you know, ultimately a lot of folks are going to be put out of their houses and ultimately worse off.

MR. FULLER: So from World's standpoint, certainly we can't comment on the subprime market. Weren't not in that, so we wouldn't know. From our standpoint, underwriting standpoint, we're so conservative we stay pretty much where we're at forever and don't see that in the loans we get.

I think Paul does bring up an interesting point that one of the points is what rate are people underwriting people at? And certainly for us, and I'm pretty sure most reputable, heavily-regulated companies that are doing option ARMs, we're underwriting them at the fully indexed rate, not at the discounted payment.

So that lends credence to the fact that, hey, they can be okay. If there's other people that aren't doing that, that's certainly a big issue, a very big issue for the borrowers and the market in general.

MR. STEIN: I just -- I'm sorry, Jack. I was just going to quickly say the issues around choices that people make, I think those are issues that are discussed every day by housing counseling organization that are working with people to help them sort out whether they are ready for homeownership or not. And certainly given our housing prices, people do have to make certain sacrifices.

We also have larger problems as a society with increased burden, financial burden, on households because of health care costs and other matters, and people are looking, for those who have homes, looking to their equity as a way to kind of get themselves out of trouble, and that's a troubling trend.

We have -- my understanding is that foreclosures are going up and defaults are going up. In fact, there was a study done by a public policy student spent some time working with the Fed and she looked at few counties within California and found some correlation between subprime higher priced loans and notices of default and noted they're going up even though in California we've been relatively -- we've been relatively low in foreclosures given our high housing costs and we're concerned that that's changing, in large part because given the decreasing mortgage volumes, we think and I think other industry folks believe, too, that the result is relaxed standards.

So World may be having -- staying with their conservative standards, and we'll see if they maintain them if they're purchased by Wachovia, but what we're seeing is that people are looking for the money. I mean, that's what the problem is. It always comes back to what are the incentives?

Brokers want to make money, lenders want to make money. And if there are fewer loans to be made, people are going to relax their standards. So we're going to see problems because of loans that have been made with the nontraditional products and subprime loans to people that didn't deserve them or can't afford them, but we're going to see I think even worse loans continue to be made because of the pressure on brokers and lenders to do deals that maybe shouldn't be done.

MR. LIEBER: Well, I think it's very clear that the housing market has been very strong over the last several years and mortgage defaults have been very low, very clearly as a result of that.

I think, Governor, you make a key point, though, that the ability for people to -- the ability and the willingness for people to put more and more of their income into homes is evident in places like Hawaii and has been evident in places -- high-cost areas, California, New York, east coast and west coast, for several years.

But I do think that with what looks like maybe an ongoing trend of house price appreciation slowing, we'll definitely see a higher default rate. And logic would tell you that borrowers who are subprime, who have historically not had a perfect record of making payments, will have higher default rates. That's one of the key reasons the interest rates are higher, is to cover the expected higher costs of default.

MR. OLSON: We see -- I'm sorry, Jack. Go ahead. I apologize.

MR. RICHARDS: No problem. Thank you. I hope it's a worthwhile question now.

MR. OLSON: I have every confidence that it will be.

MR. RICHARDS: Well, I'm switching gears a little, so if you would prefer --

MR. OLSON: Please.

MR. RICHARDS: I read a number of news stories lately about people who probably should be under a full doc loan who are actually not forced to disclose income and, therefore, get in these situations where they can't afford the mortgage. I just wonder how are those decisions made, in your view, about whether a loan should be fully documented or not and do you feel that there are abuses?

MR. LIEBER: As a major lender who does significant amount of reduced documentation lending, I think there are a couple keys points I would make. One, that much of the stated income business is there because there are a lot of borrowers who do have difficulty documenting their income. They either could have very complicated tax returns, they can be commission-based. Frankly, some may be cash-based. And the stated income does actually expand homeownership in a very legitimate manner.

Stated income lending is not new. It has existed through different cycles and it is proven that the slight premium, generally speaking -- and ours is relatively modest but a premium -- in interest rate covers the slightly higher default rate that's expected.

I think there's another very key component that's occurred in the last several years with reduced doc lending. And it's not unique just to IndyMac but even with the GSEs, Fannie Mae and Freddie Mac. They have effectively created what I would call a documentation waiver program where if you run a loan through their automated engines, they say, "This borrower is strong enough based on their credit score. I have enough confidence in the value of this home and the loan-to-value is moderate enough that I don't need to see additional data. I know that this is a sophisticated borrower who knows how to make lending decisions on their own, or borrowing decisions on their own, and we don't, therefore, need that additional information."

If you look at the pricing structures of ourselves and many of our other lenders, at certain loan-to-value ratios, the odds of default are so low that that additional information doesn't bring anything to the table and, therefore, doesn't change the pricing.

So in our case, the smart borrower, the smart broker or banker will say, "You've got a 60 percent loan-to-value. You can provide your pay stubs, you can provide your tax returns, you can provide all your bank statements, but it's not going to generate a different loan rate for you because your odds of default are so small that we don't need them."

MR. STEIN: You know, I believe that the level of documentation is determined in large part by -- that decision is made by the loan seller and not the consumer, that we're concerned about both sides of the equation.

Certainly and more importantly, I think, consumers who are being sold these stated income loans and their income is inflated by the broker -- and I'll reference my friend James Sirocca who is here and hopefully will testify later who referred to them as non-stated income loans because the consumers often don't state the income. It's the broker or the lender that will fill in the amount.

And I think that, in part, those are being pushed because they might be quicker and there's -- there are greater costs associated with them. Maybe not in every instance but there are greater costs to the consumer.

On the other side, I'll reference someone else who is here, a broker who also may speak at 3:00, who talked -- spoke with me yesterday who noted that some consumers -- and this is I'm hoping something that the Fed and the regulators might look at. It may be the case that brokers are seeing an inventive to write CRA loans to actually reduce income in a stated income loan context so that there are lower -- the borrower is seen as a lower income borrower and, therefore, the loan might qualify for CRA credit, which I -- which is incredible. So we think stated income is a big problem.

MR. LEONARD: Just quickly, I think that stated income loans can clearly serve a useful purpose for a number of borrowers, depending on their certain circumstances. I think it's useful to have it.

On the other hand, I think it's also ripe for potential abuse. And we're hearing it all the time out here. I got a call just last week from an FBI agent in San Diego who was talking to borrowers and who said she could not believe the extent to which borrowers were acknowledging the inappropriate use of stated income, stated income to make a loan pencil out.

So I think it's a real serious, serious concern and I -- you know, I, for one, would not like to see the option for stated income go away as an appropriate tool in the right circumstances, but I think it is also a tool that is increasingly being abused to create income levels to sustain loans where the actual income levels are known to not be sufficient to qualify for a loan.

MS. BRAUNSTEIN: I'd like to change topics just a second and ask a question about the guidance that we put out for nontraditional mortgages. And it was, you know, referred to in several of your opening statements on both sides of the issue.

One of the struggles we always have anytime we issue regulations guidance on any of the topics we deal with is that we are very strongly trying to balance the interests of consumers and consumer protection, which is extremely important to us, as well as concerns about regulatory burden and unwarranted interference in the markets. And so it's -- you know, it's always a struggle as you know.

And one of the things we used to say I know when we were writing CRA regulations is if at the end of the day the bankers were unhappy with us and the consumer groups were unhappy with us, we probably got it about right. Because if one or the other was too happy with us, maybe we weren't, you know, as balanced as we should be.

Okay. So given that, we issued this guidance on nontraditional mortgages. And actually, what's been interesting to me is less the comments we've gotten from the consumer groups frankly but the comments we get from the industry.

Because on the one hand, some of the industry people have come back and said to us, "You didn't give us enough structure to this. We want certainty. We want safe harbors. We want regulations. We want forms. You know, we want you to design model disclosures. We want certainty. We want to know absolutely positively we're doing what you expect us to do."

Then on the other hand we hear lenders -- and when Bruce said this it hit me. We heard other lenders say, "But no, we want flexibility and, you know, it's guidance, it's not rules, and there should be flexibility there."

So I'd like to hear some -- a little bit of discussion on that as to which way we go on this.

MR. FULLER: Well, I think for us there's a couple of key points. One is there's -- there are certain areas where we felt almost needed to be stronger because we think it's at the heart of the issue, like the deep discount on the payment that we discussed, where we feel like that's where -- you know, that's the issue of how fast neg am is going to build up and how strong. And we discussed in our letter some additional language you might use there.

As far as specific rules on underwriting and other areas, I think what you hear from us really is that we're afraid that we'll make rules and the bad actors will get around those. And how we got to balance those to use the benefit -- obviously we need to have guidance on this and we need to know where people should be, but we have to balance that to be able to still have the benefits of the loan and not -- and not prescribe it in a way that just doesn't make sense. So that's where you hear the balance from us I think.

MS. BRAUNSTEIN: And that's from you, but that's not what we've heard from a lot of other lenders. They want us -- some have even asked us to design model forms and model disclosures.

MR. FULLER: And it might be because we've been -- this is just me guessing, but we've been doing it for a while and so we feel like we'll be able to work through it. Maybe others that are new are a little less certain.

MR. LIEBER: And I would say we generally agree with Bruce's comments in that I think there would be great risk in making the guidance overly prescriptive because there will be bad actors who then will say, "Hey, you told me I had to do this on this feature, but I've got a hundred features I can deal with and you didn't mention the other 95. So I can go expand on those."

Our position is that the banks that are regulated, regulated banks, have examiners that come in on a regular basis and go through and look on a very holistic basis at loan programs. And we think the guidance should stay general and that the examiners who come out can make the decision of whether or not each institution is coming up with prudent and reasonable loan programs on all aspects, not just ones that may or may not make their way into either guidance or regulation.

MR. STEIN: Just as a general matter, sometimes I worry that we're more upset with you guys than the lenders are. So I appreciate your kind of walking in the middle there.

And just on the issue of regulation, I'm thinking back to the last hearings and when we were talking more specifically about HOEPA. And I think that's also relevant today. And I'm curious, just as you -- to look back and wonder what comments were made at the time from those who were concerned about additional regulation and have those concerns proven to be valid. Because the regulations were tightened after the hearings.

And I haven't heard much in the way of complaint about, you know, having to deal with the new HOEPA framework. So in the same vein we would urge you to go back and look at HOEPA and look at prepayment penalties and yield spread premiums.

And again, as a general matter, you know, we're interested in the results. So whether it's flexible or more prescriptive from the regulators is not much of a concern, though we do feel that to the extent that you can be more specific that it provides less, you know, wiggle room for those who might try and circumvent the regulations.

MR. OLSON: Anybody else? We're at 10:28. And this has been very helpful. Thanks to all of you, Paul, Kevin, Rick, Bruce.

We'll take a break now. We will be back at 10:45. Trust me, unless I have a heart attack, we're going to start right at 10:45. And that in doing so, that gives us full opportunity for a very thorough discussion.

Thanks again.

(Whereupon a recess was taken.)

MR. OLSON: If the panelists could come forward, we hope to get started now on our second panel.

Continuing very much on the same subject but focusing even more on informed consumer choice, we will have five panelists in total. And with the same process. So we will have a five-minute statement for everybody and then opportunity for a -- for questions from our panel. And, of course, opportunities for exchange amongst the panelists. And we will conclude at 12:15 with a break for lunch.

We will -- the procedure I think worked well in the first, when we started from the left and went counterclockwise. So Heidi, we'll start with you and then Lori, George, Michael, and Judy.

If you would introduce yourself, your group, and then five minutes. And then we'll proceed with Q's and A's.

Heidi.

MS. LI: Sure. Thank you. My name is Heidi Li and I'm co-director of Housing and Economic Rights Advocates. We're an Oakland city-based nonprofit legal organization that focuses on doing -- providing legal services and advocacy around the areas of fair housing and predatory lending abuse concerns.

Our mission as a statewide organization is to ensure that all persons, particularly lower income, minority, elderly and other vulnerable persons are protected from discrimination and economic abuses.

We work with a variety of organizations as well, not just legal advocates but nonprofits, government agencies, community-based organizations to go ahead and offer them technical assistance and training to address particularly predatory mortgage lending abuse issues and also to work with them to try to screen and assist these folks who are getting into these abusive and unfortunate loan situations.

So that's my quick introduction I hope.

MR. OLSON: My goodness, I'm stunned. Nobody has taken that little time. We'll be -- we'll save the rest of it for our questions and answers. Thank you.

Lori.

MS. LI: Well, I think that was actually just to let you folks know who I --

MR. OLSON: Oh, that was the introduction. Oh.

MS. LI: I'm sorry. That actually wasn't so short. So let me go ahead and actually talk about and share with folks today what I'm here to hopefully speak a little bit about.

And I just want to say thank you for the opportunity to testify at today's hearing. I'm here speaking on behalf of my organization but also as a consumer advocate and housing rights advocate who actively partners, as I mentioned, with a number of other types of entities and organizations to address predatory mortgage lending abuse.

Some of these organizations I understand will actually be here a little later today during the open comment period and hopefully offer their own testimony, along with perhaps a few of their clients that we've all been trying to assist with these predatory situations.

I'll start first with listing and giving an overview of what are some of the nontraditional mortgage products that many of us as advocates are seeing increasingly in the consumer mortgage market these last four or five years.

Particularly we're finding that consumers, many of whom are first-time home buyers, some of whom are refinance borrowers, are coming to us with one of the following types of nontraditional mortgage products:

A no document income stated loan, an interest only or negatively amortizing option ARM product, or sometimes what we've actually been identifying or seeing are combination of the two, and lastly, for seniors, predatory equity stripping refinance loans or reverse mortgages.

These products have been increasingly in presence in the lending mortgage market since the 2002 revisions to

HOEPA, which the Federal Reserve Board, you know, went ahead and made recommendations to congress and to the FDC to go ahead and implement. So we want to sort of say that, you know, this is something that I do think really requires some new scrutiny and looking at since the last few years.

On a related note, we're also seeing something that isn't being covered by HOEPA but we think is important to be looking at, perhaps on the federal level, and these are these detitle theft scams. We are seeing an increasing number of homeowners who have had their homes for a couple of years at least and built up some equity, and unfortunately often when they're in some sort of foreclosure or financial distress, they're getting their title to their homes actually taken from them by foreclosure scam artists and financial consultants who are ripping them off.

So here in California we have -- we are really the home for significant amount of subprime mortgage lending, I think I understand perhaps about a quarter of the annual lending that occurs. We also have a very demographically diverse market and resident base. Really the -- I understand based on the U.S. census, we have probably somewhere in the range of 20 percent each of Latino and Asian Pacific Islander residents in this state. We also have a strong African-American and other nonwhite population presence as well.

When you look at all this together, coupled with the fact that the average price for a home here is about minimum $400,000, we're really concerned that when folks are getting not only put into but aggressively marketed or pushed into these -- some of these nontraditional loan products that this becomes a very big problem, when they are not meaningfully getting disclosures about what the loans are about, what the terms are consisting of, and what's the real true result of what's going to happen to them financially once they're actually in these loans.

The other concern is that really a very high incidence of the folks that we're seeing coming to us, housing counseling agencies that we work with, other legal service providers, are really folks who are Latino or African-American. They're often lower or moderate income homeowners or individuals, many of whom are immigrants and limited English-speaking individuals, and quite a few increasing number of seniors, many of whom have disabilities.

So I think when you talk about what is a meaningful disclosure, we're really concerned that under the current HOEPA requirements, one, that there are a number of products, including these nontraditional products that are not actually covered under HOEPA, but two, that those disclosures alone are not adequate or sufficient for this type of consumer market.

How are consumers shopping for loans? Well, this is the thing. We see two things that are happening. There's really a lot of referral going on on -- in an informal manner through channels that are not your traditional lending, prime market channels. And that happens often for two reasons.

One because there is perhaps that lack of familiarity or trust that folks are -- are not feeling when they go to some of the more standard institutions, lending institutions, but two, a lot of those traditional institutions, especially with prime and other products, are not actually being based in communities and neighborhoods that are high of color or moderate income communities. So we think that is a concern.

And I think perhaps the reporting issue that you're looking at as far as enhancing some reporting as to where the loans are being issued should be something to be looked at by the lenders as part of regulations that you are looking to perhaps address with reporting concerns.

As far as going back to the referrals, we have seen that unfortunately many folks are getting referred to realtors. These realtors are people they know from their families, their friends, their communities, their churches --

MR. OLSON: Heidi, we're going to have to stop you there. I think where you are now we want to come back to.

MS. LI: Sure.

MR. OLSON: Because an issue that is really key is where people go for advice. And this is not -- we're not sociologists. We're not even behavioral economists for the most part at the Fed. But it plays an important decision in how people end up in the kinds of financial transactions where they are. So this will be really important for us.

Lori Gay, you're next.

MS. GAY: Thank you, Governor. Do we have three minutes or five minutes?

MR. OLSON: Five.

MS. GAY: Okay. I want to time myself.

Thanks for having us here. We appreciate you looking at these regs, again. It's been six years. I want to talk about what's gone on since then.

I'm here as the president and CEO of Los Angeles Neighborhood Housing Services. We're a nonprofit neighborhood lender, developer, community development, financial institution, realtor, you know, all the things that help people get in affordable homeownership and stay there.

We're a member of the National Neighborhood Network, which serves over 1,500 neighborhoods in all states throughout the U.S. as our kind of trade group.

And then today I was asked to also show up as a member of the California Reinvestment Coalition. You heard from Kevin Stein earlier.

I want to start my comments by underscoring some of what's important here in California with our coalition, that we'd love to see and urge the Fed to consider.

We'd like to see more overpriced loans within the protection of HOEPA and also -- and another review of restricting yield spread premiums and prepayment penalty provisions that we believe charge borrowers thousands of dollars for refinancing out of bad loans.

We want to have you review, again, protection for consumers from unscrupulous lenders and brokers who take advantage of borrowers not fluent in English. One of the most amazing things I've seen in my 15 years at NHS is how many documents are not in Spanish or Korean or Mandarin but yet that may be the first language of the family being served. And we've counseled them or talked to them in all of those languages, only to get down to closing and have everything in English. It's like driving a car in another country. Not a good thing.

Expand Home Mortgage Disclosure Act reporting requirements so more data is available to better detect areas of discrimination. I sat with nine banks over the last six to eight months when the HMDA review detail came in the marketplace. All of them made lots of excuses. They're all my friends. I love them all. But they made lots of excuses with the new reporting on why their HMDA looked the way it did, and then made further excuses about why basically the data didn't really reflect what was going on. I thought that was amazing.

So I want to see the reporting requirements expanded even more because I don't think we all know what's really going on and we've got to continue to dig into it.

We will always be on the side of requiring housing counseling before closing of loans, generally, because as a nonprofit we believe it's a good protection for families. I think it's difficult in the mortgage marketplace to require it, but I think the closer we come to pushing for people to think about, learn about, and really know what they're signing, it's helpful. And to receive as much neutral counseling as possible. I don't think that all counseling that somehow leads to a loan with the same group is bad. I'm just suggesting that it's helpful.

So that's my support of the California Reinvestment Coalition's position.

I want to just further state the importance of this effort today on promoting and sustaining homeownership. Our background in Los Angeles, one of our tags is that we put 55 families a day on the road to homeownership. What we mean by that is that we take the people through a system of borrowing that's important. It's called full-cycle lending.

And it works toward financially educating and counseling families about options, about what a mortgage is, et cetera, et cetera, looking for affordable loans for them and/or providing one through our company, providing construction management services since 95 percent of most of the housing loans that are done in L.A., the homes need some kind of rehab because we have older housing stock. That's a big deal. We ultimately then look toward neighborhood revitalization happening in that process.

What's the state of housing today? We've seen median home prices rise, household incomes rise at a slower level. California is the second least affordable state in the union and in California we have the top eight least affordable counties in the United States. We have a 14 percent affordability index right now on housing and 12 percent in Los Angeles county.

So I think we've got some issues in our state that are a little different than other states. Ninety-seven percent occupancy rate in a city like Los Angeles with $1,500 costs on average, Governor, for a two-bedroom apartment. So as people look to buy homes, they are then going into, so I bring this home for you, the impact is that families are looking at stated incomes as an option.

I will spend time again on the phone today with a client of ours at NHS who came through the city's rehab program to get $90,000 worth of rehab at zero percent fixed for 30 years loan because their family makes $24,000 a year, family of five. They were approved by the city for the loan that we packaged and originated on behalf of the city at NHS.

And then I found out two days ago that they wanted more money and I just couldn't quite figure that out. And so when I looked at the detail of what had gone to the city and gotten approved, they have two stated income loans. The city's loan was going to be in third position. I'm confused by that scenario. Why the city would have approved it astounds me.

MR. OLSON: Lori, these are -- we will be getting back to you on these also. What you're describing is a market where there are a lot of positive things happening in the market but some -- but there are collateral effects of that --

MS. GAY: Right.

MR. OLSON: -- of that success that have implications for individuals. And we want to come back and pursue it further.

MS. GAY: Thank you.

MR. OLSON: George, you're next.

MR. HANZIMANOLIS: Good morning. I'm George Hanzimanolis, vice president of the National Association of Mortgage Brokers. Thank you for inviting NAMB to speak on informed consumer choice relating to nontraditional mortgages.

As the voice of mortgage brokers, NAMB speaks on behalf of more than 25,000 members in all 50 states. Most mortgage brokers are small businessmen and women, guiding consumers through the mortgage loan origination process. We provide an efficient market mechanism for the distribution of mortgage products to locations where banks, lenders, and others do not go.

In order to shop, consumers need a free market, origination and consumer education, and new mortgage comparison tools such as a charm booklet and a good faith estimate that are consumer tested.

NAMB believes there are five critical tools consumers need in order to choose a mortgage, traditional or nontraditional: One, government and industry have failed to provide consumers with the necessary tools to shop for mortgage products. Therefore, NAMB has proposed revising the current disclosures to account for mortgage innovations in nontraditional mortgages. This means creating a good faith estimate that consumers receive at the beginning of the mortgage process that mirrors the HUD1, is one page in length, and provides the information valued by the customer, most notably meaningful estimates of closing costs and monthly payment.

Furthermore, any new disclosures should treat the disclosure of rate, fees, costs, and points uniformly regardless of the channel, banker, lender, or broker chosen by the consumer to originate their mortgage loan.

