October 17, 2008

RE: *Written comments of the California Reinvestment Coalition and Law Foundation of Silicon Valley to the National Commission on Fair Housing and Equal Opportunity*

Dear Commissioners:

The Gonzales family wanted to purchase a home, and told their mortgage broker they could only afford to pay $2,700 per month. Their conversations with this broker were all in Spanish, yet their loan documents were written in English, a language they could not read. Although they were told they would be paying much less, their first monthly payment was $4,700 with an interest rate that adjusted up in 6 months. When their payments continued to increase and they started to complain, their broker stopped returning their calls. Their monthly payment quickly rose to $5,000 per month, nearly twice what they could afford. If they had refinanced, they would have suffered a $16,000 prepayment penalty, which was written into their English loan documents and not explained to them upon signing.

Caroline Washington, an 83-year-old African American woman living in San Francisco, was induced by her broker to refinance her home three times in three years. Her $52,000 loan ballooned to $240,000, with monthly payments of over $1,600, representing nearly all of her fixed income. When she started to go into foreclosure, she received calls and solicitations from several companies offering to "help" her. She said, "I didn't know who was trying to help me, and who was trying to cheat me." Ms. Washington lost her home.

Both the Gonzales family and Ms. Washington testified at a Federal Reserve hearing on mortgage practices June 16, 2006 – more than two years ago. They represented the very beginning of a foreclosure crisis that will last years and claim millions of victims. The federal government failed to respond in any meaningful way to the discriminatory lending practices that led to this crisis, a failure that must be rectified lest this series of events be repeated in the coming years.

The California Reinvestment Coalition (CRC), based in San Francisco, is a nonprofit membership organization of 250 nonprofit organizations and public agencies across the state of California. We work with community-based organizations to promote the economic revitalization of California's low-income communities and communities of color. CRC promotes increased access to credit for affordable housing and community economic development, and to financial services for these communities. Over the last few years, CRC has focused increased

attention on fighting predatory financial practices in California, including high-cost predatory mortgage lending which has disproportionately affected people of color and has been the catalyst for the foreclosure crisis we are now experiencing.

Public Interest Law Firm (a program of the Law Foundation of Silicon Valley)'s mission is to protect the human rights of individuals and groups in the Silicon Valley area who are underrepresented in the civil justice system. PILF accomplishes its mission by leveraging the skills and resources of pro bono attorneys to provide high quality representation in class action and impact litigation, advocacy in state and local government, and litigation support to local legal services programs. PILF focuses its efforts on behalf of elders, youth, individuals with disabilities, those who are frequent victims of illegal discrimination and those who are poor. In the past few years, PILF has litigated two cases in federal court on behalf of borrowers who we believe were targeted for predatory subprime loans based on their actual or perceived lack of fluency in English. We have also advocated for additional protections for borrowers at the local, state, and national level, often in collaboration with CRC.

Every business day, 1,300 homes go into foreclosure in California. Many of these homes are occupied by working families, seniors, immigrants, and people of color who were targeted because of their membership in a protected class by unscrupulous lenders with unaffordable mortgages. The impacts of these foreclosures on neighborhoods are devastating: lower property values for neighboring residents, blight, increased crime, less tax revenue to local governments, and larger numbers of displaced tenants and foreclosed homeowners competing for limited affordable housing opportunities.

Much of the current foreclosure crisis is rooted in the subprime home loan market, where lenders make more expensive loans to borrowers who are deemed "credit-impaired" or otherwise unable to qualify for a conventional, prime loan. In 2006, subprime lending was a $600 billion industry that made its money trapping borrowers, often people of color, in bad loans.

Subprime lending has meant that the most critical fair lending problem for neighborhoods of color has fundamentally changed from "redlining," where lenders discriminate against neighborhoods of color by refusing to issue home loans there, to "reverse redlining," where unscrupulous originators target neighborhoods of color for more costly and more risky home loans. It appears that federal enforcement of the fair housing laws has yet to catch up with this paradigm shift.

