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We are in the midst of a mortgage catastrophe. The Mortgage Bankers Association recently reported that of the 44 million active mortgages throughout the country, approximately 342,000 entered into foreclosure during the third quarter of 2007, the highest rate of foreclosures in more than 35 years. Overall, nearly 450,000 properties were in some stage of foreclosure during the third quarter of 2007, up 30% from the second quarter. Nationally, the foreclosure crisis is worsening rapidly and is expected to deteriorate further. The number of foreclosure filings nearly doubled for the third quarter of 2006 to the third quarter of 2007. One out of every seventeen mortgage holders is no longer able to make payments on time, the highest rate in over twenty years.

This foreclosure crisis has been fueled by the phenomenal growth of predatory mortgage loans in the market. Over the course of several years, sub-prime lenders routinely made money available in exotic packages (featuring hybrid adjustable rate mortgages, low and no-document loans and interest only loans) to unqualified borrowers who had no realistic means of keeping up with their loan payments over the long term. A rash of defaults, and the ensuing foreclosures, inevitably followed.

National Consumer Law Center and our co-counsel) believe that there has been discrimination in the sub-prime mortgage lending industry that has had a disparate impact on African American and Hispanic consumers. The racial discrimination has resulted in those consumers paying higher interest rates, and suffering higher foreclosure rates as a direct result, than comparable non-minority mortgagors with similar credit scores.

Approximately 150,000 adjustable rate loans are resetting to higher interest rates every month. In 2008, $362 billion in subprime loans will reset to higher rates. Treasury Secretary Paulson has claimed that 1.8 million subprime mortgages are scheduled to reset to higher rates over the next two years. The Joint Economic Committee of Congress predicts that from 2007 to 2009 there could be nearly 2 million foreclosures nationwide on homes purchased with subprime loans alone.

There is no simple solution to this unprecedented set of circumstances. Litigation has played a role in this battle, however. Private and legal services attorneys have represented individual homeowners attempting to save their homes in court, sometimes by raising affirmative defenses and counterclaims, when allowed, in judicial foreclosure proceedings. In those states that provide for non-judicial foreclosures, affirmative cases can sometimes be brought to assert claims and defenses in an attempt to enjoin the foreclosure. There never will be enough lawyers available, however, to insure that more

than a small minority of, let alone every, homeowner will be entitled to legal representation in their individual foreclosure cases.

Rather than proceed on a person by person basis, therefore, some attorneys for homeowners have been exploring innovative litigation strategies for cases that might have a broader impact on the sub-prime mortgage industry and the foreclosure crisis it has created. Their efforts have been supplemented by state and municipal cases brought by governmental authorities on behalf of the citizens facing foreclosures in their jurisdictions. These cases may have an important role to play in providing meaningful, timely relief for large numbers of homeowners who are in default or on the verge of going into default. They also may be the basis for effective moratoria on on-going foreclosure proceedings.

Not surprisingly, there is a glaring race component that unfortunately is manifest in the midst of the predatory mortgage foreclosure disaster. United for a Fair Economy reports that the subprime mortgage crisis will cause African Americans to experience wealth losses of between $71 billion and $122 billion over its duration and that the racial bias of subprime mortgage lenders accounts for a 40% difference in losses between whites and people of color.

Class Action Litigation

The National Consumer Law Center has joined a team of prominent lawyers that are engaged in a series of national class action cases filed by African American and Hispanic consumers against individual subprime lenders across the country. Brought under the Fair Housing Act ("FHA") and the Equal Credit Opportunity Act ("ECOA"), the cases focus on the disparate impacts of the alleged "Discretionary Pricing Policies" of those subprime companies which authorized their loan officers, brokers and correspondent lenders to include subjective, discretionary charges and interest rate mark-ups in the finance charges of home mortgage loans they originated. These charges and mark-ups allegedly are totally unrelated to a borrower's objective credit characteristics and result in purely subjective charges that affect the rate otherwise available to borrowers.

The "Discretionary Pricing Policies" cases stem from the practice of subprime lenders determining a risk-based financing rate or "Par Rate" for each loan applicant. The "Par Rate" is based upon objective risk-related variables such as the individual's credit bureau histories, payment amounts, debt ratio, bankruptcies, automobile repossessions, charge offs, prior foreclosures, payment histories, credit score, debt to income ratios, loan to value ratios and other risk-related attributes and variables.

After arriving at a risk-based rate, certain subprime lenders authorize their loan officers, brokers or correspondent lenders to mark up the objective "Par Rate" to an amount limited only by the "caps" established by the lender's policies. This markup (sometimes called a "Yield Spread Premium" or "YSP") is not based on a credit applicant's score or any other risk-related assessment. On the contrary, the mark-up is

subjectively set pursuant to, and within the limits of, policies specifically delineated by the subprime lender.

The plaintiffs in these cases allege that the Discretionary Pricing Policies of the subprime lenders, although facially neutral, have a disproportionately adverse effect on African Americans compared to similarly situated Whites in that the African Americans pay disparately more discretionary charges (both in frequency and amount) than similarly situated Whites. As a result, the subprime lenders' credit pricing systems cause African Americans to pay more for mortgage financing than the amounts paid by White customers with identical or effectively identical credit scores.

These cases should be compared to the so-called "reverse redlining" class action complaint recently filed by the National Association for the Advancement of Colored People ("NAACP"). The case alleges violations of the FHA and the ECOA in addition to racial discrimination under the Civil Rights Act, against 12 banks and lending institutions. Specifically, the law suit claims that the defendant mortgage lenders have engaged in institutionalized, systematic racism by targeting African-American homeowners for subprime mortgage loans at rate that is disproportionate to the number of Caucasian borrowers with the same qualifications receiving such loans. The NAACP asserts that the subprime industry has attempted to maximize its profits by directing or "steering" African American borrowers with relatively good credit to subprime mortgages. The causes of action included claims, in the alternative, for both intentional discrimination by the subprime mortgagees and a discriminatory impact created by the policies developed and employed by the subprime mortgagees to steer African American borrowers to their subprime loans.

In another variation on the theme, on January 8, 2008, a lawsuit was filed under the Fair Housing Act on behalf of the City of Baltimore against Wells Fargo, Bank, N.A. ("Baltimore") The City alleges that Wells Fargo Bank intentionally targeted Baltimore's minority communities for predatory loans with discriminatory and unfair terms. The City claims that Wells Fargo's discriminatory lending practices have resulted in extraordinarily high rates of foreclosure in Baltimore's minority neighborhoods - foreclosures that ultimately cost the City millions of dollars in lost tax revenues, added fire and police costs, court administrative costs, and social programs needed to maintain stable and healthy neighborhoods.

The NAACP and the Baltimore cases rely, in significant part, on being able to prove actual knowledge and intent by the defendants as part of their claims. On the other hand, NCLC intends, with its co-counsel, to pursue a litigation strategy in its civil rights cases similar to the approach that was successful in the recent series of auto finance discrimination cases brought by NCLC under the ECOA. These cases, based exclusively on discriminatory effect claims, do not require proof of either the defendant's intent or knowledge. Rather, the disparate impact in each of NCLC's cases will be proven statistically by multiple regression analysis using information from the mortgagees' own files.

Our litigation, as well as the other disparate impact litigation brought against sub-prime mortgage lenders by municipal and state government entities and public interest organizations, has taken place in a vacuum created by a complete abdication of responsibility by the Justice Department and other federal agencies operating in this area. Enforcement should be a joint coordinated and collaborative effort between federal government watchdogs, state and local officials and private rights of action. For now, however, the federal government has been absent (if not obstructionist) within the equation.