Second, we need to create and implement well-designed and well-tested consumer disclosures that are uniform, consistent, and meaningful to the consumers who read them. Regardless of the distribution channel chosen, each consumer should receive the same disclosures in the same format for any particular loan product, type, or transaction, giving meaning to the ability comparison shop.

The well-documented 2004 study by the Federal Trade Commission on a proposed good faith estimate form showed that many consumers would choose a higher cost loan from a direct lender over a mortgage broker loan because they were confused by the format of disclosure.

Third, we need to protect consumer choice by keeping a competitive marketplace alive and not stifling market innovation by limited product choice. We must be careful not to rob this innovative and dynamic industry of the ability to remain a free and capitalist market that brings credit to the underserved markets.

We should not band products from the market nor set compensation or usury caps. Those have all failed in the past. We should empower the consumer with both knowledge and the ability to make an informed financial decision that fits in the context of their life circumstance. The consumer is the only person that should choose his or her mortgage, not government, not consumer advocates, and not a bank, lender, credit union, or mortgage broke.

Fourth, the government should ensure that every single mortgage originator is required to complete both preemployment and continued education requirements. Every originator should be knowledgeable about the risks and benefits of the products offered, especially nontraditional products.

If consumers shop, they'll learn about the products and choices available to them. If consumers shop and compare, then they'll have questions to ask. Consumers should not and in the competitive marketplace do not have to use someone who is not willing or not able to answer these questions.

And fifth, most importantly, we cannot and should not continue to ignore the role of the consumer versus the role of government. We must advocate for financial literacy in this country, starting at the middle school level. We must allocate funds for financial literacy programs at the middle school and high school level so that consumers are educated about the financial decisions that make and retain the decision making ability.

I know there are those who want to argue that this is a long-term solution that will take time. And I agree, it is. But we are not talking about a short-term problem that will respond to a Band-Aid approach.

The evolution of consumer finance did not begin in 1994 when HOEPA was passed into law. Since the time of barter and trade, we've grappled with the issue of how to increase fair and equal access to affordable credit for all socioeconomic classes, not just the elite few.

Laws have been passed, enforced, and forgotten as we've turned to new and different laws. We must focus on the solution that will stick. That solution is financial literacy.

Thank you and I look forward to answering any questions that you may have.

MR. OLSON: George, I think from the time that I was nominated to the Federal Reserve, I had more people from more different walks of life comment on the financial literacy component of it as being -- as being a gap that has probably been ignored, and we have a lot of catching up to do in that area.

Mike.

MR. FAUST: Thank you, Governor. My name is Michael Faust. I'm the vice president of the government affairs committee for the National Association of Mortgage Brokers.

NAMB is proud to offer educational courses and professional certification programs to mortgage professionals. Our members adhere to a code of ethics and a strict practice -- strict set of best practices. Because of this, our members are better prepared to guide consumers through the complex mortgage process.

There are numerous distribution channels in the mortgage industry today. The consumer can get a loan from a traditional depository, a credit union, a mortgage banker, and a mortgage broker, an Internet lender, and the list goes on and on and on.

Each distribution channel shares one thing in common; the consumer approaches them with the same goal in mind, obtaining a home loan. The consumer does not distinguish between a mortgage broker and a mortgage banker or a direct lender. To a consumer, they all provide the same thing, the opportunity for homeownership.

However, only mortgage brokers currently divulge the fact they earn indirect compensation when a loan closes, referred to as yield spread premium. With lenders and bankers, they claim they can't determine this income, thus they can't disclose it.

We all know this is ridiculous. They receive indirect compensation in the form of service release premium or gain on sale. This differential and disclosure provides confusion for the consumer when comparing loans from different distribution channels.

There are three interconnected components to the mortgage finance system, the government, the industry, and the consumer. Each of them has a substantial role to play when evaluating nontraditional mortgages, how consumers shop for mortgages and the effectiveness of the mortgage disclosures they use during the process.

Many industry critics have based all the problems that some consumers have from the current shopping process, products and disclosures within one point of this triangle, the industry. When they do, it simply ignores the vital roles of the government and the consumers in the loan process.

The role of the industries remain innovative, competitive, and knowledgeable, so consumers can use their financial education when they shop and compare. This can be accomplished through licensing, education, and criminal background checks for all mortgage originators.

Anyone who signs a 1003 and originates a loan should be held to the same standard, no matter the distribution channel they may work for. Mortgage brokers in many states already adhere to these standards. However, the banks and mini-regulatory schemes which mortgage bankers are licensed under do not require originators to have any licensing, any continuing education requirements, or submit to criminal background checks. We encourage the government to set a single standard the consumers can count on, no matter the distribution channel they go to to get a home loan.

The role of the consumer is to acquire financial acumen, both during school and then throughout their lifetime. The consumer should take advantage of the competitive marketplace to shop, compare, ask questions, and expect answers. And if they don't get answers, they should move on to someone else.

To make comparison shopping most effective, all distribution channels should provide the same disclosures. Let's be careful not to lull consumers into believing that the government, the industry, critics, or the industry is here to protect them at every turn. Such an approach only ensures reliance by people who feel comfortable in their lack of knowledge.

If we want consumers to be empowered to make financial decisions, then the role of government must be to provide the information and the guidance necessary. This can be accomplished through financial literacy and updating the disclosures and information booklets provided consumers. We must inject financial literally into our middle schools and our high schools.

We're aware this is not a short-term solution. This is a long-term solution. But this is a serious problem that cannot be fixed with simple slogans. Government can and should develop a simple, plain language brochure on nontraditional loan products. This should be for distribution to consumers at application of nontraditional loan products.

Revise the charm booklet to include information about features, risks, and benefits of nontraditional loan products. Consumers test the revised charm booklet and special information booklet to ensure its utility first of all and its effectiveness as an information source for consumers.

Consult with a task force that represents current mortgage marketplace. Entertain both industry and consumer input when revising that booklet. And enforce the existing laws to eliminate deceptive and misleading marketing practices. And last but not least, ensure and maintain an innovative and free marketplace.

Thank you very much.

MR. OLSON: Thank you very much, Michael.

Once a Minnesotan and now back in California, Judy.

MS. ZEIGLER: Thank you, Governor Olson, for the opportunity to participate in this important hearing pursuant to homeownership and Equity Protection Act, HOEPA.

I'm a realtor with Prudential California Realty. I live in Palm Desert, California and I'm here today representing the National Association of Realtors.

First let me put the issues in context as far as the National Association of Realtors is concerned. The National Association of Realtors has long been concerned about the impact of predatory lending on home buyers. Our primary concern is with purchase money mortgages, but refinancing, strip homeowner equity are also a problem because it can rob a family of its wealth and make moving up to a better house impossible.

In 2005 the National Association of Realtors established a subprime lending work group to develop standards that represent balance for continued valid uses of subprime loans for borrowers with imperfect credit while avoiding predatory lending practices. In May of 2005, the National Association's board of directors approved this subprime lending work group report.

The report has two primary recommendations:

Consumer education. Encourage realtors to work with existing programs and community groups to help consumers qualify for fair and affordable housing, become more financially literate, and, where appropriate, obtain counseling.

Strengthen HOEPA. Support strengthening HOEPA including expanding its coverage to purchase money mortgages, lowering the triggers to apply to more mortgages, which should have the effect of reducing interest rate and fees for subprime mortgages as lenders price their products to avoid HOEPA requirements.

Bar prepayment penalties or at least shorten the maximum permissible time to three or fewer years. Cut the amount of fees and points that may be included in the loan at about five percent, plus up to two bona fide discount points and numerous other recommendations for making HOEPA stronger.

Implementation of the work group. One of the ways the National Association of Realtors implemented the subprime lending work group report was to develop two consumer education brochures in partnership with the Center for Responsible Living. And you heard from Paul Leonard earlier.

The brochures are in a series captioned "Shopping for Mortgage, Do Your Homework First." They are available on Realtor.Org, which is the web site for the National Association of Realtors. You can download them for free and print them yourself. I know they're in English and Spanish. Or you can order them from the National Association of Realtors at a minimal cost.

The first brochure -- and I believe you have some of them in packets. Okay -- is called "Specialty Mortgages, What Are the Risks and Advantages?" Specialty mortgages are also called nontraditional or exotic mortgages. The brochures help consumers weigh the pros and cons of nontraditional mortgages. Payment shock is probably the biggest concern of interest only and payment option ARMs. We also include 40-year mortgages as nontraditional since borrowers accrue equity at a much slower rate and pay much more interest over the time of the loan.

The second brochure is called "Traditional Mortgages, Understanding Your Options." This brochure warns consumers once again about nontraditional mortgages and explains 30-year and 15-year fixed rate mortgages, traditional ARMs, including hybrid ARMs and home equity loans.

The Federal Banking Agency proposed nontraditional mortgage guidelines. The National Association of Realtors submitted comments to the Feds and other banking agencies on their proposed nontraditional mortgage guidelines for banks and their affiliates.

The National Association of Realtors applauds the strong stand the banking industries took in urging banks to make sure consumers understand these mortgage products. However, we are concerned that underwriting standards may be so strict that they will unduly restrict the ability of families to buy homes in high-cost areas such as California.

If we understand the guidelines correctly, lenders must underwrite a nontraditional mortgage loan based on the proposed borrower's ability to repay from today's current income, the maximum potential mortgage payment when fully indexed payment kicks in. The result is that only families that could qualify for nontraditional mortgages would be those that don't need them.

Lenders based on written documentation should be able to approve nontraditional mortgages for families that will be able to afford the -- that will be able to afford the higher payment based on changing circumstances such as expectation that a family member will join the workforce upon graduation or when young children start school, the borrower proposed to renovate the home and built sweat equity, or the borrower plans to live in the home only for a few years.

As a realtor for 28 years, I've had the experience of working with many clients from various income brackets and I've worked with people on interest only, payment option mortgages, and 40-year mortgages. And I'll be happy to answer any questions you have and thank you for inviting us.

MR. OLSON: Judy, thank you very much. This is a link that we haven't explored very much. We have been talking to the community groups, to lenders, but to get the realtors' vantage point would be enormously helpful.

Heidi, come back to a point, if you would, that you started on, and was discussed at some of our previous panels, particularly in Chicago, where you talked about the counseling process and -- and it's very significant in the immigrant population but not exclusive to the immigrant population, that there are ranges of preferred advisors, if you will, or where somebody is apt to go looking for advice.

And have you -- what have you found with -- in that respect and how does that -- how does that impact the service that you get or the assistance that you get?

MS. LI: Well, I think that's a very important thing to try to look at more closely. And I think I would respond by saying two things to start with.

One, we really do need to have more HUD-certified I would say housing counseling resources that are not only available on the ground but I think placed in the various communities where a lot of the nontraditional loan products are getting distributed to, originated to.

I think that's really important because people will respond to and trust and speak with people who they are familiar with and I think often will have the language access issues as well to make that more possible.

I also think that the second thing goes to the requirement for some of these -- these I think nontraditional products to have some form of required, if not mandatory, counseling in the process.

Because we are seeing too many people, as legal advocates anyway, who are going to housing counselors for that individual one-on-one counseling about a loan that they've already gotten into or a set of loans that they've already gotten into that are predatory after the fact.

And right now under the current legal or regulatory schemes, state and federal laws, there's very limited options in which people can now get out of or undo what they end up finding out are these predatory loans.

And that's a problem because we need to figure out -- yes, I agree that there's -- it's great to see that there's a voluntarily level of interest from all sides to want to encourage financial literacy at an early stage, in middle school, to see it happening as part of a larger education campaign. I think to continue to move along on that track is an incredibly essential approach.

But that alone we are seeing is not going to, I think, change the problem. And I think another reason is because of the channels -- the people that are now seeming the most familiar and the most trustworthy are sometimes the brokers and some lender representatives who are from your churches, or referrals from your churches, who are from your own community, who are the ones that --

Unfortunately though they may be referred to as the bad actors of the broker and realtor industry, they do exist. And so they're the ones that are managing to gain the most I think successful access to the most vulnerable people to these types of nontraditional products.

MR. OLSON: Lori, you talked in your presentation about something that is critically important to us, which is the revitalization of neighborhoods and the important role that homeownership plays there and, therefore, the important role of access to financing there.

I was around at the tail end of the discussion on the HOEPA regs, and one of the concerns that we had with how we set our trigger rates at that time was the concern that quality institutions would not want to identify with the HOEPA product and, therefore, what we would see in some markets is quality institutions maybe moving away from some of the higher risk markets.

Part of the delicate balance that we play is how we do that, how we continue to let lenders know that we want to see the quality lenders and brokers because -- just in the essence of full disclosure, I have a nephew who is a mortgage broker. I'm very proud of him. He's a very high integrity person. So I know that that person is -- that's the central tendency if you will.

But nonetheless, how do we -- talk to me about -- or talk to us about what some of your experience is in that respect with how you -- how you encourage lenders without mandating lenders to come into a marketplace.

MS. GAY: No one wins with foreclosure.

MR. OLSON: Amen. You are so right.

MS. GAY: We don't win. We've estimated it costs about 40 to $50,000 to foreclose on someone. Nationally we've initiated the Center for Foreclosure Solutions, which I know the Federal Reserve has supported. And we want to see more of those centers started all over the country because that's where we are.

We're up 63 percent in L.A. county from a year ago for foreclosures. Where are they happening? Seven times the rate of foreclosure happens in Central City L.A., South Bay L.A., San Pedro-Wilmington area, and East Valley where Spanish is the primary language.

So we see -- what I'd say is to encourage the conventional mainstream to stay. We have to talk about beginning with the end in mind. We want to keep people in their homes. We have to figure out a way that it's seen as profitable to lend to people who may be perceived as poorer credit quality and risky.

We've never had a foreclosure in 22 years in business in NHS. And across the country the foreclosure rate is less than three percent with the 250 nonprofits doing it. We're not perfect. We don't know it all. We work with local banks.

But there has got to be a way to say to them don't continue to finance the payday lenders, don't continue to finance some of the equity boys who are not being monitored at the level of scrutiny they need to be.

And until there's an examination process, quite candidly, that incense banks to think refi, think purchase almost at the same grading quality, if you're following me, on the CRA process, if a banker knows they get more brownie points for the purchase type transactions and is willing to buy the market to get to that place versus refinance, which protects people potentially from foreclosure, they're going to skew toward the thing that keeps them out of trouble.

So I don't want to get too deep on that, but I think the answers really lie in protecting people from themselves to some extent without government getting too involved. I understood where Michael was. Consumers need to be empowered to make their own choices.

What we see, though, is that families are not fully disclosed to, they're not fully and adequately prepared for the mortgage decisions that they make, and that many of the banks feel that their arms are twisted in terms of working with consumers to provide those adequate protections. Because when they're examined, Governor, they feel that, you know, the safety and soundness issues that come up for them encourage them to be in another place.

And I don't want to certainly take issue with the Federal Reserve or any other regulator. What I'm suggesting, though, is that people don't have all the information they need on any side of this process and so there's an aggression towards originating loans because it's profitable, to whomever, we'll take it out whenever they'll take it out, which is how I end up with a client with $24,000 a year income with $90,000 rehab behind two stated income loans. That's a heart attack waiting to happen.

And when I get on the phone with her today, I'm going to say no to all of it. And she's going to be upset with me for a minute and then I'm going to say, "In my office on Monday. We're going to fix your problem. But it's not going to be fixed with the lineup you've got."

And guess what I'll have to do? I'll pay off prepayment penalty stuff, you know, I'll sit and fight with her lenders who shouldn't have made her that loan. She didn't need a stated income loan. But this is the nature of the marketplace.

So I'm just suggesting to you that when originations on home equity loans went up to $400 billion over the last several years versus 92 billion in the '90's, I mean, people are -- the profit motive is alive and well in this country, and I think that we have to be honest about that and that we do have to push families to get educated, get smart, don't borrow wrong but borrow smart.

But there has to be some system, and if it can't come through the examination process, through the regulatory process, then maybe we need our lenders to be better educated about the real risks involved in lending to families of modest means, because that's the last of folks that need help.

MR. OLSON: George, both you and Michael talked about differentiating among distribution channels. And I know that's a -- that's an issue that is -- is an important one for you, and for obvious reasons, not particularly obvious to the consumer. But I'm interested in this -- initially in this part of it.

As lenders have increased their reach beyond what would be their typical business footprint, where they might have branches, they do it in a significant way through brokers. So how do you -- how does the broker -- how do the brokers develop that link, build those links, and what is the process by which there is a monitoring that takes place to presumably avoid the kind of situations that can exist that we've heard, for example, from both Heidi and Lori?

MR. HANZIMANOLIS: Well, first you're correct. And we are the grass roots. We're the people out there. And I'm a mortgage broker. I do this every day. I meet with my clients, my staff. My loan officers meet with clients to determine, one, is it right. We try to help educate the customer so they understand the products.

As we said before, I don't know if there's enough education out there and we need to do a better job of educating that. I think mortgage brokers on a whole do that very well. We go out, we explain the different products, we explain the processes. We also explain the risks and the benefits of each of these.

Homeownership is at its highest rate. We know that. And, in large part, that's because of what mortgage brokers have done.

So I think when it -- to talk about -- when you talk about things like suitability and issues like that that we've talked about before, we have to -- we have to be careful in what we do in limiting the mortgage broker and allowing them to continue to offer those products to the broker. When we do things that limit our ability, that can affect what we can offer them.

MR. OLSON: Michael, your -- one of the points that you made is that -- I'll have to confess I haven't looked at this carefully, so this is new to me -- you're suggesting that there are differences in disclosure requirements from different channels. And that's new to me.

So could you explain that more and tell me what -- how that impacts you and how that might impact a borrower also?

MR. FAUST: Sure. And I think part of what I'm talking about goes back to the first panel where we had one of the panelists talk about that he spent an enormous amount of time searching around on a wholesale lender's web site to find the rate sheet.

There's two different types of -- or there's multiple types of lending that happens. One is directly to the consumer by the lenders. The second one is through the broker channel where we are essentially the conduit between the consumer and wholesale lending market.

We enter into an agreement with the mortgage lenders to, you know, provide access to their services. And there are reps and warranties that we end up getting into with them as well, such as if a loan pays off early or if -- or goes into foreclosure, if there's fraud within the file, broker can be on the hook from everything from the early payoff, which is essentially a yield spread premium back, to, you know, if there's fraud in the file, the broker could be on the hook to buy the loan.

Now, that's something that no one wants to ever talk about. And the reality is when you look at a wholesale rate sheet -- that's the difference between wholesale and resale pricing, boiled down to its very essence. And the lenders, the direct lenders, still make the difference between wholesale and retail pricing. They use -- they hide under the concept of service release premium and gain on sale.

The reality is yield spread premium is carved out of service release premium. They know what they think they're going to make when they service that loan over that period of time.

And so the entire argument that we're having here is almost disingenuous by some people because what they've decided to do is they've been able to easily identify one of the ways of economic compensation for one of the distribution channels. And what they failed to recognize is the fact that that same economic works for all the distribution channels. Just some of them get a federal carve out under the secondary market exemption.

I would be concerned if I was a stockholder of a major lending institution that couldn't determine what their potential risk and/or, you know, income is when they originate and fund a loan.

So the reality is that it does affect us, especially in dialogs and conversations like this where certain lending channels are given exemptions from having to even disclose or acknowledge it, when the reality is everyone makes indirect compensation. Either comes from yield spread premium, comes from service release premium, and/or comes from gain on sale.

All distribution channels should have to disclosure in the same and fair manner, because the reality is when there's different ways it is disclosed, certain states have different disclosure requirements, and when that happens, it often provides confusion to the consumer at the origination of the level.

MR. OLSON: Judy, you talked about changes in HOEPA that -- and some of your suggestions I think implicit in that were that maybe -- in the 2002 HOEPA definitions that there were types of fees that may play into pricing that HOEPA doesn't include. And perhaps the market has changed. Are there definitional problems with HOEPA or isn't that -- wasn't that the point that you were making?

MS. ZEIGLER: No. I think what we were looking at was trying to have predetermined certain fees that you can't go over so that you would not have a prepayment penalty, for instance, longer than three years.

I experienced in my marketplace -- for instance, I had an older lady, in her mid '70's, retired and widowed, who had done a refinance on her home. Was aware that she had a prepayment penalty, but what she wasn't aware of was -- and we purposely scheduled the closing to be 30 days after the original loan was taken out.

What wasn't explained to us, or to her, or she didn't remember -- and I did not do the refinance because I was the realtor who sold her the home. She refinanced on her own three years later and then another three years she's buying another property.

What happened was her prepayment penalty was not really a three-year prepayment penalty. Because you pay interest only -- okay? You're paying in arrears when you're first paying -- she ended up -- it was actually --

MR. OLSON: It was a negative am mortgage.

MS. ZEIGLER: No. It wasn't a negative am. It was when you close the loan -- let's say you close on June 1. Your first mortgage payment is on July 1. You're paying interest from July 1 back. But then you pay the principal up front. So if she would have closed two days into the month, she would have paid for two days and then interest back.

Okay. So when she went to close, it wasn't really a three-year prepayment penalty; it was three years and four months. Don't know how the lender put that in. You know, I tried to fight it through our local state senator for her. Nothing we could do. She just -- she just decided not to pursue it. She was -- she had income. It wasn't a problem for her. But I really felt that she was being taken advantage of.

And I think that's what we're looking at, is trying to narrow some of these things down so that they're much more clear to everybody when they get into something. That it wasn't just a 36 months; it was actually in this case 40 months.

MR. OLSON: Other people have questions? Jack, we'll start with you this time if you want. You know, we actually -- this is pretty remarkable. In Philadelphia somebody actually raised their hand who was on one of the panels. Other than that, it's been pretty much a free-for-all up here. Jack has sharp elbows I'm sure by the end of the day here.

MR. RICHARDS: I'm getting much more aggressive.

I don't even know if this is a fair question, but when I've bought real estate in the past or refinanced a loan, I've had varying experiences with title companies in terms of the title officer going through the terms of the documents and some would not.

Just particularly, Judy, in your experience as a realtor, do you find that title companies on a regular basis that the officer might get involved in working with the borrower to understand the loan terms or is that a -- is that really up to the individual?

MS. ZEIGLER: I believe it's up to the individual, plus it's also regional. I presume you went with -- you're not from this area, so you would be going to like a title --

MR. OLSON: Jack is from this area.

MS. ZEIGLER: Oh, you are. Northern California, though? Okay. In Southern California we use escrow companies. You were using a title escrow company. So it was the same thing? Okay.