Study after study has shown that people and neighborhoods of color are much more likely to be stuck with higher-priced subprime loans than white borrowers. In 2006, over 45% of all home loans made to African-American borrowers in California were higher-priced subprime loans, while only 19% of home loans to white borrowers were subprime. Over 43% of home loans to

Latino borrowers were subprime. And as a whole, neighborhoods of color in California were 2.7 times as likely to get subprime loans as white neighborhoods.

To put that in context, the former Attorney General for the state of New York sued Countrywide, relying on similar data, but where the lending disparities were smaller than what we see in California for the whole industry. The New York A.G. and Countrywide entered into a settlement agreement, at which time the A.G. stated that even after reviewing more detailed information from borrower loan files, Countrywide could not fully explain why African American and Latino borrowers were more likely to get costlier loans.

The New York Attorney General actually also sued 4 large national banks - Citibank, JP Morgan Chase, HSBC, and Wells Fargo – citing similar propensities to charge people of color more for home loans than for whites, without apparent legitimate justification. In a telling statement, the A.G. was blocked in his efforts to purse these four banks by their federal bank regulator, the Office of the Comptroller of the Currency (OCC), which in essence argued that it was the only regulator with the authority to enforce the Fair Housing Act's prohibitions against discrimination with regard to its national banks. The OCC has taken no apparent enforcement action against any of these banks.

This raises the larger point that our current regulatory environment encourages a race to the bottom, where regulators are loathe to enforce fair housing and consumer protection law for fear of banks leaving for another regulator. A regulatory agency that does not attract enough banks that wish to be regulated by it runs the risk of losing the prestige, authority and fees that may come with having a large number of licencees. In this environment, it is not surprising that the OCC and the Office of Thrift Supervision (OTS) have competed to be deemed to have the strongest preemption authority.

In a similar way, Republic Bank of Kentucky is currently seeking to switch to an OTS charter, reportedly because its current regulator, the FDIC, has raised too many concerns about Republic's involvement in high-cost tax Refund Anticipation Loans and payday lending. Such regulator-shopping undermines the ability and the incentive for regulators to stand up for consumers and protected classes. These issues must be addressed in any discussion of reforming our regulatory structure.

As a result of disparate subprime lending enabled by our flawed regulatory structure, CRC estimates that borrowers of color in California (many of whom could have qualified for prime loans) paid billions of dollars more than their white counterparts over the last few years. This means billions of dollars of lost equity that families could have used to start a business, finance an education, prepare for retirement, or pass on wealth to the next generation.

During this time, brokers pushed loans that did not make sense, and in many cases were fraudulent. Lenders responded to growing competition by lowering underwriting standards and creating incentives for brokers to sell problematic option-ARM and stated-income loans. This was all done to feed the appetite of Wall Street securitizers and investors who failed to screen out the financing of predatory loans. Unfortunately, and despite repeated warnings from CRC and its allies about these practices, the federal and state regulators charged with overseeing these actors stood by, unmoved by the cries of consumers. It was only in the past few months, when these toxic mortgages began causing pain to investors the lenders who made loans that should not have been made, that the federal government has swung into action to, ironically, bail out the very people who caused this crisis. The real victims are still left without recourse.

As lending standards plummeted, borrowers like the Gonzales family and Ms. Washington began to fall towards foreclosure. With more and more borrowers defaulting on the loans they could not afford to pay and probably should never have been given, subprime lenders started to go out of business by the hundreds.

But even though problematic lenders went out business, their risky loans remain in our neighborhoods, continuing to explode into foreclosures that harm communities. An analysis by CRC and allies showed that neighborhoods of color in seven metropolitan areas throughout the country were much more likely to be saturated with loans made by subprime lenders who went out of business for making too many bad loans. In Los Angeles, the market share of high-risk lenders was 9.5 times higher in neighborhoods of color than white neighborhoods.

Now, as hundreds of thousands of California families fall into foreclosure, focus has shifted from bad lending practices to bad servicing practices, which deny families a fair chance to remain in their homes.

