Paula Rush
http://lenderliabilitylaw.com/

June 18, 2007
Docket # OP-1288
Federal Reserve Board HOEPA

After attending the HOEPA meeting on June 14, 2007 I've changed my comments to reflect arguments that I heard from both sides of this debate. I was looking for rational explanations, and nuances of common ground. Building on that thought, I was searching the rhetoric for the federal regulatory intentions and what the industry objections are based on. The meeting did enhance my understanding of the problem and revealed new insights. The problems are well documented so I was trying to focus on the solutions. The industry, it seems, doesn't want any solution imposed by way of regulations and the consumer advocates are saying we've tried it your way, now we need intervention. In this stance no common ground can be achieved.

The first rule of fixing any problem is everyone has to agree that there is a problem. It is well tested premise that denial leads to inaction. I feel that's where this industry is and possibly the Federal Reserve.

Just today I read this quote, "In my opinion, the turmoil in the sub prime market is small potatoes." - Federal Reserve economist Richard Anderson told a luncheon of the Chartered Financial Analysts Society of Louisville. This is a very ominous sign. If no one feels the problem will affect the overall economy, nothing will be done. To refer to the sheer volume of foreclosures in the terms of small potatoes is an insult to humanity. I don't see the logic behind the statement.

In addition, I delayed in sending in my comments and now two Bear Stearns hedge funds are on the verge of collapse. Is everyone asleep at the wheel? To deny the overall situation has the potential to affect the entire market is not rational.

To drive home this point I will call your attention to an excerpt from (Reuters) May 24, 2007.
Alan "Ace" Greenberg, chairman of the executive committee at Bear Stearns Cos. Inc., the No. 1 U.S. issuer of mortgage-backed securities, downplayed the impact of sub prime lending woes on U.S. capital markets. He called the last few months a weeding-out process. "I think the sub prime (problem) has been blown completely out of proportion," Greenberg said. Sadly, only a few weeks later the truth at Bear Stearns comes out.

Finally, consider this, "Option ARMs are the best-executing product in the market right now, despite the market noise," said Brad Morrice, chief executive officer at Irvine, California-based New Century Financial Corp. The company is selling non-prime loans at about 102 1/2 cents on the dollar, compared with option ARMs "north of 104," he said." He said just before they went under and left everyone holding the bag!

It isn't hard to connect all the dots. The foreclosure rates are rising due to adjustments in arms tied to rising interest rates. Interest rates are continuing to rise. The housing market stagnation started and everyone is beginning to discover that prices were artificially high due to the irrational lending practices and inflated appraisals. The fallout started as rising interest rates caused foreclosures and illuminated all the loose lending, illegal practices, and lax underwriting practices. The appraisers, brokers, lenders, title companies, and Wall Street had a hand in the mess. Now the glut of foreclosures and tightening credit standards will combine to continue to depress the housing market even further. So this is where we are now. In the downward spiral which is gaining momentum. There is no sign of a turnaround. Every sign points to this getting worse.

The issue can't help but spill over into the overall economy, and unless everyone is in total denial, it has already begun to do this. Alt-A mortgages are going to default in record numbers because although they may have started out as slightly less risky, the overall downward trend on the housing market and rising interest rates will also force many of these loans under. The majority of these loans were no doc and we know now the damage this has caused. Are you watching the insidious next bomb getting ready to drop? Pay Option Arm loans will default in epic numbers as loans recast and houses are worth less then what is owed at the same time payment will double for borrowers. As borrowers walk away, lenders will have to reveal the phantom profits were just that, "phantom." Every financial situation has its breaking point. Reports are hard to ignore pointing to a slowdown in consumer spending, a negative savings rate, housing market value declines and escalating foreclosures.

I believe everyone is caught somewhere between denial, and possibly an even more sinister place, a continuing attempt to hide the truth. GREED has fueled this problem; DENIAL will only prolong and exacerbate the problem. Why is an industry which states, it's just the "bad actors," so bent on anyone acting to correct the problem?

If a robber stole $500 from another person, they would be criminally tried and convicted. In this industry, illegal practices have proliferated and the result has been millions of dollars stolen from consumers through a myriad of techniques and hidden charges. Overcharges, junk charges, illegal charges, and unconscionable charges have become the normal way of doing business. Kickbacks, hidden through fee sharing sham affiliated entities have fueled fraud and deception. Serial refinancing stripped equity based on over inflated appraisals.