Where we are depends upon who you sign your loan documents with. Most of the time you're going to sign with the closing agent, escrow officer, or the title escrow company. And it really is individual as to how they go through it. There are certain things they're supposed to go down line by line by line, but you wouldn't really know that if you didn't know what they're going to do.

Sometimes the lender goes through and does it where we are because -- I have, for instance, a lot of clients that are from out of the area, that they're getting a loan with a lender in Los Angeles, for instance, and they're buying a second home in the desert. They may well do the loan documents there.

It seems to me sometimes if people have had a good experience with a past lender, they'll go back to that person. Whether they've explained it or not I don't know because I only know after the fact.

If it's certain -- if they're not using a lender of my choice, I'm not as involved in it as I would be when I'm suggesting, let's say, three lenders that I've worked with in the past who want my business back because they know my partner and I sell 80 houses a year and they're not going to really damage our clients because they want to keep our business.

There's a difference than if you go, as you were saying, Heidi, to someone that they met at church whose sister is a mortgage lender.

MS. GAY: Can I offer just one -- I think Judy is very right, personally and professional.

Personal. I did it by phone, my last refi. Nobody talked to me about anything. They shipped the docs to my house, I had them notarized, sent them back.

Professional. Most of the community development financial institutions that offer anything similar to this full-cycle lending model that I mentioned -- there's hundreds of groups doing it across the country now. We're also a full-service realtor at NHS. And so what we see is that those groups tend to spend the time, because, again, different profit motives to some extent, spend the time with the consumer. I require closings at our offices and we have multiple offices to facilitate that.

What you really see with the nontraditional mortgage community, and particularly if you're on the purchase money side of the market, with layered financing, you have government involved -- and watch me now. There may be four or five closings. So we're then called upon in the nonprofit community to try to show up to those and try to explain everybody's documents, which is frightening. So we tend to coalesce it all and spend our time then working with the consumer toward one closing.

It is very difficult. And we don't -- and we then work with title and escrow, try to cross-train them, you know, because when you get into multilayered financing on the purchase side, it's complex. You've got different deeds of trust, you've got different restrictions, covenants, you know, shared equity. It's complicated now.

And this is what we meant about, you know, consumers really don't have a chance is what I'm saying in terms of having a grasp of what's going on in the mortgage market right now.

And on a personal level when you look at it, you can do stuff by phone, ten minutes and they ship you your docs. Someone asked me -- and I'm honest like this. And on the public record -- exactly what my terms were on my home loan last year. And I had to really think because I could not recall. And I think that that's a challenge. And I'm in the business.

So if a typical consumer is faced with the bombardment of advertising that they receive and they have all these players Michael mentioned that they can talk to to try to get a loan, it's just too much.

MS. BRAUNSTEIN: I'd like to talk a little bit more about shopping and how consumers, especially in the lower income minority community shop for mortgages. We had a panel on this in Philadelphia. And one of the things that we heard -- we had a lot of discussion about push marketing and that in particular the brokers were doing that.

We had a woman on the panel from National Council of La Raza, Janis Bowdler, who talked about the fact that they did kind of a maybe unscientific survey but they looked at newspapers and media and listened to radio that were geared towards the Hispanic community, the Latino community. And basically all that was being advertised were subprime products, both in the -- in both ends of the media, both the radio and newspapers.

And I'd like to hear some comments on what can be done to possibly get more prime products, you know, pushed into these neighborhoods.

And how do people in the neighborhoods you work in, Lori, when they want to get a loan, how do they -- do they go to the places that they see in their newspaper and hear about on the radio? You know, how do they make those kinds of decisions?

And lastly, I was just wondering, you know, you see lots and lots of advertisements on TV now about these Internet providers, like Lendingtree.Com, where you enter your characteristics and supposedly, you know, 12 people ring your doorbell, all competing to give you the best possible loan. Is that truly only something that happens to prime borrowers or is that a useful tool for the markets that you deal with?

MS. GAY: I'll go. I'll start with your last one, the Internet use piece. We have a digital divide -- I don't always like that language but it's -- everybody understands it -- in a lot of low to moderate income communities across the country. Even though I've found now that seniors use the computer a lot more than other people I know in their free time when they can get access. And this is where we see then a proliferation of certain kinds of products targeted towards the aging population.

We are one of the few supporters I've found in the nonprofit community of some components of the reverse mortgage business and we're certified to counsel people in the use of reverse mortgages. And a lot of the seniors, just as an example, who come to see us who are low to moderate income and ethic minorities are using the Internet to find out about those particular products. And that's been an intriguing piece for us to observe.

We're on average counsel -- we stopped at 100 customers a month. We could easily do 500 customers a month in L.A. county. We're asked to do it all the time. And the challenge we've got with that particular whole piece is phone counseling is not one of the best mechanisms we found to encourage people about their options.

So the Internet is actively being used. And I would say based upon some age grouping we're seeing that. We have a lot of young people who are coming to us to buy homes, back to the other side of the marketplace, and they've used the Internet to look up credit cards and so forth and then they link to some of these sites you're talking about.

And when they come to see NHS, they've already got weird debt ratios because they've been using credit cards wrong and they have student loans and, you know, it just layers from there.

And so the Internet is more at play than we probably give it credit for in low to moderate income communities across the country, regardless of the digital divide.

The other thing I'd say is that --

MS. BRAUNSTEIN: Lori -- I'm sorry -- is that a good thing or a bad? Because the way it's portrayed, it could be a good thing that people are competing for your business and you get a better deal.

MS. GAY: I don't think people understand how to get a better deal would be my response to that. I think they're getting into a lot of stuff is what we see on the counseling side that's not necessarily good and that a lot of the web sites as it was mentioned earlier are very sophisticated and you don't necessarily get all the information you need up front to make an accurate or informed decision.

What's good about it is it gets them thinking about product options and that I have choices and that maybe there's a world out there that really wants to lend to me. That is not always been the message in low to moderate income communities of color. And I think that -- so there's some power in the Internet.

I read this morning about Bill Gates kind of stepping down and spending his time in philanthropy. And I cried, and that's me, because I'd love to see that, not just because he's a technology wizard.

But one of the things that I have an obligation to in my work is a sense of personal responsibility. I am personally responsible to care for people and to get messages out that inform them about making wiser choices about money. And I think that anyway that we can do that, whether it's the Internet, through print, through cable television, through radio broadcasts, we should. Technology is adjusting so fast. We now have I-Pod webcasts. I have no clue what that is.

So I think there is a whole bunch of stuff that's out there that we could utilize more aggressively to make sure that consumers are more financially literate and the Internet should be an aggressive tool for that.

The LMI customer response piece that we tend to see across the country, and certainly in L.A., is very much a print-related response and a radio-related response. We avoid television at all costs because it is the best mechanism for response but it's not the best quality customer.

And so in our work -- our name happens to be a very warm brand. Neighborhood Housing Services does not offend anybody. It's attractive. That's nerve-wracking because, you know, we -- we had 3,000 Korean families walk into our lobbies a couple of years ago from one TV spot, in a ten-day period. And no one on our staff spoke Korean. Frightening. All low income. Twenty-nine hundred credit reports we ran. I think Sandy knows this story. All the FICO scores above 700. Every family needed a stated income loan, though, because of the types of businesses that they were running.

So I think that families of low to moderate income respond well to certain types of advertising. They're very trusting in general of certain types of brands. It is not the bank. That's typically not what they're interested in.

So when we partnered with Wells Fargo to do a mail drop to 100,000 households of a postcard, we got 10,000 calls. And they called NHS's number, though, not Wells Fargo's number. So that's not a reflection on Wells Fargo other than that brand wasn't as trusted in those neighborhoods as Neighborhood Housing Services, who they didn't know but we felt comfortable.

The final thing I'd say on prime product, how do we push that more in the neighborhoods? I got a debit card in the mail the other day from a subprime lender. It happened again, Kevin. So I have to get bad and mean with this subprimer. I can put a second mortgage on my home with a debit card by buying an ice cream. That is frightening. And those are some of the products that are offered right now.

Prime product is critical in the neighborhoods. There are lots of families who are getting the wrong product, wrong house. And once they've got the home, they're overwhelmed with those kinds of offerings. I get three checks a week in the mail.

So I think that anything that can be done relative to regulating some of that will be powerful. Families do not know how to make those choices when faced with those opportunities.

MR. FAUST: Just an industry perspective on how consumers tend to shop for loans. It's interesting you say that digital divide, because a lot of way people tend to shop for loans is socioeconomically driven. If they've got the means, they've got the time, they will surf the Internet and collect a vast amount of information, so when they actually show up at your office, they are loaded to bear with terms and concepts and, I mean, they're ready to go.

However, you take the other end of the spectrum where a person is working three jobs, trying to make ends meet, the reality is their shopping method is a little different. So it tends to be convenience driven.

Now, they all may actually generate the same amount of income as the person that works that one job that has the economic capacity. But the reality is when they go to get a loan, they often do it by referral, friend, family, member of the church.

One of the things the brokers do is we're in the community. We tend to be the community home loan exert. Mortgage brokers are people who tend to work by referral. Want to make sure I do a good job for you so that you'll send -- you know, you'll refer your brother, sister, cousin, et cetera, to me when they say, "I want to buy a house." Tends to be relationship-based. It goes to direct mail-based or massive marketing, key and pain driven-based.

I'd like to address the Internet question about the, you know, post your application here and you'll get 12 great people knocking at your door. Those tend to be companies that are in the -- it's called a referral mold. And the way that works is essentially they put those applications, credit reports, all that out there for people to buy the lead.

So it's mortgage bankers, mortgage brokers, whomever who is actually going to originate the loan, pays for an opportunity to take a peek at the consumer. And if it's something they can do, they will -- they will call and they'll get in the bidding mode.

But the reality is they're not making the loan. They're referring it out to multiple other people who get the opportunity to take a peek at a person's employment history, down payment, credit, et cetera. And then get into a --

MS. BRAUNSTEIN: I knew that. That's why I wondered does that mean -- are people really getting better deals by using those services? That was my question.

MR. FAUST: I can tell you I just love when a consumer calls and says, "I sent an application with Blank.Com." Because I know, you know, 95 percent of the time we're going to be able to give them better terms and rates.

MS. GAY: That's right. Absolutely.

MR. FAUST: I just love when I get that phone call.

MR. CHANIN: Judy, let me follow up on this notion of shopping. And from your perspective, if it varies by ethnic group, if you could explain that.

If a consumer comes to you and they either have picked out a house or are looking for a house, and you take them through that. Take me to the stage of where they have to get financing. What is your role and do you assist them? Do you find most consumers come with a lender in mind or a broker? How active a role do you play in that process?

MS. ZEIGLER: In my particular business very active. I usually don't show people property until I know what they can afford. If you start showing property -- and obviously they're going to like more expensive ones rather than less expensive ones because they'll have more gingerbread on them and things that they'd like. And then they can't afford it and then they're disappointed and you can't find them anything in their price category. I'd rather start lower and then work them up and show them what they can get if they want to make higher payments.

I usually recommend three lenders. My partner and I have a list of approved lenders that we have worked with.

When Lori was talking and Michael about the Internet lending, for instance, I have yet to close a loan with a client that is a purchase from an Internet. I have had the experiences that have not been great, where these poor people come to closing -- well, I can say I had one that closed, at a huge difference of what they thought they were closing at.

What I think is needed, especially with a first-time home buyer, I would never recommend that. I think you need to go in and you need to sit face-to-face and that person on the other side of the table can look -- look them in the eye and say they're either getting what I'm saying or they have no clue and I have to start over again, whether it's English, Spanish, whatever it is. They don't -- you know, you get that deer in the headlight look and you have to start over again.

And because I've been in the business 28 years, I've started with my clients and probably prequalified them a little better than some agents that just, you know, jump in the car and shop.

I believe, though, it's interesting with the Internet, going back to that one a second, with the seniors. As you said, they have more time.

MR. FAUST: She said that.

MS. ZEIGLER: Well, in the beginning, people didn't have the -- seniors weren't on the Internet that much, they weren't shopping that much. But they have found if they want to talk to their grandchildren, they'd better get on the computer or they won't be talking to them. So we have many -- many of our clients are very tech savvy that are seniors and retired that never used a computer in their business but they're using it now.

What I've had is that if they want to do a loan application on the Internet, I have asked them -- and I have several lenders that will do it at no charge -- double app so that when we get to closing you know it.

Often times you start with a lender -- and in our area we also have Indian lease land, which throws another wrench into it. So you get to a closing and these people think they're going to close and all the sudden the lender calls and says, "What do you mean there's a land lease?"

Now you have the seller that's got the moving van, the buyer has the moving van, and there's dominoes with people moving and they can't close because this lender doesn't do leased land.

So there's a big difference in lenders, just like there is everything else. And I'm sure there's great -- it's just a different business model. And I'm sure it works for some people.

And I would think with a refinance, it would not be a problem because you're already in your house. And if it takes another 60 days, you can do it. But if you're trying to move for a deadline, it's been difficult, at least in my experience.

MR. CHANIN: Let me follow up in terms of nontraditional mortgages. So you've either prequalified someone -- what types of individuals get those products? Are they people who seek to buy a larger amount of home? Are they people who seek to minimize their payments? Are there any trends or are -- things that you see in terms of those individuals that get those option ARMs or interest only?

MS. ZEIGLER: In my experience, it's been people that can probably afford to pay cash but they're doing it just so they can write off the interest income.

MR. OLSON: Expense.

MS. ZEIGLER: Pardon me?

MR. OLSON: Write off the interest expense, right?

MS. ZEIGLER: Right. Write off the interest expense. So it's a tax write-off.

MR. CHANIN: Maybe income. May be that wealthy.

MR. OLSON: Well, you never know. Sometimes we have somebody from the IRS. If somebody is writing off interest income, they'll --

MS. ZEIGLER: No, I misspoke. But they need the write-offs. And especially if they're retired, they're not getting as many write-offs as they used to when they're in business, so this is one product that works for them.

Also, in second homes, many of them are going to be in it for three to five years as a second home. When they turn it into their retirement home, whether they stay there and refinance or whether they pay it off because they're going to sell their home in Michigan and retire where we are, that's an interest.

I do have one client, for instance, going through this now. He's 55 years old, first-time home buyer. His FICO score is in the 800's, but he doesn't make enough income to qualify for certain things. He is engaged, and in the next few years, he'll be in great shape when she's done with her schooling and she'll move in and she'll start paying with him on the mortgage. So in this case, you know, they're going to go with something that would be a nontraditional product.

MS. GAY: Can I offer that in a lot of load in my communities, it's the nontraditional because I want the house I've seen on my way to work. And even though I was told by NHS or some nonprofit that I might need to wait a little bit, the broker told me because I have a 750 FICO score I can borrow 200,000 more dollars. We see that all the time.

And then people are asking to marry it with the individual development account money that I might have been helping them with. And so that's where we see problems, is when you then want to utilize subsidy along with nontraditional mortgages that may have been intended for some other person or some other purpose.

And I think that the microwave approach is bad. And families who are pushing to get in at no matter what the cost, as quickly as possible, is not a safe opportunity.

MR. FAUST: You know, one of the things I think that we -- we need to make sure that when the consumers are shopping, the people they're working with are professionals. And part of that means pre-education. That also means continuing education. That means criminal background checks.

In many, many states like California, there's three different licensing schemes that have happened in this state. You know, mortgage professionals can work -- and that's three just under California. That's exclusive of all the federal opportunities that exist as well.

In California you can be a real estate licensee. There's about 450,000 real estate licensees that could do a loan. At least they have pre-education, continuing education requirements, they have a background check.

There are about 3,000 CFL's in the state of California, a little more than 3,000 CFL's. The corporation is licensed. The individuals who actually originate the loans may or may not have any pre-education, any continuing education, or any criminal background check. And many of those mortgage bankers will say, "We do criminal background checks." You know, it's incumbent upon the government to make sure that if they're doing that, they provide in some way, shape, or form.

You talk to the District Attorney's Association, State of California, as well as the local prosecutors who are the ones that truly carry the water on going after predatory lending throughout the country, and what they'll tell you is that the people who tend not to have any pre-education, any continuing education, any criminal background check, they're just moving from state to state, you know, exploiting the systems.

So I think that when you get down to draw your regulations, make sure that everyone adheres to the same standards on pre-education, continuing education, you know, and make sure they have a criminal background check.

Because yeah, there are bad actors in the industry that will tell them, you know, "Oh, yeah, you got 750 FICO, you can buy the house." But if they're doing that in a fraudulent manner, it's incumbent upon the government to enforce the laws we already have.

There are a lot of statutes on the books, both federal, state, and local, that already address loan fraud. The reality is you ask any DA, they'll tell you they're up to their gills with usually one person who is in charge of enforcing all the white-collar fraud that goes on, whether it's mortgage, credit card, or whatever.

If there's nothing else that came out of these series of hearings and it was the Fed to drive the ball across the goal line to make sure there was adequate funding to enforce laws we currently have -- that includes advertising, deceptive practices -- if you guys did nothing else besides that, I think everyone in this room would give you guys a huge round of applause and know you truly did something, didn't just play around in the fringes.

MR. RICHARDS: Michael, in your opening comments, one of the other things you mentioned was the need for uniformity when it came to alternative mortgage products, uniformity in terms of documentation disclosure.

MR. FAUST: Sure.

MR. RICHARDS: Could you expand a little bit on what you believe -- you believe uniformity would look like?

MR. FAUST: Well, first of all, I think you need to make sure that whether a person is a broker or a banker, they're not having to use different forms. Many states have their own regulatory schemes. They require brokers to provide this set of disclosures, you know, bankers to provide this set of disclosures.

So when Joe Consumer goes from place to place to place to shop, he ends up -- first of all, every disclosure packet is, you know, anywhere from 20 to 50 pages long because everyone is either trying to comply with every state law and/or prevent from getting, you know, sued for something that may or may not have anything to do with the transaction, but also ensure that the forms that are created --

I mean, let's look at the truth in lending form just for a second.

MR. CHANIN: Let's not.

MR. FAUST: Let's do. I mean, let's be honest. You got that nice little four boxes across the top. There's that one box that says "Finance Charge." Well, that was great when you had a choice of 15-year fixed mortgage or a 30-year fixed mortgage.

Now let's take it to the option ARM. Okay? I mean, if someone paid essentially the 15-year payment, the amount financed would be one number. The fully indexed 30, that's a different number. Interest only, potentially that's a different number. And when you get to neg am, especially if the thing recasts somewhere down the road, that's a completely different number.

The forms that you have, while adequate under what we would consider traditional products, I hate to say it, don't even come to the minimum line. You look at stuff that's in there in the good faith estimate, you know, principal and interest, all still on one line.

I mean, the reality is in California we do a lot of loans that are interest only because the consumer wants the choice. I mean, option ARMs are a good product for some consumers. You know, commission-based employees have what I heard referred to earlier today as lumpy income. Some months you make money, some months you don't. You need that option of flexibility.

You know, the reality is disclosures need to be the same no matter what distribution channel it comes through. You need to make sure there's a special information booklet that -- and it's updated regularly, not updated every six to ten years. It's something that's updated on a regular basis to address terms. And you need to make sure the charm booklet is up-to-date on nontraditional products. You know, part of this is making sure those things are included in the up-front process of the loan disclosure process.

MR. RICHARDS: Thank you.

MR. OLSON: Heidi, did you have a comment?

MS. LI: Yeah, I just want to follow up and respond to what Michael was talking about, which is I think he's actually touching on something that's very much speaking to the heart of this issue, which is what is meaningful disclosure, especially when you have these nontraditional, exotic, interest only, option ARM products.

For example, if you have, exactly as he was pointing out, you have someone who comes in, isn't very sophisticated as a consumer, and just gets the written TILA boxes of the TILA notice, and it's in English and perhaps also that's not the language in which they were actually conducting the whole communication with the broker or lender with, how are they going to know that ultimately when they go to the closing that they picked option number one, option number two, option number three, or option number four, and what each one of those really consists of?

I mean, to me it seems like so either there needs to be that -- at least the minimum I think he's suggesting is some additional required disclosure requirements for these nontraditional products in writing, in a written format that is really meaningful to the particular consumers that are getting them.

And I would really say those types of products do need to be included under HOEPA as being covered, not just the refinance loans that we see are covered presently, and perhaps under certain interest arrangements that they're going to be getting.

For example, just the payment of some portion of the interest only option one situation, that they would be actually given really the clear indication by legal requirements that you should go and get some, you know, pre-signing, HUD-certified, impartial counseling.

And not to say that all of the folks who are in the broker industry or in the lender industry are out to get the consumers. But the problem is that I think that Lori is speaking to and I'm speaking to, the folks we see -- I mean, I think there are a lot of really educated consumers out there who really know what to look for.

And I think that's a wonderful thing to know about. And they don't really need perhaps all of these protections that we're -- or at least some of these protections that we're suggesting should be added.

But it really is this side of the consumer market that is the most likely to really have the problems with not understanding what they're getting themselves into. And I've seen now too many in the last year, in Oakland, in Contra Costa county, in the South Bay, in San Francisco, my colleagues and I, we have seen too many people who came to us, went to one of these housing counseling agencies, sat down with someone who could individually go through with them, "This is what I actually got into because it wasn't explained to me before I signed all these papers at the title company. And if I had known, I would not have taken this loan out."

There are some folks that no matter what you do, they're going to -- the dream of homeownership is just too strong. And I don't think we're trying to capture in our net with our recommendations those folks because that's kind of, you know, you're going down that path no matter what.

But there are too many that we're actually still seeing who really if they had been given a little more meaningful disclosure, an opportunity to really know what they're getting into with some of these products, I think that it would make a difference.

So I just want to say that.

MR. OLSON: Let me change the subject slightly but link two things that were mentioned earlier.

And, Lori, you made a statement that's one of the -- has been one of the most fundamental precepts of mortgage lending, which is in a foreclosure everybody loses.

As a lender, we would do almost anything to avoid a foreclosure because we did lose. It was in Minnesota. It was a year from the time that we initiated the foreclosure when we could get at the house. The lender could not gain -- could not gain a nickel beyond their costs and the loan amount. And that's true in most states I believe. I suspect it's true in California. And, of course, the borrower loses.

But a couple of you mentioned equity stripping. And something that is I think just insidious. But if the foreclosure process is now becoming an opportunity for either equity stripping or for profit taking among the players that participate in that foreclosure process, that's something that's -- at least it's new in my experience.

Judy, I think you mentioned the term "equity stripping" also. Do you find it -- did you mention it?