Shockingly, there are virtually no rules, reporting obligations, or regulatory oversight which bind loan servicers in their dealings with borrowers seeking to avoid foreclosure. As such, it should not be surprising that in three CRC surveys of home loan counseling agencies serving over 10,000 borrowers per month, the most common outcome for homeowners cited was foreclosure.

As people and neighborhoods of color are disproportionately impacted by subprime lending on the front end, so too are borrowers and their communities disproportionately impacted by foreclosures on the back end, creating a double victimization that threatens to dramatically erode wealth in affected communities.

There are ways to alleviate the devastating impacts of foreclosures. Policymakers must act quickly, and pursue solutions that match the magnitude of the problem we face, including:

- Imposing a moratorium on all foreclosures related to predatory loans.

- Requiring that servicers offer long-term, affordable loan modifications for borrowers trying to stay in their homes, including reform of the Bankruptcy Code to allow judges to modify the terms of homeowners' mortgages.

- Requiring detailed and public reporting by each company about whether they are truly working to keep borrowers in their homes for the long term.

- Enforcing consumer protection, Community Reinvestment Act, and fair lending laws to ensure that low-income neighborhoods and neighborhoods of color are neither targeted for high-cost and abusive products, nor ignored by mainstream financial institutions. Ironically, we now face the prospect of a re-redlining of neighborhoods of color, as these "emerging markets" of yesterday are labeled the "declining markets" of today, deemed too risky by the same corporations that saturated these communities with subprime and option ARM products. The regulators and all responsible lenders cannot allow this to occur to neighborhoods that are now in dire need of credit in an effort to stave off a historic loss of wealth by households of color.

- Reforming the bank regulatory structure so that banks cannot choose their regulator, and so there are no incentives for agencies to refrain from regulating.

- Prohibiting predatory lending practices that will lead to a future crisis if we do not act responsibly. A recent CRC survey of 50 community-based organizations providing services to families at risk of foreclosure prioritized the following actions:

    - Ban abusive practices like prepayment penalties and Yield Spread Premiums;

    - Prohibit brokers and lenders from steering borrowers into more costly products than they qualify for;

    - Require the translation of key loan documents where loans are negotiated in a non-English language;

    - Increase penalties for wayward brokers so they will not continue to perpetrate abuse in communities; and

    - Hold Wall Street firms and investors liable for financing predatory loans.

In addition to the much-needed legal reforms discussed above, increased federal enforcement of fair housing laws in the mortgage lending context is critical given the wide-scale nature of this problem and the lack of comprehensive state, local, and private enforcement mechanisms. First, many of the institutions that have issued predatory loans are federally regulated, severely limiting the ability of state regulators to police them. And even as to the lenders and brokers

over which the state has authority, the agencies charged with oversight are chronically underfunded and understaffed, rendering them of little use. Locally, while many District Attorneys are making a valiant effort to prosecute the worst of the worst mortgage brokers, in our experience they are too often simply overwhelmed by the volume of evidence, the complexity of issues, and the tactics of aggressive defense counsel. And even successful criminal cases are focused on the acts of brokers, not the lenders who ultimately bear significant responsibility for these practices. Further, neither state nor local efforts have focused on the fair housing implications of predatory lending, approaching it from a criminal or consumer law perspective. Finally, private enforcement is very challenging; private for-profit attorneys shy away from these complex, time-consuming, and expensive cases, and non-profit legal service providers whose resources are already stretched thin can only satisfy a fraction of the community's need for legal representation. HUD and DOJ's Civil Rights Division should enter the fray to vigorously investigate and, where appropriate, prosecute lenders who have violated the FHA and other fair housing and fair lending laws.

The Gonzales family and Ms. Washington testified that they hoped the laws would change soon to help homeowners struggling to remain in their homes.

Over 2 years and millions of foreclosures later, so do we.

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To view a short documentary about the foreclosure crisis, and for more information, visit www.calreinvest.org