False Advertising Tricks of the Trade. You don't need to look very far to see the false advertising everywhere. Please consider that everyday someone is taken in by a cleverly designed ad to draw them in and mislead them. The industry sells with a totally fraudulent presentation from the beginning using aggressive lending practices. Madison Ave style loan advertisements were designed to mislead borrowers into taking loans they could ill afford. Pop up ads on every web site you visit. The industry took the most important financial decision many people make in their lifetime, packaged it and sold it in the same way Madison Ave would sell a toothpaste. They can take horse droppings and wrap it up in nice package and call it *manure*, but at the end of the day, it's still CRAP.

The financial advice was irresponsible. Borrow as much as you can based on an adjustable rate, instead of the more prudent advice, buy what you can afford. Prudent underwriting standards would have made this scenario impossible. So brokers pitched and packaged the story, lenders underwrote the paper, and Wall Street bought the end product. The borrower was nothing but a pawn in a game of extreme profits for the industry. But the industry destroyed the very market they depended on for their sustenance. Every player in the transaction made huge profits and all they needed to get the ball rolling was a body to give a loan to.

The industry is afraid of regulation leading to legal actions against them. Unfortunately, the fact that they will have to answer for what they have done and what they may do in the future is not a good reason not to regulate them. In fact, regulation and more oversight are long overdue. The inaction earlier is the problem, not the possible action now. I feel the pain of consumer advocates who say, pardon me but I've been telling you about this problem since 1998. With every federal action or settlement comes an open door for more lawsuits. This is occurring everyday across the country. Consumers are suing lenders, Attorney Generals and federal agencies are suing lenders, lenders are suing brokers and appraisers, borrowers are going into bankruptcy courts, Wall Street is suing lenders to buy back loans, investors are suing Wall Street investment firms for misrepresenting stock values. This is a huge mess. The potential of legal problems as an argument for guidance instead of regulation is simply ludicrous. Can it get any worse?

If regulations are about conducting business in a legal and ethical way, then is the industry saying they don't want to be held to that standard? Any regulations need to be applicable across the board to everyone equally with no distinction between a broker, lender, or national bank. This is critical and the main reason for a National standard. However any National standard should not restrict any state's ability to enact even tougher standards within their state. Along with regulations and National standards for lending practices, we also need National standards for foreclosure. Going forward the huge mess that is already unfolding and the potential for more problems as we go forward necessitates some sort of National standard for protecting the borrowers who truly were put into loans by predatory lending practices.

If federal and state laws were broken in the creation of the loan, then borrowers deserve a review of documents before a foreclosure can take place. The regulations need to state what loss mitigation standard lenders are required to offer if predatory lending issues exist. It is wonderful that Attorney General Marc Dann has halted all New Century foreclosures in Ohio pending review of documents for predatory lending, but what about others not in Ohio who have been victims of New Century and other lenders? This is a huge problem occurring around the country. Although auditors have already been forced on companies like Ameriquest, the FED should be watching closely as cash strapped lenders are in a hurry to foreclose and get rid out from under the bad loans they created. This is perhaps the dirtiest little secret in the industry right now. Their loss mitigation plan is to foreclose on as many as they can and be done with the bad loans. No one is watching. Only the strong that can fight back stand a chance, the rest are being run over by the lenders.

Just this week I listened in on a webcast from KBW Mortgage Finance Conference held in NYC on June 12, 2007. Some rather eye-opening statements were made. Lenders said they are looking to turn over properties as soon as possible due to the downturn in the market. They said if a loan is going under then the sooner they could secure that property and sell it the better off they will be. They also made jokes that Alt-A mortgages were for borrowers with better self-images and these loans were for the naive and unsophisticated borrowers. There was talk of the rating agency role and how pension funds need AAA ratings. The comment was the rating agencies don't want to downgrade MBS due to the sell off which would ensue. Dangerous territory. There was also talk of securitization issues. The contracts state that the mortgage servicer can only alter terms on 5% of loans in a pool. So in the name of profits how can loan terms be modified and still please the investors holding them. But everyone laughed and said it won't be politically correct to just come right out and say it is the poor borrower against the hedge fund interests.

These issues will be a political hot button and a legal one if more are held liable for aiding and abetting fraud as Lehman Brothers was. In my opinion this is a huge problem and needs a prompt solution. A bandaid won't do. Nothing short of total reform and regulations will fix this problem. Neither side should object to these solutions. Why is the industry holding so steadfastly to practices, which have severely damaged their business at this point? No one can deny the real estate market in a standstill and mounting foreclosures is not good for their business. So it only makes sense, at least to me, that anything aimed at jump starting or at least stabilizing the market again would only be good for everyone. With the, "bad actors" removed, unable to conduct business the way in which it was done due to the new stricter regulations and oversight.