MS. ZEIGLER: Wasn't me.

MS. BRAUNSTEIN: No, I think Heidi and Lori talked about foreclosure scams.

MR. OLSON: So how does -- is that going on and how are you going to add those issues?

MS. GAY: My debit card scenario was equity stripping opportunity.

MR. OLSON: I mean in connection with the foreclosure process.

MS. GAY: Okay. I was going to say it's all relative.

MR. OLSON: Except the predatory side is something. But to use that foreclosure process where there presumably are a lot of safeguards for the homeowner in it to -- that's what I was focusing on.

MS. GAY: Chicago NHS for the last two and a half years has done something called the homeownership Preservation Initiative. Some of you are familiar with the data find. Fifty percent of the foreclosures in the city of Chicago involved homeowners who never called for help.

And so as they then dug underneath that data, what they found was that the -- some of the lenders involved in what they called equity stripping understood the cost of doing business before the loans were made, understood the profits they'd make, targeted specific kinds of families who were less knowledgeable, less informed, lower income, and then the same property was sold four, five, six times within that period of time, four to five years.

And so I guess the notion really becomes -- let me use a quick example. We spent some time during a merger two years ago, a bank merger process, working with a bank to help them understand a program that they offered internally to their own -- or I should say to their customers. If you borrowed money from that bank, you had the opportunity within a couple of years to refinance at no fees. Not an unusual product.

The way that they went about alerting the customer to the option to refinance -- because there was a trigger.

You know, it was an ARM type deal. There was a trigger that the loan would be more expensive and you could refinance if you paid in a timely manner to a lower cost fixed rate loan.

The way that they alerted the families was with a letter in the mail. And they had 14,000 families they were alerting who fit this profile in the year that they had me review.

And they said, "Only 400 people responded to our letter." And I said, "Well, did you call? Did you send more letters? I mean, what did you do?" And they said, "Well, no, we just responded to the 400 and then only 40 of them --" so we went from 14,000 to 400 to 40 "-- participated and actually took on the fixed rate loan."

And I said, "Well, how's that working for you? Doesn't it strike you that something is wrong with that process? Because the other 14,000 or 13,000 and some change that went into a higher rate priced product," I said, "somehow in there that doesn't win for the customer. And you, in effect, don't really give them the option of converting because you didn't make any effort toward helping them understand what was really going to happen. All they know is they then got the payment notice and it's, you know, $100 more a month."

And so in our world, as we talk about equity stripping, it shows up in a lot of formats is all I'm trying to say, whether through foreclosure and there's a tactical strategy to continue to target the wrong people with the wrong house, wrong price, and that happens, and/or whether it's through its existing product and that product is available to people who make not the best informed choice, and then there's not the information disclosed to them to let them know that there are other options available.

Clearly in the foreclosure process, as we all know, the sophistication shows up in that, you know, homes in certain areas are more likely to be foreclosed upon because of the types of loans that are made in those areas.

Our foreclosure study that we did with the Joint Center for Housing Studies at Harvard a year ago showed that in the neighborhoods where the foreclosures were happening in L.A. -- we call them hot spots -- at seven times the rate the rest of the county, in those neighborhoods subprime lending was 85 percent.

I'm not mad at all subprimers. Bunch of them are my friends. But I want the prime rate market to be more available in those neighborhoods. Because one out of four of the loans that were originated ended up in foreclosure. And so somehow it just wasn't the right placement.

And the stripping then that goes on in an appreciating market is if, in fact, those families keep borrowing with the wrong product, you're just never going to gain -- there was a statistic I reviewed last night that said something like certain types of subprime loans cut the equity in a home by 50 percent in the first five years. And so the stripping mechanism can sometimes just be product placement. And I think that that's where we need to show up.

And I should say this so we're on record for this detail, that the National Home Equity Mortgage Association has a borrow smart curriculum that we deem as viable and that we encourage consumers to review, both on line and in print and in class -- there's three ways to get access to it -- that they created to encourage consumers to participate actively in understanding what they're borrowing.

MS. BRAUNSTEIN: Heidi, before you respond -- and maybe I misheard your question. But I know that in Chicago, Bruce Gottschall was on one of our panels. And, of course, he runs the foreclosure program in Chicago. But one of the things he talked about -- and that's what I thought you and Heidi were alluding to in your opening comments -- was that there even were more insidious things going on in some cases where people would start in the foreclosure process and some people actually would go to seek help and that there are had been companies set up and -- set themselves up as to help you through foreclosure and those were the folks that were coming in and -- and I thought that's what you were asking about.

We know about the stripping that goes on because of bad loans and stuff. But this was actually people who were trying to get help to do work-outs and not -- and pull out of foreclosure, and that companies, if they didn't go to the right people, all of a sudden they lost their home and this person that was supposed to be helping them is the one who made them lose their home.

And so -- and Heidi was nodding maybe. Is that what you were talking about?

MS. LI: Yes. In addition to what you had just spoken to just now, Lori, I mean, that's what I was referring to earlier in the opening. And really this is an increasing problem.

I mean, the National Center -- Consumer Law Center just put out a report in the last two years that looked at this problem of foreclosure scams and detitle theft throughout the country.

And I think that one of the things I want to make mention of was that here in California, we are at least on that level one of the states that actually has some legal protections at the state level to try to help protect those folks who they basically -- they are a homeowner. They've owned their home say for five to ten years or more. They have a fair amount of equity in the home.

But because they're a senior, because they may have other reasons why their income is now suddenly limited or has become limited, they start to go a little bit into distress with keeping up with either a current mortgage payment situation or they may think that they need to take out some sort of financing assistance to help with hospital bills, some other obligation.

And what happens is there's a very aggressive market now of these folks, these businesses that are presenting themselves as foreclosure consultants and/or financial consultants. And they're basically going ahead and sometimes knocking on the doors, especially if many of these homeowners -- in certain communities they're doing a lot of aggressive advertising, calling.

And what we're finding is that folks who are maybe again not the most sophisticated or even a little uncertain or distrustful of other options because they don't know that maybe they exist or they're not well placed in their communities, prime lending options, they go ahead and start to go through a process where they think they're getting a loan and they're not.

So here in California we have a Civil Code section 1695 and another -- it's called a Home Equity Sales Contract Act. And we also have an accompanying Civil Code section that's called the Mortgage Foreclosure Consultant Act where if a certain type of process is not gone through as far as certain written disclosures about what the purchase loan --

If it's a purchase contract actually involved versus an actual refinance loan, that there's a certain number of days in which that homeowner has the opportunity in which to be able to review that now contract for sale which they've been told is not a sale contract but a loan contract and also be able to cancel it.

And they also are given certain rights to go ahead and be given written notice of how they can go about the cancellation process. If that doesn't happen, they're entitled to actually up to three or possibly four years after that transaction seek to undo or cancel that sale of their home. And that's what we call an equity purchaser situation where there is an unknowing equity seller. So we see that.

And also in California we have Civil Code section 1632, which I think is a very useful model perhaps for federal purposes to look at as far as giving disclosures in writing, at least some of the key loan disclosures to folks, in the language of the transaction if it's not English.

MR. OLSON: Kevin referred to that.

MS. LI: Yes.

MR. OLSON: I think Leonard has a --

MR. CHANIN: One final question. We're committed to, as Michael suggested and Heidi, to reviewing regulations and disclosures. That's a long-term goal with consumer testing and the like.

MR. FAUST: Good luck.

MR. CHANIN: We will need it.

But one of the things I'd like your views on is are we still in the paper world? That is, in terms of your experiences with consumers and looking at, reviewing information, are paper documents still the way that consumers best are likely to review the information, understand it, or is it possible to push consumers toward the Internet or towards DVDs, any other means of trying to better communicate with consumers?

MR. FAUST: I think the answer is all of the above. I mean, I hate to say it. I mean, you've got -- you've got everything from, you know, paper tigers to E tigers that they'll tear it up no matter which way you go. But you've got to have it all.

I mean, it's like some consumers that want to fill out the application on your web site. They don't want to come visit with you. These tend to be more sophisticated, you know, people that are extraordinarily tech savvy.

I live and work in the Roseville area. Let me tell you, a guy that's 30 years old working at Intel, he doesn't need a piece of paper. But he's very comfortable on line. You still have to make sure the disclosures, though, are there in paper. I don't think you can, you know, give up one for the other. I don't know.

George, what do you think?

MR. HANZIMANOLIS: That's my sentiments exactly. We have -- within my own company, we have a web site. We get a lot of applications on those sites. And like Michael says, some of those people are very comfortable filling out an application and doing things long distance like Lori did with her last refinance.

However, in the large majority of the cases, it's followed up with a face-to-face. So I think the customer likes that we'll do the DVD by mail, they can apply on line, but in most cases, it's followed up by a face-to-face so we can sit down and really make sure they understand the process as they go through.

So I don't think we'll ever do away with the paper part of that.

MR. OLSON: Well, thank you very much, panel. Very useful and we had -- I think we're -- the convergence of opinion from group -- from people that represent very differing points of view I think indicates that there's an underlying presumption that the mortgage market on balance contributes significantly to what we think is positive societal value and we're all trying to focus in on how we can make it better.

Thank you very much for your participation.

We'll be back here at 1:30. We have one more panel.

If you would like to speak at 3:00, please sign up outside so that we can call on you. Thanks.

(Whereupon a lunch recess was taken.)

MR. OLSON: It's 1:30 and we would like to get started.

First of all, it's Friday afternoon and the sun is shining and it's gorgeous and you folks are in here. So everybody gets a certification of appreciation for being good enough to stay here during the -- on a Friday afternoon.

The sole exception to that will be me. I'm going to be leaving here right at 2:00 to catch a plane back to the east coast. I will hand the gavel to my esteemed colleague here, Sandra Braunstein, Sandy Braunstein. As the expression goes, and you will be in very good hands from that point on.

We will continue with the same subject but with I guess a more specific focus and this time particularly on the reverse mortgage product. And we will have -- we'll go in the same format. In other words, we'll ask each of you for a five-minute introduction of your topic.

Peter indicated to me during the lunch hour that it's very difficult for him to compress his thoughts to 45 minutes, so this is going to be a real challenge. But I think it's clearly an introduction to the topic. But it's in the dialogue that so much of the real public policy issues get addressed.

And we again have a timer who will notify you as to the -- give you a one-minute notice and then a time is up. And we will also continue to go from left to right.

And we'll start, Ruth, if you would identify yourself, your organization. And you have five minutes.

MS. ROMAN: Thank you. My name is Ruth Roman. I'm with the Department of Housing and Urban Development in Washington, D.C. Governor Olson, thank you for the opportunity to testify on the Federal Housing Administration's Home Equity Conversion Mortgage program.

The HECM program launched in 1989 was designed to meet the special needs of elderly homeowners by insuring mortgages that turned their home equity into cash in a safe and affordable manner. The program has been tested for 16 years and has proven to be a success story and a model for the private sector.

With over 43,000 loans insured by FHA in fiscal year 2005, the HECM product has experienced tremendous growth over the last several years. There has been an increase of more than 200 percent from fiscal 2003 when FHA endorsed just over 18,000 loans. We're projecting another increase in loan volume in fiscal year 2006 to approximately 60,000 loans.

Today HECMs continue to be at the forefront of the reverse mortgage industry, representing approximately 95 percent of the business today. The product is less expensive than other reverse mortgage products, providing higher cash proceeds to borrowers and offering unique consumer protections.

This afternoon I'll provide a brief overview of the HECM product and mention some proposed legislative changes that are now being considered in congress.

The HECM product provides a number of benefits to seniors. There are no restrictions on how the proceeds from the HECM loan could be used, no repayment is required as long as the HECM borrower remains in the home. Unlike a traditional mortgage, there are no monthly principal and interest payments. The lender pays the senior.

HECMs are also nonrecourse loans. The borrower heirs will never owe more than the value of the property, even if that value has declined and the loan balance is greater than the loan's appraised value.

In order to be eligible for a HECM, a senior must be 62 years or older, own their home free and clear, or have a small remaining balance that can be paid off with the reverse mortgage. They must occupy the property as a principal residence and not be delinquent on any federal obligations.

Eligible properties include single family homes, town houses, condominiums, manufactured homes, as well as two- to four-unit developments that are owner occupied.

The HECM program has no income asset, employment, or credit requirements. And an appraisal is required to determine the value of the property and ensure the property meets FHA standards.

The amount of money a senior can receive from a HECM depends on several factors, including age, appraised home value, the location of the home, and current interest rates.

The HECM program is extremely flexible, offering seniors five payment plans, options that permit the borrowers to draw funds on a monthly basis, in a single lump sum, through a line of credit, unless some tap funds is needed, or through a combination of these methods. The senior can easily change payment plans at any point in time.

The standard cost of a HECM include an origination fee, a mortgage insurance premium, third-party closing costs, a servicing fee, and interest. In most cases, the fees and costs may be financed into the loan, so a senior incurs little out-of-pocket expense.

All seniors contemplating a HECM are required to receive counseling from a qualified HECM counselor. The purpose of the counseling is to ensure the senior understands the product's complexities and costs and are aware of alternatives to a HECM before making a financial commitment.

The HECM becomes due and payable when the last surviving borrower dies, sells the home, or permanently moves away from the home. The mortgage can be paid with or without the sale of the home.

If the heirs want to keep the property, they can obtain a traditional mortgage to repay the HECM. If the property is sold and the home has accumulated equity beyond what is owed, the difference is kept by the heirs. If the loan balance exceeds the value of the property, the heirs will owe no more than the value of them. FHA insurance will cover the balance due the lender.

Although the HECM program is a great success story, we at FHA recognize there are areas for improvement. We are working with the reverse mortgage industry to address some areas of concern.

For example, we are working with the AARP foundation to improve the availability of quality counseling across the nation. AARP has played a critical role in training HECM counselors and providing them with tools and information to improve their efficiency and effectiveness.

In addition, FHA supports a bill pending in the U.S. congress, HR-5121, the Expanding American homeownership Act of 2006. HR-5121 proposes to eliminate the cap on the number of HECM loans FHA can insure.

The bill also proposes to increase the loan limits for HECM to a single national loan limit set at the conforming limit. Currently the HECM program is tied to the FHA 203B loan limits which have the effect of restricting the home equity seniors can tap.

FHA is also proposing to expand the program to permit seniors to purchase a home with a HECM. Today these seniors can purchase a new home and then take out a HECM in two distinct mortgage transactions with two distinct sets of costs.

Passage of HR-5121 will permit FHA to offer HECM products to purchase a home or tap into the home equity with a reverse mortgage in a single transaction.

In closing, all of us at FHA appreciate the Federal Reserve's interest in the HECM program and thank you for the opportunity to testify.

MR. OLSON: Thank you much very, Ruth.

Arthur.

MR. AXELSON: Yes, I'd like to thank you all for having me here. I'm Arthur Axelson. I'm a partner in the law firm of Reed Smith, located in the Washington, D.C. office.

And I represent a number of reverse mortgage lenders, service providers throughout the year since I represented some pilot lenders in 1989 when the HECM first came out.

I have been asked to speak about Fannie Mae's Home Keeper product, which is Fannie Mae's proprietary product. While Fannie Mae is a client of mine, I want to make clear that I'm not speaking on Fannie Mae's behalf. I'm here as a private citizen.

The Home Keeper, as I said, is Fannie Mae's proprietary reverse mortgage product and it was an alternative to the HECM that Fannie Mae developed back in 1995 -- right now it really is only a minimal share of the market -- I think it's about two percent of the market share. Because it's hard to compete with the amount of proceeds that the HECM provides to consumers.

Originally the Home Keeper had an equity share component in which the consumer could get additional funds in exchange for agreeing to share ten percent of the appreciation, an extra ten percent of appreciation with the lender.

Due to various problems and issues of unjust enrichment, if you will, if the consumer died prematurely, caused Fannie Mae to eliminate that option. And without that option, the proceeds really -- the consumer generally would get -- would receive more -- greater amount of proceeds under the HECM than you would under the Home Keeper.

The Home Keeper is set up fairly similarly to the HECM except there are only three payment plan options. Under the Home Keeper, there's a ten-year plan, which provides for monthly payments to the consumer, there is a line of credit plan in which the consumer can obtain advances in any amount they want, whenever they need it, and there's a combined modified ten-year product, which combines a monthly payment with an available line of credit reserve that the consumer can draw on.

Again, as Ruth indicated, borrowers who are 62 years old and above who own their own home and use it as their principal residence and either own the home outright or have a small purchase money balance on it are eligible for the product.

The closing costs are less than under the HECM. You have an origination fee equal to the greater of two percent of the home value or $2,000. You don't have an MIP, initial MIP cost or monthly MIP cost that you do on a HECM.

There is a monthly rate change. It's a variable rate. With the monthly rate change, that's based on the weekly average of one month CD index and there's a 12 percent lifetime rate cap.

Any consumer taking out the Home Keeper is required to get consumer education. They're required to participate in a consumer education session prior to a loan application. Fannie Mae provides a curriculum and workbook that must be used by the counselor. And generally HUD-approved counselors or Fannie Mae reverse mortgage specialists can do the training.

There is an option that the lender can provide education, but again, they must use the Fannie Mae materials and the person doing the education has to be separate from the underwriting and processing of the loan. It has to be a different employee.

Now, there are a couple of advantages to the Home Keeper. One, the Home Keeper is not -- is subject to a higher loan limit. Fannie Mae has a higher loan limit than FHA. As Ruth indicated, there's a movement to move HUD's limit up to the Fannie Mae limit.

But the Home Keeper also has an option, which Ruth just indicated HUD is thinking of adding, which is Home Keeper for Home Purchase. And this provides flexibility for seniors in if they want to relocate closer to their children or into a senior community or something like that, they can sell their home and then take a Home Keeper for Home Purchase in which they can decide how much down payment they want and how much proceeds from the Home Keeper they would want towards the purchase. And it can be paid out under a line of credit in one lump sum, which would go, you know, towards the seller of the property.

If there are funds left over that exceed the purchase price, the consumer can then set up a line of credit or a monthly payment so they can also have an income stream.

That's basically the terms of the Home Keeper.

MR. OLSON: Thank you very much, Arthur.

Jim Mahoney.

MR. MAHONEY: Thank you, Governor, for this opportunity to speak. I'm Jim Mahoney, the chairman and CEO of Financial Freedom Senior Funding Corporation.

I apologize, your briefing materials didn't make it into the book. We'll provide that later because I'll be speaking about a product.

MR. OLSON: Let me just, if I can -- and this goes for everybody -- everybody has until August 15 to provide additional supplemental information. I said that at the opening, but I'm not sure I repeated it. So that would go for all of you that would like to provide additional information for this hearing.

Thank you.

MR. MAHONEY: Thank you, sir.

Financial Freedom works in 50 states. It's headquartered in Irvine, California with four major offices. Our operations date back to 1993. And we have over 1,600 wholesale brokers and correspondents, as well as over 1,300 employees.

MR. OLSON: Can you speak into the microphone, Jim?

MR. MAHONEY: Sorry.

We are specialists. We focus exclusively on reverse mortgages. It's the only product we do. We do offer all reverse mortgage products in the marketplace. We are the largest HECM originator and servicer in the country as well.

Today I'd like to speak specifically about proprietary reverse mortgage programs that we've developed. We've developed a product known as the Cash Account, which is for homes with values in excess of the FHA limits and the Fannie Mae limits of such.

We have two plans with multiple options. That is a LIBOR-based product where the amount of money the borrower can get is a function of which option they choose. All plans, however, have no limit on home value. Indeed we've done a home with a value of $18 million, did a reverse mortgage. So it has far uses just beyond those who need it to live every day.

There are no equity sharing or shared appreciation features in the product. There are interest rate caps on all of our options. There are no maturity fees. And we also require independent counseling by a HUD-approved counselor on this product. Like the Home Keeper, it can be used for home purchase, unlike the HECM.

The Cash Account product has three different options. It's generally a line of credit, a very simple line of credit. There's no monthly tenure payment like the HECM or Home Keeper as such. But what we have done that is different is we've addressed the up-front cost issue in that we have two options that reduce the amount of cost to the borrower up front.

One is called the Zero Point, which there is no origination fee. The interest rate is the same. However, the borrower is drawing more money than the standard product.

And then lastly, the most popular portion of our product is the Simply Zero product that has no origination fee and no up-front costs. This is -- we had hoped to do this as an introduction to HUD and the other products as a way by which we can start to lower the up-front costs in the industry as such.

We also have an important feature of that product which is called the Equity Choice feature, which says you can basically carve out a portion of home equity and not have it subject to the mortgage. So you can basically preserve anywhere from 25 to 50 percent of the home equity for your heirs and for the estate.

Also would like to address servicing. Again, we are the largest servicer. We have over 90,000 loans in portfolio and $9 billion in servicing. Ninety-five percent of it is the FHA agency and Fannie Mae product and the other five percent represents our proprietary products that we've offered in the marketplace.

Many traditional mortgage servicers will say it must be easier because of you don't collect payments like a traditional mortgage. The reality of it is it's much more difficult. Customer service elements of a reverse mortgage servicing department mean you're spending a lot more time with the customer working through problems. When you're talking about a 75-year-old, that's a much different conversation than it is with someone much younger.

We do make monthly payments to borrowers, as you know, under the HECM and Home Keeper products, we also make line of credit draws, and we also basically deal with payment plan changes, which is one of the options under the HECM as such.

We perform occupancy audits to make sure the borrower is in the home. We follow up on any types of defaults due to property tax or insurance nonpayment. We monitor repairs. We also process claims for the investor to HUD and we perform physical inspections.

I will mention that we are introducing a new way to access your line of credit, which is basically to provide a checkbook and/or debit card to seniors, much like you'd use on a traditional line of credit and such.

In closing, again I'd like to thank you for this opportunity. And I believe that this is a product whose time has come based on the continuing improvements in product as well as the volume in the industry.

MR. OLSON: Jim, thank you very much.

Peter Bell.

MR. BELL: Governor Olson, thank you for the opportunity to appear before this hearing today. My name is Peter Bell and I serve as the president of the National Reverse Mortgage Lenders Association based in Washington, D.C.

A few weeks ago, the New York Times published an editorial acknowledging the importance of Reverse Mortgages for Aging in Place. To quote the editor of the Times, the financial challenge of retirement is to make one's money last while paying health care costs that inevitably increase with age. It is becoming clear that to meet that challenge, many older Americans will need to cash in their home equity.

What the Times looked at in preparing that editorial is that there are 21 million homeowners over 62 years old and that they possess $2 trillion in housing wealth. This is an enormous resource that can help many seniors live more comfortably and help control government expenditures for long-term care.

The reverse mortgage industry has been growing to better serve seniors and make reverse mortgages more widely available. Since HUD's implementation of the Home Equity Conversion Mortgage program in the late '80's, FHA has insured over 200,000 reverse mortgages. Forty-three thousand of those were made last year. And earlier this morning, I received year-to-date figures through May of this year. May was the largest month in the history of the program with 8,414 loans made, bringing us year-to-date to 48,088 loans, up 77 percent from the same period last year.

As you've heard from the previous speakers, there are three products that are active in the reverse mortgage market, with FHA, HECM accounting for a predominant market share but the Financial Freedom Cash Account growing in its use around the country.

It's interesting to take a look at what FHA brings to the reverse mortgage market. The federal guarantee provided by FHA on HECM benefits consumers in a few ways. First and foremost, it allows a higher percentage of equity to be loaned than on other products that don't have the same federal mortgage insurance.

HECM also includes numerous safeguards that are inherent in its design. Key among these, as Ruth mentioned, are the mandatory counseling, a limitation on the fees that can be charged, caps on the interest accrual, and the nonrecourse feature that assures that a borrower can never owe more than the value of their home.

The other products that have evolved in the years since HECM have basically emulated these safeguards, so HECM has led the way in creating a much better reverse mortgage market.

Reverse mortgages are getting increased attention in the Medicaid debate and more recognition as a financial vehicle to help seniors meet health care costs, a topic I'm sure Barb Stucki will address in detail in a few minutes.

Earlier this year, congress passed legislation to limit the amount of home equity that a homeowner can have and still qualify for Medicaid, limiting that to no more than $500,000 in home equity. States can override that and raise that to $750,000. This is an attempt to create a situation where people are encouraged, some might say forced, but to utilize their own resources to take care of their long-term care needs.

Legislation is under consideration in several states around the country to use -- to encourage broader use of reverse mortgages for seniors to take care of their long-term care needs.

The New York Times editorial that I referred to in my opening suggests that allowing people who use reverse mortgages for home-based care to shield some assets from Medicaid estate recovery would probably be the most important incentive that the states and the federal government can enact.

When discussing reverse mortgages, the question often arises of why not use a home equity loan if people need money out of their home or sell and move to a smaller home. There's a few answers. There's very good answers to both of these other options.

A home equity loan, of course, requirements payments on a current basis, and to seniors on a fixed income, it would be very difficult to make those payments, if they would qualify at all under the debt-to-income ratios. They would, in effect, be drawing down on the home equity line in order to make the payments back on that home equity line.

And selling and moving misses the point entirely. Reverse mortgages are for those who want to stay in their homes. Study after study shows that seniors, a large majority of seniors, prefer to age in place and stay in their homes as long as possible. The line we often here them say is they want to leave their homes feet first.

There's also a false economy involved with selling and moving. The people that say people should sell and move say it's because of all the costs involved with a reverse mortgage. Well, if you look at the cost of selling a home and paying the realty -- the real estate commission on that, the cost of buying a new home, which presumably has another real estate commission involved in it, the cost of moving, not to mention the inconvenience, those really far outweigh the cost of utilizing reverse mortgage.

Finally, a major obstacle stands in the way of growth in the reverse mortgage business. Congress set a cap on the number of loans that HUD can insure, currently at

250,000 loans. And we will bump up against that in the months ahead.

MR. OLSON: That's a great place to stop, right there.

MR. BELL: Okay. That was my last point.

MR. OLSON: And we'll have a chance to get back to you as well. We'll move over to -- how do you pronounce your -- Bronwyn. You told me before and I forgot, so I apologize for that.

MS. BELLING: That's okay. I accept any reasonable facsimile. Thank you.

Good afternoon. My name is Bronwyn Belling and I manage the AARP foundation's reverse mortgage education project which is funded by HUD and the AARP foundation.

In the 1980's, AARP spearheaded the effort to enact the federally-insured Home Equity Conversion Mortgage, or HECM program. Since then AARP and the AARP foundation have worked to improve the program's counseling and disclosure requirements, which will be the focus of my comments today.

First let me speak to reverse mortgage counseling. The single most important consumer safeguard in the reverse mortgage market is the counseling required by the HECM program.

Over the past five years, the AARP foundation's counseling project has developed a variety of tools to improve HECM counseling, including basic and advanced counselor training, a rigorous national exam for HECM counselors, a detailed protocol of HECM specific counseling policies and procedures, generic consumer information on HECM loans and other alternatives, model software for analyzing and comparing reverse mortgages, a multifaceted program of counselor backup and support, and counseling evaluation by way of a client satisfaction survey.

Homeowners counseled by a select network of exam-qualified counselors who follow our counseling protocol have given consistently high marks to this counseling. While less than a third of these clients considered themselves to be well-informed about reverse mortgages before counseling, more than nine out of ten say they were well-informed after counseling.

HUD has steadily increased the amount of funding to pay for counseling by these exam-qualified network counselors. It has also incorporated parts of the project's counseling protocol into its requirements for all HECM counselors.

In the near future, we hope that HUD will require all HECM counselors to pass the exam and build more of the protocol into its requirements for all HECM counselors.

We support HUD's efforts to obtain significantly more funding for this high quality HECM counseling, and until it is obtained to permit counseling agencies to charge clients a modest fee for counseling, if it is provided by exam-qualified counselors who follow a detailed counseling protocol.

Until reliably sufficient funding is found, however, we are concerned that lenders and agencies may be tempted to create financial relationships that may compromise the independence and quality of the counseling.

Let me speak next to reverse mortgage cost disclosures. Reverse mortgages can be very expensive. A HECM borrower at the average age of 74 with a home value equaling $362,790 or more could receive a credit line of approximately $209,000 this week in San Francisco.

The total up-front costs on this loan could be about $16,900. In addition, the ongoing monthly fees could be about $16,600. So the total cost, not including interest, could be about $33,500. For some borrowers, these non-interest costs could be even greater, exceeding $50,000 in some cases.

Consumers need to understand all the costs of these loans. In particular, they need to see the total projected cumulative cost of all ongoing monthly servicing fees and HECM insurance premiums. The method and assumptions for projecting the future dollar amount of these charges should be the same as those prescribed by Regulation Z for calculating the total annual loan cost or TALC rates. We also need to correct the way that origination fees are disclosed to avoid misleading consumers.

On other loans this fee is expressed as a percent of the actual loan amount, but on HECM HUD limits this fee to two percent of the home's value, or a HUD limit for the county in which the home is located, whichever is less.

Many HECM consumers nonetheless assume that their origination fees are two percent of their loan amounts, so they are surprised to learn that a HECM origination fee when expressed as a percent of the maximum loan amount at closing currently ranges from about 2.3 percent to 3.9 percent, which means that it more than doubles and may nearly quadruple the one percent origination fee charged on HUD's forward mortgages. All reverse mortgage origination fees, therefore, should be disclosed as a percent of the maximum loan amount at closing.

Thank you for the opportunity to comment on these matters. We will be submitting a supplementary statement, providing more information on HECM counseling and reverse mortgage cost disclosures.

MR. OLSON: Bronwyn, thank you very much.

I am now going to turn the mic and the gavel over to Sandy.

And Shirley, I guess you're next.

MS. KROHN: Thank you, Governor Olson. And have a nice afternoon.

MR. OLSON: Thank you.

MS. KROHN: Okay. My name is Shirley Krohn and I am the board chair of the Fair Lending Consortium. And this is a group of people in the greater Bay Area comprised of -- and we're very fortunate to have these people -- lenders, bankers, and credit unions, lawyers, legislators, local and state government entities, federal agencies, financial and loan counselors, fair housing providers -- let's see -- law school students who work in legally underserved communities and grass root organizations who are seeing lending abuse on a daily basis from the front lines.

We've just recently prepared this brochure. It's just come off the press, so it hasn't been made public yet. But it names the consortium members on the back and it has a toll free number that a consumer can call to find out about a good loan, where to go. And some of the information in here is about how to avoid a predatory loan.

But for today's talk, I want to go along with the subject matter and that is about reverse mortgages. Let's see.

I happen to think -- it's my personal opinion -- that a reverse mortgage is one of the most brilliant products that has ever come on the market. And I think it's really something that, like has been alluded to from everybody so far, it's going to be the wave of the future for seniors.

Peter made the comment about people living on fixed incomes, and in some cases as low as, you know, seven, $800, maybe $900 a month, and are sitting on this huge amount of equity in their homes.

Taking out a loan doesn't make sense for them because that adds another payment to an income that's probably already strained. So the idea of a reverse mortgage is very appealing.

But they're also complex and they're expensive, and I'm not so sure that lenders really do a very good job of explaining or disclosing like Bronwyn said about the disclosure, about fees and whatnot.

I think that this is a slippery slope because I think many seniors are seduced into thinking that this is a product that works well for them, but they don't know what they're getting into insofar as the cost is concerned.

And I'm hearing about some new products today that I think are very encouraging. But for right now, that's kind of the perception. And it may ruin the market a little bit. Even as much as it has escalated, there are people that probably would apply for a reverse such has been indicated if they knew more about what they're getting into.

Okay. So for today let me just spend a little bit of time talking about a bill that is making its way through Sacramento right now that will address two out of three of the issues that have been discussed through all the panels today, and that has to do with senate bill 1609. And that bill has three components to it. Like I say, two of the components address what we've already discussed today.

First, 95 percent of reverse mortgage borrowers receive counseling when applying for a HECM loan. We've already talked about that. We know about that. This leaves a remaining five percent who apply for another type of reverse product offering a higher maximum to go without counseling. It simply isn't required.

Now, that's going to change. And this is prepared notes. So I'm understanding that there's some stuff happening that is frankly good information.

Our bill requires that every reverse mortgage borrower, no matter what the product, receives counseling from a HUD-certified housing counseling agency to assist the borrower in making informed choices. The borrower would be provided with a list of counseling agencies in their vicinity, including counselors who could provide telephone counseling.

Telephone counseling is not optimum, but we have many rural areas in the state of California that just simply you're probably not going to find a counselor close by. So that may be the only thing that's available for them. So that's one of the things that came up through all of this.

Secondly, many reverse mortgage consumers are compelled to purchase or given the option of purchasing an annuity as a part of the transaction. And we want that to have -- right now there's like a three-day rescission period. We want to separate the annuity sale altogether, altogether from the reverse mortgage product. And that's an issue that's in discussion right now in Sacramento about how long that separation could be. Three days not acceptable. Five, seven, maybe 30 days. But that's still up for grabs.

And the final one has to do with the language situation that came up earlier. We have a very diverse population in California and we need to have languages built into all of the documentation.

So with that I will stop.

MS. BRAUNSTEIN: Terrific. Thank you very much.

Barbara.

MS. STUCKI: Good afternoon. My name is Barbara Stucki and I'm the director of the Use Your Home to Stay at Home Initiative for the National Council on Aging.

I want to thank you for providing us the opportunity to testify on the use of reverse mortgages among homeowners with a chronic health condition.

For impaired older Americans, sustainable homeownership is often linked directly to their ability to continue to live at home. Today about three-quarters of older homeowners have a physical or a mental limitation. Many of these elders are unprepared for the financial challenges that can come with a chronic health condition. This is true not only for cash-poor seniors but also for middle income families who often struggle to pay the extra cost of help at home.

With over two trillion tied up in the homes of older Americans, there's a growing awareness that this asset could be an important resource for sustaining older homeowners, which in my world is termed "aging in place."

We believe that the recent rise in the reverse mortgage market has been fueled by growing numbers of seniors who see these loans as more than just a tool for financially desperate elders.

The potential impact of having more impaired borrowers could be substantial. In a recent NCOA study, we estimate that about 13 million older households are candidates for using a reverse mortgage to pay for long-term care.

Greater use of reverse mortgages could also have a significant impact on government expenditures for long-term care. Of the estimated 13 million candidate households, about five million already rely on Medicaid for long-term care or are at financial risk for needing government assistance due to a chronic health condition.

Growing use of Reverse Mortgages for Aging in Place also has implications for consumer counseling and education. The impaired elders have unique needs when deciding to take out a reverse mortgage. A chronic health condition can make it hard to know how much longer a person can continue to live at home. In determining the appropriateness of these loans, it is important to consider how long the funds will last to pay for essential services.

We believe that helping older homeowners to age in place will require additional reverse mortgage counseling. We comment HUD for its efforts to address this need.

We were recently approved by HUD to become a HECM counseling intermediary. We are partnering with the Administration on Aging to create a new aging in place network to provide potential borrowers with in-depth information on a wide array of social and health services, along with housing and other financial options.

As reverse mortgages become a mainstream product, federal and state policymakers are increasingly looking to these loans as an important new policy tool. For example, the recently passed Budget Deficit Reduction Act will, for the first time, limit the amount of home equity allowed for Medicaid eligibility. This law explicitly allows seniors to use a reverse mortgage to reduce home equity to meet the new Medicaid guidelines.

The 2006 National Long-term Care Education Campaign included information on reverse mortgages. This topic will also be featured as part of the new federal long-term care clearinghouse.

In addition, as part of a new study funded by the Department of Health and Human Services, we are working with Minnesota, Washington state, and the City of Los Angeles to explore ways for states and municipalities to promote the use of reverse mortgages among impaired elders.

Greater focus on aging in place can be a powerful framework for strengthening ties between agencies that seek to improve the quality of life for seniors. At the same time, there will likely be closer scrutiny of reverse mortgages by legislators, other government agencies, and consumer groups. There will be a growing need for systematic data on borrowers and the impact of reverse mortgages on seniors' ability to age in place.

Over the past three years, we have been conducting research to better understand the unique needs of this population. But this is just the tip of the iceberg. We urgently need additional data and research to better understand older homeowners and their use of home equity.

In conclusion, reverse mortgages have the potential to be a powerful force for system change and to expand the boundaries of what is possible in using private funds to enhance sustainable homeownership among older Americans with a chronic health condition.

We appreciate the opportunity to testify today and looks forward to assisting the Federal Reserve on issues relating to this important new component of the reverse mortgage market.

Thank you.

MS. BRAUNSTEIN: Thank you very much. And right on time.

Okay. I'd like to start out by posing a couple questions to the panelists. I think this has all been very interesting. And one of the things that strikes me in listening, which has been different from what we've heard in other panels, not just this morning but actually in the other two cities, is that generally there's been this real bifurcation on the panels among whether something was good or bad or -- you know, there was a lot more black and white. And this one is not that way at all.

I mean, I didn't hear anybody say this was a bad product or should not be offered. In fact, it was quite the opposite. It seems like everybody is saying it's a good thing. But that there are some concerns about costs and disclosures and information and education. So I'd like to explore those issues a bit.

One of the things that was mentioned by several of the speakers was the bill to raise the threshold for FHA insurance on the HECM products. And, Ruth, I know you mentioned it.

And one of the things I was just wondering is what is the position of -- something that struck me as interesting, while it seems like that's a necessity because we're bumping up against that, at the same time the private market is developing alternatives to HECM.

And so can you, and also your fellow panelists, kind of address that terms of, you know, is there a dire need to raise the threshold? Should people be relying more on the private market for these products? How does that -- what are the pros and cons of that?

MS. ROMAN: I think from FHA's position, we think that it's still very important to raise the loan limit to the conforming limit. The other products have different features than the HECM product. The HECM product still allows for a larger loan advances to be made, so there's still, you know, value to having more funds available through the HECM product.

MR. AXELSON: I agree with Ruth. I think a lot of the proprietary products, including some that are coming onto the market I think in the next number of months, I think are geared more to nonconforming loans, which is above Fannie's threshold and would be above the threshold that HUD is asking for.

MR. CHANIN: Let me follow up on that. And earlier discussions, both today as well as in other cities, have -- the mortgage market is quite robust. And Jim or Peter or Arthur, the products have been out there I guess for 20 years, give or take. It sounds like the private market hasn't developed at least as expansively as in other areas. And why is that? And to the extent it has developed, it seems like it's paralleled quite closely FHA's program in terms of counseling and so forth.

So how do you see this developing in the future and do you see different products coming on in terms of different features, those without counseling and so forth?

MR. MAHONEY: I think we view the counseling as best consumer safeguard. That's why we require it on proprietary products. So all reverse mortgages we do have independent counseling. So we think that's a great consumer safeguard.

If you look back at volume in the industry, up until about four or five years ago, was really quite small. So the secondary market that traditionally drives product development wasn't really interested, particularly in the middle of a refi boom in this county, to really look at product development for an industry that was doing 8,000 loans a year.

For example, in 2001 we did $300 million in loan balances. We did $3 billion in 2005 and we'll do $6 billion in 2006. So now the secondary mortgage industry has really started to become more interested in it. There's more data available about the borrowing statistics, life expectancy, things of that nature with these products. So now you're starting to see a full development in the secondary industry.

The HECM is the most financially appealing product in the context of how much money a borrower could have, so it will be competitive for homes under the FHA limits going forward into the future. It's very difficult for the private market to emulate that product.

MR. CHANIN: And do you not see different permutations on the product? For example, the cost is fairly significant. You said I think, Bronwyn, up to $60,000 in fees over the life of a loan.

I'm sure that there are agencies out there that could offer the product with lower fees but maybe without all the safeguards if you will. Do you not see those products developing?

MR. MAHONEY: I think you'll see products certainly develop. There are fees that are structural elements of the HECM in particular, the servicing fee, which is normally built into the interest rate on a traditional loan that the borrower doesn't see.

A lot of things that are different structurally today will change and emulate the traditional mortgage market as we go forward. I think you'll see very competitive products as such, but I don't think you'll see the consumer safeguards because of the class we're dealing with, when we're dealing with seniors.

MR. AXELSON: I think you will see some of the fees being built into the rate somewhat. But also I think the nonconforming market, I think traditionally reverse mortgages I think back -- when HECM first came out in '89, it was really -- the product was really geared as a product of last resort I think for senior homeowners who were really -- they needed medical care, they needed medicine, and that's what the proceeds were used for.

I think we're starting to see a shift in what's going to be the typical HECM borrower. And we have our Baby Boomers going to be -- supposedly the first ones are going to be 60 this year. Within a couple of years they'll be eligible.

I think it's -- in a sense it's more financially -- a financially savvy group of consumers, people that are more used to mortgaging their homes and more aware of some things than the last generation. And so to some degree they may not need as many safeguards and the pricing may be able to be adjusted for that reason.

MR. BELL: A few thoughts in response to that. First of all, it needs to be understood that the lion's share of those fees, more than half, are the HUD mortgage insurance premiums, including up front and the half percent per year ongoing on the actual balance that's been drawn down.

There are a lot of us who believe that there's room to reduce that, and we do have a working group with the department to study the program actuarially, to analyze that.

The fee structure that's in place today was established prior to any experience. It was set up front when the program was implemented back in the late '80's. And now that we have a decade plus of experience, we're able to go back and analyze that and work on that.

Also, as volume grows, fees fall because part of the challenge now is that we've been doing such a small annual volume that the costs of a company -- like there's a very large cost to enter this. All the systems have to be completely engineered from the get-go for this product. There aren't off-the-shelf systems for this like there are for other mortgages. And that has to be amortized over a much smaller universe of loans. As that grows, we will see all of that fall in place.

Now, the private product would come in and have the advantage of not having all these mortgage insurance premiums. But basically the way they compensate for that is by providing less money. They self-insure in effect by having a lower percentage of value. So you may knock down the fees, but you're also reducing the amount of money that's available.

MR. CHANIN: Okay.

MR. RICHARDS: Well, just following up on that, Peter, I presume then once you take out a reverse mortgage, it's difficult to increase the amount that you've borrowed. Is that right?

MR. BELL: No. On the contrary. Not at all.

There's a few things that happen. On the HECM product, or other products that have a line of credit feature, if somebody originates the loan with a line of credit, the unused balance in the line of credit grows from year to year.

So if someone has a HECM, say their home is worth $200,000 and their age gives them 50 percent of that, they start with $100,000 to keep it simple. If they leave that $100,000 in that line of credit, a year from now they'll have roughly $106,000 in that line of credit. There's a growth feature there that's going on.

Secondly, there's the opportunity to refinance a reverse mortgage. And HUD actually does a reverse mortgage insurance premium now -- congress enacted that in 2000 -- to allow people to do that.

So what happens is -- a few things can happen over the life -- since the original loan was taken out. The person is older of course, giving them a larger percentage of value. The interest rates could have fallen, giving them a larger amount. And, of course, the home value could have grown and, along with that, the FHA limits.

So if somebody had -- in my $200,000 example, their age gave them 50 percent, six years ago -- nowadays their home may be worth $300,000 and their age gives them 65 percent. They could go back and get a new reverse mortgage to take advantage of that new situation.

MR. RICHARDS: And do there tend to be prepayment penalties with these?

MR. BELL: No. There are no prepayment penalties whatsoever on any reverse mortgage product.

MR. MAHONEY: Just as a point of information, as a servicer we see about five percent of our portfolio -- pardon me. Sorry. As a servicer, we see about five percent of our mortgage portfolio refinanced into new HECMs every year.

MS. BRAUNSTEIN: I didn't hear anybody mention during their opening that there were so-called bad actors out there taking advantage of people on reverse mortgages. Is that a problem at all? Are you seeing that?

MS. KROHN: I think it applies in reverse mortgages when you try to bundle an annuity with it. I think that the -- and this is not something that the Fed would necessarily be involved in. It's an insurance issue.

But what we have found is that very often somebody will go into a bank or a financial institution to apply for a reverse mortgage, or start the process, and before they close on that account, they're referred to that nice young man over there, that nice young lady, who is sitting at a desk with no name tag on it, identifying them as an insurance salesman.

And recently I had a chance to talk to the Department of Insurance in Sacramento about this, and they said that that's a very serious problem, where they're just sort of slipping these annuities into the signed documents.

And anyone who knows annuities will know that you probably shouldn't be selling them to somebody in their mid 70's or 80's because they may never live to get the full benefit of them.

So that's one thing that we've seen very commonly applied.

MR. BELL: Can I respond to that?

MS. BRAUNSTEIN: Go ahead.

MR. BELL: I've heard more discussion of that topic in the Sacramento area than I have anywhere else nationally. So I guess there might be some folks that are pursuing the sale of the annuity simultaneously in that particular instance than I'm aware of anywhere else in the country where it's going on. But a few things on it.