An overhaul is long overdue of the 30 year-old forms, which have failed to keep up with the creative loan products of today. The GFE, all disclosures, and the HUD-1 need a format that would make it crystal clear for a consumer to understand. In addition, an enforcement of sensible underwriting standards and enhanced penalties for non-compliance is needed. The underwriting guidelines I'm suggesting would not make any loan product obsolete, but clarify under what circumstances they can be used under.

The market prices, which were unrealistically high due the fast and loose lending standards, are already going through a painful correction. The new loans are reflecting much more realistic prices and a new trend toward fixed rate mortgages. The appetite for exotic mortgage products is diminishing both from consumers who now understand them and investors who see the risk level involved. Many lenders and brokers have been forced out of business. In my opinion all we need is a return to balance with the loopholes for fraud and misrepresentation closed.

Lenders, brokers and investors, will have to take some responsibility and losses. If violations of laws occurred in creating loans then the borrowers deserve to be made whole again. This will cause some short term losses for all the players who participated in the malay. However, since when does the need for profit margins, outweigh an illegal act? Everyone who touched the transaction needs to be held accountable. The government needs to have the will to go after the executives who profited handsomely during the last several years. They were the beneficiaries of the "fruits of the fraud." Will this put some smaller lenders like New Century under? Absolutely. Should these types of lenders go under? Absolutely. The remaining lenders who hopefully conducted the least amount of bad behavior will be stronger.

In fact, there are some lenders, banks, appraisers, and title settlement services that you will hear very little about because they didn't choose to participate at all. The list of those who did is very long. In my recent foray into these issues I'm finding the legitimate and ethical people are very happy things may change. They lost business by refusing to stoop to the levels of others.

Problems and possible solutions.

RISK LAYERING

I agree with the industry on only one point, it's not the loan products that harm, but the way in which they are used. The ability to use products and terms like prepayment penalties, ARMS, stated income, and other industry standards is not per se a problem. These products have been around for many years now and when used with prudent underwriting and with meaningful purpose they are good and useful products for the borrower they are appropriate for. The problem is the selling of these loan products together and the intentional misuse for profit. So the dilemma is how to provide for good innovative products balanced by consumer protection. It's simple, you can't give a 100% LTV adjustable arm based on an inflated appraisal to someone with no income documentation and include a prepayment penalty in anticipation of default, sale or refinance. Or worse, add a prepayment penalty to compensate the broker for making a bad deal for the consumer. The argument from the industry for the reasons a prepayment penalty is necessary is based on outright misrepresentation of how they are being used in the sub prime market. So the answer is prudent underwriting which has not been the case. Regulation could easily state which combination of loan products can be used and which combinations can't. Simple. Regulations could also easily address the consequences for breaking the rules. In addition, borrowers in certain loans of high-risk nature should not be trapped by a prepayment penalty that was used as compensation in the form of a YSP to a broker. If a YSP exists then a prepayment penalty should not.

ACCOUNTABILITY

If, as the industry states, it is "bad actors" who have perpetrated all the fraud, why are they so against accountability. If you didn't do anything wrong what are you afraid of? Each deal that a broker submits contained the terms I described above. Each lender's underwriters accepted these loans. The same lenders provided the rate sheets with the incentives (kickbacks) to encourage certain detrimental loan terms. This is not "bad actors." This is lax underwriting and incentives to induce fraud. My argument would be that once the "bad actors" are removed wouldn't the legitimate lenders be stronger, and have more market share. Why are they so against the enforcement and improvements aimed at helping the entire industry as a whole? Level the playing field with the same rules for everyone and remove the incentive-based reasons the "bad actors" are committing the fraud. The mainstream industry has conceded that many things they did only to compete with the extreme competition from upstart lenders hell bent on making loans at any cost. Those lenders read like a predatory lending who's who list. It was like a plague that infected the entire industry.

DISCLOSURES

Don't just disclose –EXPOSE. Much talk has been made about disclosure. Disclosure improvement is needed. Not cryptic YSP -POC disclosure, but true plain language disclosure. Timing of disclosure is critical. When applying for mortgage the 3-day law already in place needs to be enforced. The borrower should also be given a disclosure at this point that they have a two week window in which their credit can be pulled by multiple lenders without hurting their credit score. Disclosures should be clear and void of any fine print * disclaimers. Disclosures must include penalties for deviation in final settlement terms. As part of these disclosures every borrower should be given an explanation package of critical laws of the state they are in and legal remedies available to them if those laws are breached. For example although a law exist with an extended three year right of rescission for certain TILA and RESPA violations, it is not revealed on the RESPA disclosure statement or in any TILDS. Borrowers should be informed up front of what the laws are and therefore it would make it harder for a broker or lender to break them. Take off the mask of deception available to the "bad actors" in the form of the lack of knowledge of the consumer. Force them to reveal the laws they know they are breaking in the form of good meaningful disclosures.