First of all, we as a matter of industry practice, when we are dealing with a borrower, we make a disclosure that basically makes clear to the borrower that this money is yours to spend however you want, and you are under no obligation whatsoever to purchase any particular service or product from any particular provider on that. The money is disbursed to you, it's your money. We do not disburse to any third parties, and we do make that disclosure on it.

Secondly, there is no product that does require the purchase of an annuity. There might have been once upon a time a good number of years ago. There is nothing in the marketplace, nor has been, for several years now that requires the purchase of that.

And thirdly, if there is an annuity purchase involved, I believe the TALC disclosure requires that to be disclosed in there so it does show up in the numbers that are provided to the borrower.

MS. KROHN: I mean, you guys are far better experts to discuss this than I am, but what I will tell you is that there are some bad boys out there that are doing this kind of thing. And here again it's not a Fed issue; it's an insurance issue. But it is happening. And I don't think it's just in the minds of those in Sacramento. We may have some testimony to that fact later in the open mic.

MS. BRAUNSTEIN: As a follow-up to that, too, in talking about possible bad actors, one of the things we've heard a little bit about that I'd like to hear from you is that, as you say, up until recently these loans were not a big product and now it's starting to increase. And I would imagine with the Baby Boomers coming that it's going to increase even further.

What do we see in terms of advertisements for these loans? Is there starting to be very aggressive kind of push marketing like we see for other kinds of products to certain populations and, you know, what's -- can you --

MS. BELLING: I can speak a little to that. I think Peter speaks for most of the major reverse mortgage lenders in his association, but there are other brokers and lenders who are not members of NRMLA, of the association.

And I think, you know, they -- to NRMLA's credit, they do have a very good code of conduct that sets standards for their members, but we do get complaints from other lenders who are not -- and on behalf of brokers and other third parties who are not affiliated with the national association.

I think in terms of advertising, most of the advertising that we do see is pretty much above board. We hear about seminars and other questionable events going on around the country, and I think people tend to turn to AARP as sort of a consumer watchdog for these kinds of practices.

In 1997 we heard about a fee being charged from a third party in Southern California to direct people to a reverse mortgage lender that led to a lot of confusion and a lot of financial abuse frankly. And HUD stepped in and efforts were taken. There were some lawsuits. It's a much longer story.

But HUD -- the truth in lending requirements were broad and HUD expanded the requirements under the counseling certificate. And the major lenders in the field who were buying these loans from these referring third parties basically said they would no longer do business with them. So fortunately those folks are no longer, to our knowledge, visible in the market.

But I do think with the growth of the market that we have to be more vigilant. And I'm appreciative that AARP is held in such high trust in many places that we do tend to get these kinds of complaints from time to time.

We now sort of automatically share them with HUD staff, both in Washington, D.C. and regionally, when they -- and most of them do pertain to third parties selling the HECM in combination with other products or home repair schemes and so on.

So I think we have to remain extremely vigilant.

The counseling component is a good consumer protection but it isn't everything. And some of these things do happen outside of the -- my concern about waiting 30 days after the reverse mortgage transaction, then it falls completely out of the purview of all the disclosures and what have you.

So I don't know if a delay is really going to help much if someone comes behind a month later to sell someone an annuity. If they don't fully understand the transaction, then I think they're a little bit more at risk than if it has to be disclosed in the current TALC requirements.

MS. BRAUNSTEIN: One of the things that's been talked about obviously is the required counseling. And I have to say that in preparing for this hearing and reading through lots of materials on all different products, including this one, one of the things that really struck me was the booklet that AARP has out.

MS. BELLING: Right.

MS. BRAUNSTEIN: And the fact that it's like 45 pages long.

MS. BELLING: Indeed it is. This is a major complicated financial transaction that involves your largest and many people's only major asset. So it speaks to the complications and the depth of the transaction and how important it is for consumers to understand not only how the loan works but alternatives to the loan as well that may be much more suitable to meet their needs.

MS. BRAUNSTEIN: Which made me wonder how much people really do understand these transactions when they get into it. I mean, that's a lot to absorb and understand.

Peter.

MR. BELL: Sandy, I would say a few things. First of all, there's been a lot of efforts within the industry to get out and do consumer education, both by AARP, NCOA, the industry itself, each of us separately, a lot of us collectively.

There's a lot of web sites. We do get a lot of traffic on our web site. On AARP, the reverse mortgage page I think is one of their most frequently visited pages in the whole AARP web operations.

People do a lot of homework on these. It's very interesting. And beyond doing the homework, they do it on their own, they get educated by the lender, and then they go and they get the independent third-party discussion with a counselor. So there is a fair amount that's out there.

Besides AARP's book, there's a couple of good books that have been published commercially. There's the Dummy's Guide, Reverse Mortgage for Complete Idiots. There's books by journalists. We have a series of consumer books that we distribute free to consumers. We give out tens of thousands of those. Maybe even a hundred thousand of those every year.

So there is a fair amount -- Fannie Mae puts out information. There's some very good videos. Jim's company has done an excellent video, as has another organization. So there's a fair amount of information that's out there.

But once again, the counseling network is a key component of the consumer education process. There's no other product that I know of that exists where this counseling is in there that, you know, before you could do the transaction you have to go to that counselor.

We cannot subject the borrower, the prospective borrower, to any costs whatsoever until that prospective borrower has been through the counseling and provided a counseling certificate to the lender.

MR. CHANIN: Let me shift --

MS. STUCKI: If I could just add to that. One of the things that we have been doing is partnering with the Administration on Aging, because we're trying to get out through as many different conduits as possible to reach potential borrowers who may be facing different needs.

The Administration on Aging has its aging network with thousands of members who are already counseling seniors about a wide array of issues dealing with chronic health needs. And they have stepped up to the plate and are actively getting involved in providing HECM counseling through our new network.

And I think that's going to be another opportunity and avenue to address the very specific needs of seniors. Because often times the needs of somebody who has a health condition and the solutions are going to be rather different from somebody who is trying to either pay the monthly bill or buy an RV.

So I think we're going to start to see perhaps more specialized counseling coming out. I know we are also talking with a financial planning association to start educating financial planners more about this issue. And I think that is -- again, part of the thing is that we get a more targeted message out to address specific needs, and I think that's beginning to happen.

MR. CHANIN: Let me shift a little bit. And Arthur, you and Ruth both mentioned, Ruth in terms of prospectively, that HECMs or reverse mortgages either can or maybe will be with legislation be able to be used to purchase a home.

Can you discuss that a little bit more and the other panelists on both sides whether you see that developing in terms of the product, whether you see issues associated with that use of these products to purchase a home and just those types of issues?

MS. ROMAN: I would say from FHA's perspective, we just know that there's been a lot of interest and expressed to FHA for that type of product. And we know it's something that currently occurs with other products and so we're trying to figure out once the statute hopefully is passed -- right now we're working on how that would be structured and actually how it --

MS. BRAUNSTEIN: People are having a hard time -- I'm sorry, Ruth. Can you bring it closer?

MS. ROMAN: OH, what I was saying from FHA's perspective, we received a lot of interest to getting that type of product for HECM.

And, you know, we're hoping that the statute will be passed. And we're really looking at the other products that are out there for purchase and focused on how to operationalize it.

MR. AXELSON: Fannie Mae has had the product -- I'm not sure -- for purchase for a while. I'm not sure what the numbers are in terms of -- but it does give the seniors greater flexibility. I mean, you know, a lot of them want to age in place, but sometimes they want to relocate for family or health reasons or whatever.

And rather than getting a traditional mortgage, I mean, the Home Keeper for Home Purchase, they can often qualify for larger amount of funds than -- and buy a better home because there's no income limits or income test. It's based on their age, the value of the property. And so it just -- it's another flexible piece to, you know, retirement solutions and planning.

MR. CHANIN: Peter.

MR. BELL: Sure. The classic case of HECM for home purchase would be a case where you have a couple that's been in a home for a long time. It's very often a multi-story home, deferred maintenance, a lot of property to take care of. They don't necessarily have cash sitting in the bank to be able to take care of it and they're interested in moving to a smaller, newer, single story product that better fits their needs.

Well, very often these days with home values being what they are, land costs, development costs, that smaller and newer product is actually more expensive than the value of their older home. The HECM for home purchase concept will allow them to sell their home and either supplement the proceeds that they get from that or even perhaps not throw all the proceeds that they take out into the new purchase.

So, for example, if someone got 50 percent of the value of the new home, if they were buying a $300,000 home, they could get 150,000 out of the HECM. If their old home is worth 200, they could sell that and have no mortgage to make, have the $300,000 home, and have $50,000 cash reserves.

So it really totally transforms their living -- could totally transform their living situation. So it would be a very good product to have.

MR. AXELSON: And the borrower can decide how much of their own money they want to put down and how much they want to borrow. So there really is flexibility.

MR. CHANIN: Bronwyn?

MS. BELLING: Yea, I was going to say I think some people are -- that the HECM for home purchase would allow people to trade down and into more appropriate living arrangements, pretty much what Peter had to say as well. So I think it would add a lot to the options.

You hear a lot of sometimes negative criticism about these loans keeping people in older houses longer than is appropriate. So allowing them to move to something more suitable to meet their needs better, I think it would be a very good thing.

MR. CHANIN: Okay.

MS. STUCKI: Just to add to that, again coming from the perspective of a chronic health condition, this is exactly a great idea. There are many new models for housing that are now being opened up, co-housing and other kind of models where a person still owns their -- the place where they live, but they're not necessarily the traditional single family home.

And to the extent that these kinds of loans can enable a person to move to these very supportive settings and also provide some additional cash to help them pay for the services that they need to be able to sustain themselves in the home, it may be ideal for somebody with a chronic health problem.

MS. BRAUNSTEIN: Have there been problems in the existing portfolios with -- this sounds kind of morbid -- but people outliving their loans basically and using up all their equity and their payments cease? Because obviously medicine is improving and people are living longer. And, you know, they took out a loan maybe 20 years ago and not envisioning that they'd still be alive now but they are.

MR. AXELSON: I mean, the benefit in HECM of the ten-year plan payment is that as long as the consumer remains in their home and using it as their principal residence, their payments continue whether the outstanding balance is below or exceeds the value of the home.

MS. BRAUNSTEIN: No, I understand that. But I guess I'm asking a more general question. Because HECM came along a little bit late -- there were products before HECM and some of those -- you know, I'm just wondering about even the private products that were out there before HECM came along with its safeguards. Have you heard anything about there being problems like that for people who got them?

MS. BELLING: The earlier -- there were some private plans before the HECM that involved giving up a share of the future appreciation or an equity -- a share of the equity in the house and there were some problems with that.

I think that's why AARP has supported and advocated so vehemently for the counseling component to really help people -- require people to understand the transaction before they enter into it.

In terms of HUD's own evaluation of the HECM program, they're periodic analyses of the HECM program itself indicate that the financial model that's set up the HECM program is quite robust and that there is an appreciation assumption built into the financial model for the HECM. So it seems to be holding its own in terms of the mortgage insurance premiums that are collected being sufficient to cover the expected losses on the program.

But as property -- as the 203 -- as the maximum single national limit goes up and property values continue to increase, that might also adversely affect, you know, the cushion that HUD has built up in the mortgage insurance premium pool. So it's something that everybody has to I think keep a close eye on.

And I know HUD did an actuarial study that looked into some of these matters. So things are changing very dramatically as property values appreciate so much.

MR. AXELSON: Also, I'd just like to point out there had been some litigation in connection with some of the older products that had the shared equity feature, et cetera. To my knowledge, there's not been litigation on the HUD -- on HECM or Home Keeper or the Cash Account, the more modern products if you will.

MR. BELL: It's possible that somebody could outlive the money that's available to them. If they take it as the ten-year payments, then they won't. As long as they're in the house, that money will keep flowing. If the money was -- the payment was predicated on them living to be 92 and they lived to be 102 or 112 or 122, they'll still continue to get those payments.

But otherwise, if they take it another way, it is possible that they could outlive it. It would be possible that they could outlive their money without the HECM. The difference is they would have had to sell the house and moved out without the HECM and then they would have outlived their money at some point and been equally there. I mean, that's one aspect.

You know, I don't know how you can design a product to deal with that. But I think they've done a very job at FHA in designing this product that if people do take that life ten-year option, they have the ability to stay in that house right until their very last day and always continually receive income from it.

MS. ROMAN: I would add that we do operate the HECM program on a modest credit subsidy, so we do have a small reserve to cover any losses.

But to Peter's point earlier about perhaps looking at reducing the MIP, FHA at this time doesn't see us reducing the MIP because we think that could run us into a positive credit subsidy and requiring congressional appropriations which we don't have now.

MR. MAHONEY: Just very quickly, most borrowers take out the loan thinking they're going to die in the home. And the typical borrower is 74- or 75-year-old senior that probably has a 12- to 13-year life expectancy. Reality of it is the loans on average are repaid in seven years.

So although they take out the loan thinking they're going to stay there forever, they have to downsize, they go to an assisted living facility, somewhere along the line they're actually moving out sooner, selling the house, taking the equity with them onto the next living place to pay for their retirement.

MS. BRAUNSTEIN: And, Barbara, did you have a comment about that?

MS. STUCKI: No.

MR. CHANIN: Let me shift to disclosure. There has been a lot of discussion about counseling. And it seems from everyone's point of view that counseling is not only very helpful but the most important channel of communication in terms of consumers.

But I would like to focus for a moment on the truth in lending and other disclosures. Do consumers look at those or are they very secondary in use to consumers? How does that fit in in terms of the products and consumers understanding these products?

MR. AXELSON: Well, I just wanted to comment because I -- I drafted a lot of these disclosures through the years. And I was surprised some of the comments across the room that the borrowers didn't understand this or that, because there are certain things that are clearly disclosed in the disclosures. And to say -- then to hear, well, they don't know, you know, to me means they're really not reading them.

MR. CHANIN: Those may be only the disclosures you've drafted. Perhaps you --

MR. AXELSON: That's right. So there's clearly some disconnect there. Because there were certain things that were raised that buyers should understand this but that are clearly required to be disclosed in truth in lending and they're in there.

MR. CHANIN: And in your sense, the consumers, do they read these or they really rely on the counselors to explain these obviously very complicated products in some instances?

MS. KROHN: When you're handed a stack of paper that thick and you are expected to read every single piece that's in there, disclosures or no disclosures, truth in lending or no truth in lending, you absolutely have to have counseling to understand. And especially if you don't speak English and the person that's negotiating the loan with you is doing everything in English. You've got to have the language of the person -- of the borrower. And in California we've got six languages that are part of a Civil Code that governs that for everything except for reverse mortgages.

So the comprehension and the understanding, I think it's critical. And there is a lot of counseling I'm sure, but counseling coupled with being able to understand and comprehend what is being communicated so that they have a better chance of coming away with an understanding of the product.

And you know what? All the counseling in the world isn't going to make somebody understand everything there is to understand, but you got to do the best you can do to make sure that that's communicated.

MS. BELLING: I was just going to add that I heard a lot of -- several people allude to HUD-certified counselors. Actually, HUD only certifies the agencies to do this work, or approves agencies to do this work.

And we provided this national exam and now have about 350 counselors who have met a very high qualifying score on this national exam that follow our detail protocol.

They go into a fair amount of detail about the total annual loan cost rates.

But there are something like 1,000, 1,200 HUD-approved housing counseling agencies that allegedly offer this counseling. And, you know, we do hear some horror stories about -- we produced a video in 1997 that's 30 minutes long with half of it is interviews with three reverse mortgages borrowers. And we hear stories of people being propped up in a chair and shown this video and asked to sign -- and asked if they have any questions and can they sign a certificate.

So we would like to really see -- we worked very long and hard to raise the standards and the quality of this counseling. We'd like to see HUD step up and require all the counselors to pass this exam so that everyone is delivering accurate information.

The other point about the TALC rates is it's only an estimate and it presumes that the borrower choose -- takes half the money at closing and nothing thereafter. So it's just sort of -- and it presumes -- it gives some snapshots about property appreciation into the future.

But nobody has the crystal ball to know exactly when they're going to draw down the money and what's going to happen to either their home value or the interest rates out into the future. So it's really hard to really get a handle on what the real costs are of these loans because so much, you know, drives from the decisions that you make after the loan is closed.

So I think it does speak to the importance of the disclosure, and trying as our statement said to include some of these ongoing fees that aren't fairly captured and this -- in the current disclosure formula. So I think there is some room for improvement there.

MR. CHANIN: Okay.

MR. AXELSON: One thing. One of the biggest complaints I hear from my clients is that they need more and better qualified counselors because they -- I mean, it's much better for the lending community to get an educated consumer who understands the product when they come back to them from counseling.

I mean, most of the lenders do not -- you know, don't want to shove this down someone's throat when they don't understand what they're doing. That's not going to help anybody.

MS. BELLING: And we need more funding to pay for the counseling. Because HUD can mandate it, but there isn't money behind it. And we have a real predicament with the growth of the market now.

The origination fees are just a percentage of the HUD limit or the home value, so they're ramping up every year and that just drives the costs up.

And, you know, the average origination fee on these loans now is $5,000 versus the average maximum claim amount is $250,000. And yet we're struggling to get 100 a 125 or $150 fee to pay for what in our case constitutes two to three hours of in-depth personalized one-on-one counseling with a homeowner.

So not only is the counseling important, but it has to be supported in a way that's sustainable so that the counselors who do this really important good work are reimbursed appropriately for their efforts.

MR. CHANIN: Jim or Ruth?

MS. ROMAN: I just wanted to say that HUD is moving in the direction of certifying counselors. We recognize that we need to make sure that quality counseling is taking place. And so we have a proposed rule that we're planning on putting forth that would require all HECM counselors to take an exam, to pass the exam in order to provide HECM counseling. And also to have ongoing continuing education as well.

MS. BRAUNSTEIN: Peter.

MR. BELL: Yeah, two things. One, I'd like to correct something for the record that was said that's incorrect, which is the statement was made that there's -- there is translation requirements under Civil Code in California for mortgages but not for reverse mortgages.

Reverse mortgage is subject to the same Civil Code on that. The exemptions under the Civil Code are for certain types of licenses, and those exemptions exist for all mortgages, whether they're reverse or not.

The pending legislation would take reverses and treat them separately from other mortgages so there would no longer be the exemptions that exist for the mortgages. But we do currently come under the same Civil Code.

On the counseling issue, funding for counseling has been very problematic. The state involved, AARP, the department, the industry, the counseling community, have all been working together to try and address this.

And my understanding is that HUD is close to issuing a mortgagee letter that will allow a counselor -- I'm sorry, a borrower to pay a fee for counseling out of the loan proceeds.

And after the counseling session the -- basically the counseling certificate will have details of the counseling session and the fee to be paid and, upon closing, the lender will remit that fee to the counseling agency to cover that.

And that will provide a lot more financial support for counseling than is available now. And my understanding is that mortgagee letter is -- whatever this means in HUD terms -- eminent.

MS. BELLING: The complication from our point of view is that will apply to any HUD-approved housing counseling agency and any HECM counselor. So it will allow the person propped up watching the 30-minute video, now allow that counseling agency to charge that fee to a borrower, prospective borrower. They aren't a borrower at that time. The consumer. So they really don't get anything for their money and now they're having to pay for it on top of it.

So we're hopeful that HUD will move forward with the exam requirement as quickly as possible. And we see this as an interim solution that we support, but we really need to close the loop and make sure that if people are required to pay a fee for a service that they're getting a service that's -- they're getting their money's worth.

MR. BELL: Right. Presumably once HUD implements this exam, in order to get paid, the counselor will have to have passed that exam and be on the roster.

MS. BELLING: Right. But they're not happening at exactly the same time.

MR. MAHONEY: As one last comment, there are tools in the marketplace already to support better counseling and such and many of the counselors use them.

AARP developed model specifications for illustration software that -- we developed our own proprietary software used by all of our brokers as well as our retail loan officers to illustrate the product. And that software is used by almost 2,000 counselors in the marketplace today.

So the tools are out there. Getting the certification and getting the funding is the two primary issues.

MR. CHANIN: Jim, can I ask you a question? Do you retain the mortgages you originate, your reverse mortgages, or do you sell them?

MR. MAHONEY: We sell them into the secondary market.

MR. CHANIN: And if you could tell me, does Fannie -- or is there an active secondary market? Has it developed or is it developing or -- other than Fannie Mae?

MR. MAHONEY: Historically all -- Fannie Mae has been the only investor in the FHA, HECM and the Home Keeper, which is their proprietary product. Lehman Brothers has been the sole purchaser of our proprietary product, the Cash Account, as such in recent years. That's changing and I think you'll see new investors emerge this year.

MR. CHANIN: Okay.

MS. BRAUNSTEIN: Okay. I think we're going to wind down here. Anybody want to make any last comments?

MR. AXELSON: I just have -- I have a problem with these foreign language requirements. Because where do you draw the line?

I mean, it certainly -- with Spanish, which is one of the largest non-English speaking groups in the country. But then, you know, I understand like in California, there are I forget how many dialects of Asian. I mean, where do you draw the line?

And how does the private market keep up with -- I mean, how many sets of documents in how many languages are you going to be required -- are you going to require in -- you know, different states you have different minorities. Where does that go?

MS. BRAUNSTEIN: Shirley.

MS. KROHN: No, I agree with you actually. The Civil Code 1932 in California stipulates the six languages as being Spanish, Chinese, Tagalog, Vietnamese, or Korean because that represents the greatest population. May be different in Nevada. I mean, if you're looking at a federal statute about this, it could be different in Arizona.

Every state is going to have to -- if people agree with the whole notion about doing counseling and having the documents in the language that it's negotiated, we can't assume that everybody is going to understand the English version or you just -- you know, just not going to work.

But you're right. Every state is going to have their own language requirements. And how does the statute define Chinese?

MR. AXELSON: Right. That's what I'm saying. I mean, how -- I mean, lenders dealing with state -- you know, 54 jurisdictions between the territories and now they may have different states are going to require disclosures in different languages and different dialects? I mean, it's not -- it's not workable.

MR. CHANIN: Sounds like you need to brush up on those late-night language lessons there.

MR. AXELSON: You know, even the new immigration bills are requiring that people learn English. At a certain point I think you can't call on the lending community to cater to every foreign language.

MR. BELL: There are provisions --

MS. KROHN: All I can say is I would hope that every potential borrower would have an equal opportunity at getting information about a loan or about a product that they are applying for, feel that it's -- it's a necessity in their lifetime and that they understand the documents that they are signing. And if that means putting them in that language, then I think it's a no-brainer. But that's my opinion.

MS. BRAUNSTEIN: And I think we'll let that be the last word. And I want to thank our panelists very much for coming today and we really appreciate it.

We are going to take a short break. We're going to take a ten-minute break. It's ten of 3:00. At 3:00 we will reconvene for the open mic session.

If you have signed up, we would ask that during those ten minutes you come forward to the front of the room and identify yourself -- John, there you are. Okay. If you have signed up for the open mic, if you would identify yourself to John, right there who is waving. And we will start at 3:00.

(Whereupon a recess was taken.)

MR. OLSON: Okay. We're going to get started now. The sign-up is over. We're starting the session.

And we have a lot of people. We are -- as we said this morning, each person will have three minutes to make their statement. However, I want to reiterate the fact that you can submit for the record a written statement as long as you would like and you have until August 15th to do that.

So if you don't have it with you today, you can submit it afterwards, anytime up until August 15th. And we would like to hear from you. So feel free to do that.

But for purposes today of speaking, you have three minutes. And Naomi, who is the timekeeper -- raise your hand -- will give you a sign when you have one minute left and then when your time is up and we'll move on to the next person.

I would ask people -- I do have a sign-up list, but I understand some people -- it's not perfect because some people who signed up this morning aren't here and things like that.

So I would ask, too, for the record, for purposes of the court reporter, that you start by just giving your name and the organization that you -- if you're representing an organization. Some people may just be representing themselves, which is fine, and then make your statement.

And we'll start -- Waiching, we'll start with you. You I know.

MS. WONG: Okay. Thank you.

MS. BRAUNSTEIN: But introduce yourself for the court reporter.

MS. WONG: Sure. My name is Waiching Wong and I'm currently a program manager for economic development at the Greenlining Institute. We're in Berkeley, California. And we're a multi-ethnic public policy advocacy institute that seeks to provide consumer protection to low-income minority communities.

And currently there's about, we guess, $1 trillion at least in the home equity market. And this market is essentially unregulated, and not because it's unimportant to regulate but because of substantial amount of subprime lending that we're concerned about is done outside and to those -- done by those who are outside the purview of regulations. So we believe that the situation is much more dangerous than most people suspect.

And one example that Greenlining has been involved with is Ameriquest, an institution that had best practices in place for subprime lending and that even testified on them, but then they violated their own best practices because people within the organization that had decision making power also had huge financial incentives to violate them.

So with this history in mind, Greenlining has two recommendations. First, we believe that the five or ten largest regulated financial institutions with expertise in home equity loans should, with strong community input, develop a national standard that can be regulated yearly and can inspire national confidence.

Once there is such agreement, many community groups, including Greenlining's members, including Alan Temple Baptist Church and West Angeles CDC just to name a few, would support that federal legislation that would make it tougher for nonregulated institutions to have lower standards.

And what we mean by that is the regulation would enforce that and require that every unregulated lender put on their applications, in bold letters, and in strong language, language that informs potential borrowers that, A, this institution is not regulated by federal regulations, that this loan may not meet the high standards that are set forth by the industry.

And also, as a result of that, all loans -- and under this the loan notice cannot be final for 14 days and the borrower be given 1-800 hotline that is staffed by multilingual experts who can inform borrowers if the loan meets federal standards, if there are alternative options available, and can also refer the borrower to other institutions that can offer them something better.

And this alternative has already been examined by lawyers and deemed constitutionally valid. And Greenlining will be presenting this idea again to the new Federal Reserve chairman later this year at out annual meeting and also expect to meet with Sheila Behr, the soon-to-be new chair of the FDIC, and John Dugan, who is already taking action in this regard. And we want to discuss those things with them.

And Greenlining believes that these recommendations can greatly reduce the harm that ensues from the predatory subprime lending and, you know, prevent that type of lending altogether.

Thanks.

MS. BRAUNSTEIN: Thank you.

Next.

MR. KENNEDY: Thank you. Good afternoon. I'm Allan Kennedy. I'm from the San Francisco District Attorney's Office here on behalf of San Francisco District Attorney Kamala Harris.

I work in the elder abuse unit and I also handle the real estate fraud matters that our office prosecutes. And I just want to basically put on the record for -- as far as this hearing is concerned that DA Harris and our office are very concerned about the use of predatory loans, particularly in the San Francisco area, of course, since that's what we prosecute.

Unfortunately, we have a very large number of potentially vulnerable elders in our district, in our jurisdiction here, that are homeowners, long-time homeowners, who have been subject to very predatory or very onerous conditions in terms of loans that have been made, either in terms of reverse mortgages, in terms of second home mortgages, or equity lines of credit. And unfortunately they've been -- often take advantage of the vulnerabilities of the elders in our community.

And we've had this -- we've had a number of cases come to our attention in our office over the preceding years involving elders who have very limited mental competency, and that is made obvious when assessments are done by say psychologists or psychiatrists and yet these people have committed themselves to very difficult home loans that unfortunately, in many instances, have resulted in foreclosures and loss of their homes.

And it's a real concern of our office that whatever tightening of regulation -- and I'm not one to be as good on the specifics of that as many of the speakers here today are, but any tightening of regulations in terms of the subprime market, particularly as it relates to the elderly is concerned, we are very much in support of because of the many instances that we've seen over the years in which the senior citizens in this area have been subject to these kinds of loans.

With the high value of real estate in San Francisco and the whole Northern California area, this is really a problem because it's almost been a real magnet to people from outside the area to come here to seek to make high commissions on the -- on second or equity lines of credit on our homes here.

And so I'm just here to say that we see this problem a lot in our office. And we just hope that whatever further regulation that can happen or requirements on counseling or -- because we have a very diverse society -- very diverse community here, the requirements that were discussed earlier about language requirements, they're very much a problem for our senior citizens in this community as well.

So thank you.

MS. BRAUNSTEIN: Thank you.

MR. ZAHRADKA: Good afternoon. My name is James Zahradka. I'm a senior attorney with Public Interest Law

Firm, which is a project of the Law Foundation of Silicon Valley in San Jose. Thanks for the opportunity to speak today.

And at first I just think I need to say that I was under the understanding that we get five minutes today based on the press release. I'll limit my comments to three. But I think that's unfortunate.

I just hope that the written comments are indeed taken quite seriously and reviewed with perhaps even more care given the limitations on time.

So I'll give you my three recommendations first and then do as much detail as I can given the short time.

First, the Fed should bring more high-cost loans within HOEPA's protections for borrowers against predatory lenders. And specific ways to do that -- you've heard a little bit about these already -- but you should include YSPs and prepayment penalties in the points and fees calculation and also lower the points and fees trigger from eight to four, five percent of the loan amount.

Secondly, the Fed should protect consumers from unscrupulous lenders and brokers who seek to take advantage of borrowers who are not fluent in English. And you heard a little bit about that, too. Modeling on Civil Code 1632 I think is a good way to start.

And third, the Fed should protect borrowers from being pushed into loans that are not suitable for them. And one very key aspect of that is the abuse of no document or low document loans. You also heard about that a little bit earlier. And I'll hopefully have some time to give you a little detail about that.

So our experience with this is based on my -- my program and our sister program, Fair Housing Law Project, representation of dozens of borrowers over the past five years or so after our colleague, Heidi Li, started us in this work some time ago when she was with our organization. We've represented them on -- dozens of people who have been victimized by predatory lenders.

Particularly we had two cases involving groups of homeowners who were victimized based on their language ability and/or ethnicity. And this gets to the issue in the -- I think in the public request for comments about the HMDA data, which shows indeed Latino home buyers are getting costlier loans. These cases show very clearly that that was based on factors not related to legitimate underwriting criteria but it was based specifically on their ethnicity or on their language abilities.

And that -- those cases, one was a purchase loan and one was a refinance, which I think underlines Judy Zeigler's point earlier that HOEPA should indeed be expanded to include purchase loans.

So we've also advocated for some legislation in this area. We were stymied on the local front by California Supreme Court decision about Oakland's ordinance and we've been stymied on the state level frankly by the financial industry's very strong position in Sacramento. You might say stranglehold.

So we really look to the Fed for leadership in this area. We're not having a lot of luck in these other arenas. So we hope you all will do something about this.

So getting to the YSP issue, the whole point of these fees is to award the broker for getting a more expensive loan. So to not include those in the calculation when you're deciding when a consumer is getting into a dangerous loan it seems unfair.

And I'm out of time, which is quite disappointing. But I guess I will give the rest of my comments in writing.

MS. BRAUNSTEIN: Thank you very much.

Next. Mr. McCurdy?

MR. McCURDY: Yes. Thank you. My name is Jonathan McCurdy. Thank you for coming.

MS. BRAUNSTEIN: Can you speak directly into the mic so people --

MR. McCURDY: Thank you for coming. Thank you for coming.

I've been a lawyer in both public and private practice for 30 years, working in low-income minority communities. For at least the past ten years, I've been working on behalf of victims of predatory loans or mortgage brokers who sell them.

I am not here today, though, to talk on behalf of the victims. I'm here today to offer you a perspective from the elicit unscrupulous mortgage broker.

In California real estate and mortgage brokers operate under the same license, and we as mortgage brokers work very hard every day in the vineyards of the distressed non-English homeowner.

Our message to you is that we really like the regulation scheme and the -- and the effort put into this the way it is. Through a dedicated team of language-sensitive community runners, cooperative no CM lenders, flexible closing day investors who can get as much as 400 percent annual rate of return, entrepreneurial straw buyers who we've been paying 3,000 a hit to act as purchasers -- but now we found we can use stolen identities and eliminate that cost, pocket it ourselves.

Through the use of this dedicated team, we're able to resource underutilized and wasted equity -- I heard people refer to this as skimming. I think that's a very bad word for it -- we're able to resource this underutilized and wasted equity from the low-income communities and release it into the marketplace, where it will do some good for all of us, not just the unfortunate homeowner who is probably going to lose her house anyway.

My message is don't change a thing. But most critically, if you're going to change some things, keep income asset stated loans, yield spread premiums, English only docs, real important asininity immunity. If the banks were on the hook for all this elicit conduct, I just think they'd stop it.

Unfettered underwriting discretion, don't tighten that up, please. And of course -- this goes to an issue brought earlier -- please don't spend any money on enforcement because right now we can get away with anything. If you change any of these things I've talked about, I'm out of business.

Thank you.

MS. BRAUNSTEIN: Thank you.

MR. MORGAN: My name is Ian Morgan. I represent AARP and the Community Action Volunteer Center, Santa Clara county. And I'm also a volunteer in the San Jose Information Center, which is rather unique. It's the only one in Northern California.

Thank you. I learned a little today. I thought I knew a little. Now I'm little confused. When I get a phone call on anybody inquiring, we simply refer them to the

Council on Aging because we don't know how to do any better than that. We know they've been very busy, particularly with counseling for Medicare Part D.

Obviously counseling is very important. We think it is essential, is mandatory. And my own personal view is I think, like any other professional occupation, it should be certified by examination.

That's all I have to say. Thank you.

MS. BRAUNSTEIN: Okay. Thank you very much.

UNIDENTIFIED SPEAKER: My name is Nuris (phonetic). And I'm retired. I'm a volunteer for AARP and part of the Community Presents Team for the Concord area. We generally do have a lot of seniors and we do get feedback from them.

The thing that most of the people over there feel is they want strong, meaningful consumer protections against predatory lending. Having said that, AARP earlier expressed a position of counselors, which makes absolute sense. The counselors should not only be -- there should be funding released. But not only should they be trained, tested, and available, but they also should be held accountable for the advice they give. And there must be some mechanism.

When we have these counselors advise an elderly lady who is 70 years old and say, "Okay. Go ahead and do this," and if that is a very wrong advice, then the counselor should also be held responsible. So there should be mechanism to get the elderly person the right, honest, good advice that the person needs. It shouldn't be haphazard. It should be carefully thought out when the person gives an advice.

The other thing was things should be in plain English. If it is two percent, it should mean two percent and not 2.3 percent. Because elderly people are real aligned to figure that one out, you know. And if you advertise in Spanish, then you should be able to give the document in Spanish to a Spanish-speaking person because you have taken the trouble to advertise in Spanish. So why can't you have the documents for signature in same language? Otherwise don't advertise in Spanish.

And the last but least is we need you, you people, to look at how to reduce the closing costs. They are high.

Thank you.

MS. BRAUNSTEIN: Thank you very much.

MR. KRYSTOFIAK: Thank you very much for allowing me the opportunity. Governor, I appreciate you being here, along with the council.

My name is Steve Krystofiak and I am a mortgage broker. I'm a mortgage broker that is sick to my stomach to see how this industry is being used on a daily basis here in California.

I'd like to start off with a question to Leonard. Leonard, what is a subprime loan?

MR. CHANIN: I don't think we're responding to questions. There is no definition that I'm aware of of a subprime loan.

MR. KRYSTOFIAK: Exactly. And that's very scary today that subprime loan -- I've heard that terminology today easily over 50 times. And it's very scary that there is no definition but yet it's been used 50 to 100 times today.

I'll tell you another thing that is scary. I'm a mortgage broker that has access to a loan where I can do 100 percent financing, meaning no down payment, stated income.

That means the stenographer here could tell me she's making $200,000 and I'll believe it. She could also tell me that she has $500,000 in the bank. I'll believe that, too. She could also have a FICO score of 620, where 680 is average. So she could have a very low, low FICO score. And I could get her a loan for $950,000. That is scary, also.

Banks are lying when they tell you that stated income is only for people with high FICO stores. I think I just proved that. Banks are also lying to you when they say that stated income loans or stated asset loans are just for people with low LTV. I think I just proved that as well.

I have taken an informal survey of account executives from banks. And these are federally charted banks, ones that would have their same names on baseball stadiums, football stadiums, ones that everyone here in the audience has heard of. And they said between 40 and 50 percent of their loans in the Bay Area are stated income loans.

I think that's a very strong answer to why incomes in the Bay Area having been relatively flat over the last four years but why home prices have doubled. There should be a very strong correlation, and that is stated income loans.

The fed government has come up with an idea saying, well, with subprime loans and nontraditional loans, DTI limits should be higher. Well, why should DTI limits -- for anyone who doesn't know, that's debt-to-income. It's a ratio. Come and see me later if you want me to explain that a little more. Debt-to-income limits should be a little lower. Well, that won't do anything if I'm telling you I make $200,000. I'll just say I make 250 instead.

Some people might say that there's a reason why stated income -- it helps people get homes. It does. It gets people homes who are on a cash business. I don't believe that banks should be rewarding people who only make cash, don't pay taxes, with easier ways to buy a home. I also believe that that makes it an easier tool for people to get homes that they truly cannot afford.

I'd like to audience to take a second to think imagine if colleges -- Department of Education I'm sure would like to have more people go to college. Imagine if when you're 18 years old, 17 years old, filling out your college application, imagine if you could just simply state your GPA, state your SATs. Everyone would be wanting to go to Stanford and would be qualified.

Everyone in America wants that American dream to own a home. Through stated income loans, they are qualified with a low or high FICO score.

Now, what would happen --

MS. BRAUNSTEIN: Thank you, Steven. I think that's -- we'll stop there. But we'll look forward to your longer written comments being submitted into the record.

MR. KRYSTOFIAK: I don't write books very well but okay.

MS. BRAUNSTEIN: Thank you.

MS. UPP: Thanks for having us here today. And I appreciate the time to speak with the Federal Reserve Board of Governors.

My name is Stephanie Upp and I'm vice president of the San Francisco Earned Assets Resource Network, or EARN. We help low-income families save money and invest in assets, homeownership, small business, and college education. We do that through a two-for-one savings account that's matched. It is called an individual development account.

And what I want to talk about today -- I agree with a lot of what's been said so far. One concern that I have and I want to make sure that you all note this is that the emphasis, especially in the last panel, on education and counseling, by far we understand that education is important component of building assets and homeownership and that we want to give people the tools and the education and skills that they need to make wise choices, but nobody out there is going to make -- with all the education in the world is going to make a wise choice if the only products they have available to them is predatory products.

Again, what we didn't talk about at all on the last session on reverse mortgages was the back end of those products that were being offered. We talked about how they operate, how you can enter into them, and then we had more of half of our discussion was about education and counseling and certifying counselors.

But just to echo what these two gentlemen said, while it's important, we have no way, then, of certifying the motivations of those counselors after the fact. And again, if the only product available to our senior citizens, our minorities, folks with low income and low credit scores are predatory mortgages, then as a general society, as local economies and state economies, we're just setting ourselves up to fall.

And I just also want to express concern over zero down loans, three and five year ARMs, especially now as interest rates are starting to go up. We understand that our low-income clients are investing in houses and buying them and we're very concerned about the mortgages that they're entering into.

And so we're starting to focus on housing preservation measures and what kinds of tools and skills and products can we develop to help our low-income -- low and moderate income families stay in the houses that they're purchasing today.

And we want to make a call now to all the bankers, mortgage brokers, and realtors in the room to be socially responsible, to join us and to build products, and to advocate for a better and more responsible lending.

MS. BRAUNSTEIN: Thank you very much. Thank you all.

And we'll have the next group of people come up, if they're here. Pearl Caldwell, Eve Orton -- and by the way, I totally apologize if I'm mispronouncing any names -- Don Gerimonte, Peter Szego, Gerald DeRyan, Laura Baldwin, Moses Diaz, and Celia Blanco. Those folks could come forward.

Same as before, we have a timekeeper who is right there, Naomi, and she will signal you when you have one minute left and then when your time is up. Everybody has three minutes.

And I would ask that you please talk directly into the microphone when you make your remarks for two reasons. One is for our reporter, our court reporter, and the second reason is because people apparently in the room are having a hard time hearing folks unless they're directly into the mic.

You can start, yes, sir.

MR. SZEGO: My name is Peter Szego. I'm a volunteer with AARP. I'll restrict my comments to two points. First is the language issue which has been raised by several other speakers.

I live in San Jose. The City of San Jose, jointly with the County of Santa Clara, recently completed a professionally-conducted needs assessment for seniors, a senior needs assessment. Among other things, this showed that 48 percent of the seniors in our area are not fluent in English.

So I think this shows and we know from experience that many of the problems that we've encountered with loans have to do with language, at least in part have to do with language, issues of communication. So I think it becomes absolutely essential that not only the question of credit instruments but particularly the counseling be conducted in a language and cultural fashion to reach the people involved.

The second thing I want to mention is just sort of a report on something. Our local area Agency on Aging, together with the Housing Law Project, which was mentioned here earlier by another speaker, and with AARP, have recently obtained a grant from the Artstone Foundation, the purpose of which is to work in our locale on predatory lending issues. We're going to do that as a combination of counseling, helping people that have gotten into difficulties, that aspect of it, and some elements of education. So we're hoping this will help our local situation.

Thank you.

MS. BRAUNSTEIN: Thank you very much.

MS. BLANCO: My name is Celia Blanco and I work at Sentinel Fair Housing. Sentinel Fair Housing is a nonprofit agency based in Oakland and we investigate and assist consumers with complaints and other discrimination in housing. And that includes discrimination in loans to purchase or refinance a home.

We have recently started to operate with Carol and others agencies in Oakland to investigate the complaints from some client of other loans. Some of the complaint people have made are feeling pressure to close the loan, loan terms, or a type of loan that's different than what the lender had initially put forth, receiving loan documents written in English when the terms of the loan were discussed in another language, for instance Spanish, loans with higher payments than the borrower said that they could afford, and high interest rates.

This year we hold two educational workshops in March and April where we tried to explain to our clients problems with predatory loans as well as their rights in connection with the loans. All these loans were no document and income stated loans, where the borrowers were not usually asked to provide any income information or verification.

Of the borrowers we've seen so far, all are either Spanish-speaking, Latino, or African-American homeowners who used brokers. And it's important that these type of loan be regulated and covered under federal law. And so written disclosures in Spanish or the language they were discussed would have made a difference.

That's all.

MS. BRAUNSTEIN: Thank you very much.

MR. DIAZ: Good afternoon. My name is Moses Diaz and I'm a staff attorney at the Fair Housing Law Project of the Law Foundation of Silicon Valley. And I thank you today for the opportunity to give you my comments.

First of all, I'd like to state that I think HOEPA is a great statute. The protections against certain prepayment penalties, balloon payments, and asset based lending for residential real property is great, but -- the statute has a lot of potential but not a lot of teeth at this point in time, and it's primarily because of the triggers.

In 2006 the trigger was either the greater of $528 or eight percent of the loan. While the homes in the greater Bay Area, eight percent of the loan is going -- is going to be a lot of money. And what tends to happen is there's no coverage. And yet we have some of the most vulnerable borrowers here in this area.

One of the problems here, HOEPA applies to refinance transactions. And what usually happens is when you refinance, you refinance for a higher principal amount. And the loan after the interest only period, the borrower -- because typically the subprime loans are interest only loans. After that interest only loan, the borrower has to start to pay the principal. And usually they can't afford to pay both interest and principal, so they have to refinance again and it starts a vicious cycle.

Where does the cycle end? Who knows? But what are the results? The ramifications are increase in inflation, because every time they refinance every few years, it's going to drive up the cost of the home. And every time they refinance, the principal amount of the loan is going to go up.

The borrower is never going to truly own their home. They're always going to be refinancing before that interest only period ends and they're never going to pay off the principal. The principal is just going to keep increasing and increasing and increasing. And they're really just a glorified renter because, in the end, they're never going to own that property.

I have a HUD1 here in my hand from one of the transactions that I analyzed. And the origination fee was five points, or $21,600, on a $432,000 loan. HOEPA couldn't help this person here. So that's one of the greatest areas where I think the Board of Governors can really make a difference.

And we've heard a lot -- you've heard a lot of other suggestions. And I also recommend that you increase the limitation period from one year to two years as well.

Secondly, I just want to touch briefly on the translation requirement because I have a lot of clients that come into me with these kind of issues. And they never know what the terms of the loan are. Even if the -- they don't -- aside from the promissory note -- they don't even get the disclosures in Spanish.

You only have to translate them one time and you can use them over and over again. So it's not a big cost. And the lending industry is always complaining about that. But you know what? If you want their money, translate their documents for them.

MS. BRAUNSTEIN: Thank you very much.

MR. DeRYAN: Good afternoon. Thanks for allowing me to speak. Gerald DeRyan. I'm representing the over one million AARP members and Nancy Pelosi and counselor's district. And as you can see, there's a great interest in AARP around here on what's happening.

I agree with what the gentleman just said, the same thing. The HOEPA -- this idea of eight percent and what it means around here and how it's just -- it just escalates everything and they never get out of it.

But I watching C-Span just the other day and the counselor from California and Los Angeles were complaining that this present administration is telling them to -- there's too many defaulted loans out there and sub loans. So these ones that are making all the payments and they're getting -- and eligible for new loans, they charge them extra percents, which is the worst thing possible.

Here are these people that pay, don't default, and you -- and to cover some of that over there, you're going to charge these people more. And I thought that was unbelievable. And that was right on C-Span.

But the problem with language, San Jose and L.A., San Francisco alone has over 47 foreign language groups in our public schools, 47. Just think of that. San Francisco we have seniors. We have the Senior Action Network composed of over 150 senior action groups in the city, of which AARP is a member, and they're all focusing on these things and this idea of the language and can't they understand it.

I'll give you one example, cell phones, which Public Utilities Commission is trying to get a bill of rights on that. They advertise full-page ads. And they look like they're selling you pictures of music. And what is selling you minutes? Way down there somewhere and you're paying $25 and next month is 200 and on.

And then the people -- they're lobbying people to -- they're not counselors. They're sellers and they're coaxing them into getting all these things. But when they get the bill, it is in English. They don't understand it. They don't get the disclosure. Same thing.

So these problems are -- so keep -- keep these bills up-to-date and listen to what the input is. Because I think people are doing a good job, but we have to tighten these things. Because -- we have to do it. And the low document loans and sub loans, we have to help these people. They're doing -- reward them. Don't put a further burden on it.

Thank you much very.

MS. BRAUNSTEIN: Thank you very much.

MS. BALDWIN: Good afternoon. My name is Laura Baldwin. I'm with the Monterey County Housing Alliance. I'm the executive director. We're located in Salinas, California. And we're a housing -- we're the only HUD-approved housing counseling agency on the central coast.

I'm here today to represent the needs of people who have been victimized by predatory lending practices in Monterey county, specifically predatory lending as it relates to mortgages. Every day I see the destructive effects of abusive mortgage loans and the clients that we serve in Monterey county.

Mr. and Mrs. Sanchez came into my office with their 16-year-old daughter several weeks ago. Their daughter had translated the loan transaction for her parents, who do speak English. They speak middle -- they have minimal speaking skills and their primary language is Spanish. They were in the -- they're in the low to moderate income levels.

And just to give you an idea of the characteristics of the loan papers that I reviewed, they're first-time home buyers. They purchased their home a couple of years ago. There was a total of, believe it or not, 13 points associated with this loan transaction, prepayment penalties that we calculated to in the sum of $12,000. There was a mandatory arbitration clause. There were also unnecessary insurance products tacked onto the loan product, to the loan papers, in excess of about $8,000.

On top of that, they were met with aggressive tactics to sign their papers immediately. When the disclosures were being discussed, they were asked only to go ahead and initial the boxes and that it would be explained later. They were promised copies of their loan payments to which they still have not received a copy.

And upon further assessment of their loan papers, we determined that they -- they have very good credit and were steered into a subprime or B and C loan when they could have qualified for a mainstream loan.

This is a family that -- where language and literacy is an issue. This is a family where, yes, they do speak English, but because the whole process of understanding loans is very complex and basically understanding the glossary of terms that are associated with the loan process is like learning a brand-new language. Language and literacy.

In Salinas, California it's the least affordable place to live in the nation. Why? Because it's highly desirable to live there. It's a beautiful place to live. Competition for homes is fierce.

And the reason I'm here today is to ask the board to please help us level the playing field by creating accountability, improved accountability standards, to please strengthen the anti-predatory lending and consumer protection laws that are in existence right now, and to also invest in housing counseling agencies that can be your greatest partner in making sure that not only are these predatory lenders armed with the tools -- armed with the tools to be able to continue in this practice but arm the consumers with the same tools and education and knowledge so that they can avoid becoming a victim of predatory lending.

Thank you much very.

MS. BRAUNSTEIN: Thank you much very.

MS. ORTON: My name is Eve Orton and I'm a member of AARP and a number of other organizations that deal with seniors.

And I would like to see SB 1609 submitted bill passed because it has a number of things that will help prevent some of the things we're talking about today.

It isn't -- the house that the person has as they get older starts falling apart. My friend, her roof is going. She needs a new car. So she's talking about a reverse mortgage.

And I know there's a lot of different languages. In fact, last count in San Jose was 84, the difference between languages and dialects. So that's hard on the industry, true.

But something should be made to happen to put it in dollars and cents so that they know how much their loan is going to cost, how much it's going to cost financing, so it's actually they can see it. Most people understand, no matter what language, if they see dollars and cents. And it should be taken care of.

And they need time to think it over after so they can take it home and there should be a demand that there's enough time after that.

I think that's all.

MS. BRAUNSTEIN: Thank you very much. And thank you to all our speakers.

The next group -- I just want to check. I had called two names who didn't come forward before, if they're here, Pearl Caldwell and Don Gerimonte. No?

Okay. We'll move on to the next group, Martha Jimenez, Leticia Gonzalez and Gerardo Gonzalez, Caroline Washington, Christy Leffall, J. Reyes Rios, Ricardo Corona, Marna Schwartz. Let's see if that pretty much fills the seats for now.

Okay. We'll get you the next group. We're not going to forget you.

Okay. Same as before. I just want to remind people you have three minutes. We have a timekeeper who will give you a sign when you have one minute left and then when your time is up.

And ask you to please speak directly into the microphones for purposes of the court reporter, as well as so everyone in the back of the room can hear you.

And with that we'll start, please.

MS. JIMENEZ: Hello. My name is Martha Jimenez and I'm a resident of the Bay Area. And I am here as -- to share my experience as a victim of predatory lending.

One year ago my sister and I decided to join together to be able to buy a home. And we were referred by a friend from our church to a Spanish-speaker broker.

We went to the broker, and in our first meeting with the broker, he discouraged us to have me as part of the loan on the basis that since they had a good credit score, which was about 750, they were able to afford a good loan without me. My credit score was a little bit more than 700. So they -- they trusted the broker and they went forward with the -- with a loan.

And all the communication that they had with the broker was in Spanish. All the loan papers that they received were in English. The broker discouraged us to -- or discouraged me and them to -- or he was not willing to communicate with me. Maybe because I asked too many questions. And he was more willing to work with them because they were the ones on the loan.

So after they signed the papers, I reviewed the papers and I was shocked to discover the loan that they got, which was very different from what he promised initially.

I took my sister and my brother-in-law to legal counseling and housing counseling. And when we went to counseling, we discovered that they had a loan with adjustable rate of 6.8 percent with a two-year prepayment penalty and a second home equity loan with an initial APR of 7.26 percent that adjusts daily.

Through counseling we discovered that if I had been part of the loan initially, they would have been eligible for a better loan.

This experience shows the need for loan products like this to be covered by federal law so that written documents are in the language that the people understand and that housing counseling be required before people sign this kind of documents.

Thank you.

MS. BRAUNSTEIN: Thank you very much.

MS. MARCUS: Hello. My name is Maria Marcus. I work here for the Federal Reserve Bank and I will translate for Mr. and Mrs. Gonzalez.

MS. BRAUNSTEIN: Thank you.

MS. GONZALEZ: My name is Leticia Gonzalez. My husband is Gerardo Gonzalez.

MS. MARCUS: Okay. They were interested in purchasing a home. They were -- they talked to a broker who was -- who helped them sell their previous home and look into buying a new one.

They told the broker they had $123,000 to put down as a down payment and they wanted their payments to be at $2,700 a month.

The broker -- all of the conversations were done in Spanish. All of the paperwork was in English. The loan -- the monthly payment ended up at $4,700 a month, which was more than the family could afford.

So initially the loan was an adjustable rate for two years. The payments actually went up this last month for a $1,000 because the loan that they did receive was adjustable after six months.

Initially when they were discussing the terms of the loan, the family said that they were only going to be able to give the, you know, $2,700 payment. And this is when the broker that they were dealing with said that she would personally lend them $1,000 a month so they could make their payment.

This went on for six months. And Mrs. Gonzalez has proof of the check stubs that she deposited into her account from this broker who was giving her monthly payments.

After six months, when the family talked to the broker, letting them know that the terms of the loan had changed and they weren't able to afford this anymore, the broker cut off all communication with the family and they haven't been able to get in contact with her since.

Her husband has, in fact, contacted the Gonzalezes asking for the $6,000 that they have loaned them to pay for -- you know, to help towards the mortgage.

So I think most of you understood that. They were told that there was going to be no penalties if they wanted to refinance. However, when they started the refinancing process, they had a $16,000 penalty if they want to refinance their home.

Currently they're paying the new -- it's almost $5,000 that they have to pay monthly and it's something that the family cannot afford. The Gonzalezes have eight children at home, so that cost is well and beyond what they had originally anticipated on paying monthly.

So the home insurance they're paying is $1,600 a year for their home insurance.

All the paperwork were in English. And they just feel, you know, that they were really betrayed by this person whom they trusted and is a Latina as well. So all of the conversations were conducted in Spanish.

So when they initially did all the paperwork, the house was 584,000. A week later, when they were closing, it was $604,000.

Thank you.

MS. BRAUNSTEIN: Thank you.

Just a question. Did you pursue this with legal services or --

MS. MARCUS: Acorn is the company that's representing them. And I believe they have a meeting on

Monday with a lawyer.

MS. BRAUNSTEIN: Thank you very much.

And thank you, Maria.

Next speaker.

MS. WASHINGTON: Good afternoon. My name is Caroline Washington and I am a client of the Acorn Housing.

I first wanted to refinance my house to lower my payments. A couple befriended me from my church and said they were mortgage brokers and they could help me.

In November of 2001, I refinanced my then mortgage of 52,000 to a new loan of 152,000. I never received any paperwork about the loan and these brokers didn't even give me information about what happened.

In July of 2003, these same brokers convinced me to refinance again and to take out some cash and lower my payments. This time the loan was far -- this time the loan was for $202,000. I only got a few thousand dollars from the transaction to pay off a few credit debts. But my payments were higher than -- were higher each month instead of lower.

During this loan transactions, the broker would come into my home and take important loan documents away and they never brought them back.

In May 2004, the same broker refinanced my house with a new loan of $240,000. My new loan payments were $1,678 per month, while my only income from retirement and

Social Security was $2,155. I could not afford this and I began to fall behind on payments.

These brokers then suggested that I move to a smaller place and sell my house to some people they knew. Over the last year, I've had numerous calls from people who say they can help me, really, just -- they just want to buy my house from me. It's been hard for me to identify who was trying to help me and who was trying to cheat me.

This past winter I was assigned a conservator and a case worker from Adult Protective Services to help me sort out financial problems. Unfortunately it was too late. Last month my house was sold in a foreclosure sale, and after living in my home for over 25 years, I'm facing eviction.

If I had had mortgage counseling before refinancing, I could have avoided most of these problems. I just didn't understand what I was getting into.

I really hope that laws will change to protect homeowners, especially the elderly, because we need a lot more help understanding the refinancing and mortgage of loans.

Thank you for your time.

MS. BRAUNSTEIN: Thank you very much.

MR. CORONA: My name is Ricardo Corona. I'm a counselor for MEDA, Mission Economic Development Agency.

And I work with Latino population. I can say that

90 percent of my clients are Latinos and 40 or 50 percent of my clients are just Spanish speakers.

I try to help them to buy their first home. This is why -- in San Francisco. And lately I've been having a lot of cases, a lot of calls from people who want me to help them to have a -- help refinance their home or find a better loan because they can't afford the monthly payment.

And I will say just three things that I find is the most commonly -- that I find most common from my client. One is the stated income loan. Many borrowers are loan based on stated income loan, often inflated by the broker with no documentation to show the borrower are able to afford the loan.

Most of the time the broker tell the borrowers that in order to help them to buy a home, he will make it up an income that will allow the borrower to qualify for a higher loan amount. The problem with this is that a borrower cannot afford the loan that they qualify for.

For example, I had a client who her monthly gross income is around $3,000 a month and was qualified by a lender for a stated loan, without any documentation required, that was based on a salary of $16,000 a month. The monthly mortgage payment were more than 5,000 or more. So she can't really stay at home. We tried to help with selling the home, but he is -- there is nothing at this point.

Reasonable high interest rate loan are often offered with what seem to be a reasonable interest rate. However, if the loan was fully examined, one would find that the difference between an interest rate and the actual annual percent rate, APR, is substantial and ultimately means that the loan is very expensive and predatory.

Again, I have a client who requested to have a six percent interest rate, but the broker never ever said to her that APR was 10.50 percent, which means it's a very high-cost loan. She's unable to make the monthly payment now. And she has been in that new home for two months. And it's not -- no longer able to pay that amount of money.

And the other thing that is very common is they never ever explain their document. Broker were great at trust with the potential borrowers. This mean that the borrowers are dependent on the information that the lender provides, in particular not English speaker. Borrower rely on their mortgage lender to help them understand the loan documents.

Predatory lenders encourage borrower to sign document without truly understanding all of the information. They may direct buyer to sign here and there, instructing their client that this paperwork is merely procedural.

If the communication for non-English speaker occurred in native language, the document are always still written in English and, therefore, there's limited English, borrower can easily sign document without a full understanding of their contents.

Thanks.

MS. BRAUNSTEIN: Thank you much very.

MS. SCHWARTZ: Hello. My name is Marna Schwartz and I also work at MEDA, Mission Economic Development Agency. I coordinate the homeownership program. We also help to coordinate an anti-predatory lending committee and a campaign around that. And I would like to share with you a couple of concerns with regard to pre-purchase predatory lending.

In particular, there's a lot of concern about the adjusted rate mortgages, the ARMs right now, because we see many potential buyers getting into dangerous loan situations since there's been a visible increase in adjustable rate mortgages and interest only and 100 percent financing loans. These loans can be perilous for first-time home buyers if buyers are not fully versed in the consequences of market fluctuations.

In particular, we have seen buyers get into adjusted rate mortgages whose interest rates and ultimate monthly mortgage payments are quick to float above the new buyer's ability to pay. Consequently, the buyers become at risk of losing their newly bought homes as they get further behind in their payments, moving from default ultimately to foreclosure.

Also, because we live in such a high-cost area, there's additional concerns that are very specific to this Bay Area. So buyers in the San Francisco and the Bay Area are interested -- are at increased risk for predatory loans because they become desperate to qualify for loans that would afford them homes in such a high-priced area.

I want to give you an example of what that may look like. The median sales price here in San Francisco is $750,000. And that would require an income of over $150,000 with no debt, a $50,000 down payment, and less than a 6.75 percent fixed interest rate for 30 years.

Well, the folks that we work with and that many of these organizations represent are not making that kind of salary. And they are then trying to afford homes that are way out of their price range and are doing so by using loans that get them into a lot of trouble.

Low and moderate income buyers are then pressured to lie about their incomes as Ricardo mentioned, especially through stated loans, in order to qualify for loans that are -- can afford a purchase price of that $750,000.

And finally, as Ricardo also mentioned, we wanted to talk about language. We work with Spanish speakers. And although that we've seen a growing number of real estate professionals, mortgage lenders in the field who are

Spanish-speaking, the documents as mentioned earlier are not yet in a language that helps folks understand what they're getting into.

Also, we find that realtors and lenders build that trust and ultimately can lead their clients into a delinquent state.

So thank you very much for your time and I hope you take these comments seriously.

MS. BRAUNSTEIN: Thank you.

And before we go, did you want to make a statement?

MS. LEFFALL: Yes, please.

My name is Christy Leffall and I work with Acorn Housing in Oakland, California. Thanks for the opportunity to speak today.

You can see some of our clients are here that have done mortgage counseling at our office. And primarily what we do is we work with folks who are facing predatory mortgages and possibly delinquency and foreclosure.

I just want to talk about some of the things I see in counseling every day when I'm meeting with these folks. A lot of the target population is represented here, families that don't speak English, the folks that are elderly and don't have the whole capacity to understand what the mortgage loan and refinancing process is like.

A lot of folks don't have, you know, maybe family that can help them to come to counseling or even participate in sort of the loan documentation signing. So you get a lot of people who just aren't, you know, ready to sign on loan documents and get caught up in these sort of situations.

Some of the main -- the loan types that I see a lot are option ARMs, negative amortization loans that clients have no clue they have until they come to counseling. See lots of families that come in and have, you know, two loans instead of one loan. They don't have any clue why.

Interest rates are much higher than they were told they'd be. Even sometimes the payments. The payments sometimes are even more than the family makes in income. So they're told, "Okay. Well, you can refinance in six months," or, "I'll help you pay," things like this that, you know, sound totally crazy to us.

Certain people are, you know, representing themselves as, you know, a friend of the family, someone that, you know, speaks their language. And this is a problem that's among brokers, among realtors.

And other things I see, loan flipping, as with Mrs. Washington's case. She was refinanced I think four times within five years, with the same brokers, you know, time after time.

And so having mortgage counseling prior to doing refinances, especially in the subprime market with elders, is really, really crucial. And that's one thing I want to pressure on the Federal Reserve Board to put that into law nationally. Also, obviously loan documentation, having that be in a language that the clients can understand.

And those are my main comments. And one more thing would be obviously the housing prices in the Bay Area are much higher than the HOEPA protection. So that's a huge, huge thing happening. You know, families come in every single week with loans in excess of $700,000, $500,000, in Oakland, San Francisco. So those are the folks we need to really be protecting with legislation.

MS. BRAUNSTEIN: Thank you much very. And thank you to all our speakers on this -- in this group.

We have a few people left still on the sign-up sheet, so I'll call them forward. If J. Reyes Rios is here, Ana Rivera, and Nery Hartschen is here, as well as we never did hear from either Pearl Caldwell or Don Gerimonte. If either one of them are here, this is your final opportunity to come forward.

Okay. Thank you much very. And we all -- I've seen you before right?

MS. JIMENEZ: I will translate.

MS. BRAUNSTEIN: Okay. No problem. That's fine.

And we will go forward with the same rules. I think people have heard them now. Three minutes. You'll get a signal from the timekeeper.

We ask that you start by stating your name and if you're from an organization what the organization is and to speak directly into the microphone so the court reporter can hear and people in the back can hear.

And with that you want to start.

MS. RIOS: Hello. My name is Silvia Rios and this is her brother-in-law Reyes Rios. And thank you for listening to us.

We decided to buy a home. They referred us, someone, a realtor or broker, who spoke Spanish of course. We told him the payments that we could make. He said okay and asked the information to him, or from him.

He took us to see homes. We saw one that we liked. Time passed by. He did not call us. He called us later and said that the house was already sold.

He called again and to ask if we could see other houses. We went. We saw another one and we liked it. He put forward the offer and he said -- but he never called.

The papers were in English. He signed. Later he called again and said, "I need you to come and sign." He went to sign the 4th of May. And there he was the owner of the house.

He never sent any papers. He never called. I'm mad with him. He gave until the 10th. The broker said, "Come here, sign," but he never said for what. After signing the broker told him for what, "The house is yours."

The house said in the paper four rooms, two bathrooms, but there, right there, the broker said it only has registered three bedrooms and one bathroom.

They gave them until the 10th to call in, say whether he wanted the house or not. Mr. Reyes called the 8th of May, "I do not want the house because it doesn't have what you told me." He said, "The house is yours. We did not place a gun on your head so that you could sign."

We have lawyers -- we have lawyers so that we don't go to court. But I don't understand why. Court why?

Someone already looked at our papers and we are scared for the payments. The broker never explained the consequences, anything. He did not explain the payment was going to increase.

We would go and see houses of some prices and we would ask can we afford this house and the broker would say, "Yeah, we are right there. We are right there."

MS. BRAUNSTEIN: Can I ask a question? Have you gone to see anyone like a housing counselor, like Acorn or anybody like that since this has happened?

MS. JIMENEZ: They have already went to Lao Family.

The papers say that the interest can go up to 18 percent. Even the price of the house was not initial price that they initially heard from the broker. The papers had a different number than what the broker told them initially.

MS. BRAUNSTEIN: Thank you much very. And we wish you good luck.

MS. RIOS: Thank you for listening to us.

MS. HARTSCHEN: Good afternoon. My name is Mary Hartschen and I'm a volunteer for AARP and I'm also a commissioner on the advisory board to the Area Agency on Aging in Alameda County and CSL, California Senior Legislature. So as you can see, I'm strictly on the senior side.

But from what I've been hearing, this involves everybody all around, young, old, or whatever, mostly Latinos, which I'm one of them. And there's not much that I can say because I think that my colleagues at -- that are also volunteers in AARP have said everything, very grand, in a grand way of anything that I could add to it.

But I will say that we need a lot more accountability on the people that do the lending, and we also need people like the ones that are here that are sentinels and watch over seniors and everybody else because it seems that the cheating goes on for everybody, not only for seniors.

So what I think -- the reason I'm here is because I'm asking from the Board of Governors and the Federal

Reserve Board that maybe they should take a long hard look at the language which is written regarding mortgage loans so that maybe perhaps people that will be needing a loan won't be having this problem. And if the board really looks at it, maybe they'll insist on having a meaningful, protective predatory lending that won't have so many problems.

Thank you.

MS. BRAUNSTEIN: Thank you very much.

And I'd like to thank everyone who participated today, all our speakers during the last hour, as well as all our panelists.

I'd also like to say thank you, a big thank you, to the San Francisco Federal Reserve Bank, who hosted us today and did an excellent job with that.

And I want to thank Jack and everyone else, John Olson, and everyone else, our timekeepers and everyone who was involved in that.

And with that our meeting is adjourned.

(Whereupon the hearing was concluded at 4:15 p.m.)

CERTIFICATION

I, the undersigned, a Certified Shorthand Reporter of the State of California, hereby certify that the foregoing hearing was held at the time and place herein stated; that the hearing was reported by me, a Certified Shorthand Reporter and a disinterested person, and was thereafter transcribed under my direction into typewriting; and that the foregoing is a full, complete, and true record of said hearing.

I further certify that I am not of counsel or attorney for any of the parties in the foregoing hearing, nor in any way interested in the outcome of the cause names in said action.

IN WITNESS WHEREOF, I have hereunto set my hand this ______ day of ________________, 20____.

____

LAURA A. REDING, CSR NO. 9711