GOOD FAITH ESTIMATES

Or the "Fairy Tale" estimate would be more accurate. The good faith estimate has fast become a tool for the damaging deception of bait & switch. Using this tool is a violation against all lenders who try to play by the rules. The companies using this as a bait & switch tool are corrupting the process of fair competition. Simply no consequence exists currently for submitting a total fabrication of terms. This document should be enforced through federal regulations for acceptable tolerances no different then the final HUD 1, making certain items non-changeable at closing. I feel this regulation could be the single most beneficial tool for the borrower to gain back some control of the process. Bait & switch is very costly to the borrower. Interest rates are changed, costs are added, cash out terms are reduced, and prepayment penalties are added at closing. This creates an uneven playing field for lenders and borrowers. Terms that should be illegal to change include adding a last minute prepayment penalty that wasn't disclosed initially. I don't see why any terms should change once the GFE is given or what is the purpose of it. However I do realize that honest mistakes can be made and those should be correctable, but what company doesn't know their fee for doc prep, and general charges. With everything automated, if it's truly fair to all borrowers and fees are equal for everyone, this wouldn't be a problem. Why should one borrower be charged more for a fee because the person preparing the transaction thinks they are less knowledgeable, or in a weaker bargaining position or will not question it. While another borrower who knows better will not agree to it.

INDUSTRY ARGUMENT

I heard over and over again, issue guidance not regulation. Guidance is based on trust. The trust a borrower and the government placed in the players in the transaction has been misplaced. Nothing short of regulation and harshly enforced penalties will eliminate the ability for the criminals to perpetrate fraud. There are good laws already in place including TILA, RESPA, and basic common law principles. The problem is that the entire process has been corrupted to the point that laws are having trouble keeping up with the industries creative attempts to avoid them. Laws are hard to enforce and borrowers without the resources of lenders find it hard to fight back. How can a consumer fight back against a lender who can hire the best law firms in the country with the ill-gotten gains they stole from the borrowers? How is that fair?

HOEPA

At the KBW Mortgage Finance conference, a speaker said, after HOEPA was drafted the FED was concerned that the number of HOEPA loans dropped to only 25,000 loans in a year. The industry is using a scare tactic in trying to hold on to its control through threatening a reduction in available mortgage capital. This is a twisted view and an outright lie. Certainly since HOEPA was enacted the exact opposite has been the case. Capital skyrocketed. States who have banned prepayment penalties have proven the industry threats as being empty. The purpose of the HOEPA regulation, as I would interpret it, would be to reduce high cost abusive loans. The terms and practices it addressed were tantamount to loan sharking and taking advantage of a disadvantaged borrower. So the reduction in these loans should have been a good sign. However the industry adapted and adopted new practices to charge the same consumer high fees and rates in a different way. The switch was made to inflating the amount a person could borrow using no doc loans, switching everyone to adjustable rate loans to become HOEPA loans in two years, inflating fees which weren't picked up as finance charges, and charging prepayment penalties as back-end fees. They charge just under the HOEPA triggers to begin with, knowing shortly that adjustment will take place and magically that non-HOEPA loan at inception is a HOEPA loan on steroids getting stronger everyday. Quantity is not the goal, sustainability is the goal. HOEPA triggers are to high to have an impact on the majority of transactions, but even more problematic is the industry has created new products and terms purposely designed to avoid HOEPA triggers. What the industry lacks in morality- it makes up for in ingenuity.

PAY OPTION ARM & EXOTIC MORTGAGE PRODUCTS

I would like the opportunity to argue strongly that industry is adopting new loans structures and products to avoid HOEPA triggers. "Pay Option Arm" loans should be considered HOEPA loans, and in fact are much more costly with floating monthly interest on increasing balances. The POA loan is an ongoing monthly interest adjustment loan on ever increasing loan balances. The lender can put anyone in loan with a rate under the HOEPA interest rate triggers if they know on a POA or a 2/28 they will quickly be able to increase them to a rate over or very close to the HOEPA trigger. These practices are undermining the entire basis of HOEPA. This is just a clever way to make a high cost loan.

The POC-YSP is a tool to avoid HOEPA triggers and is used as an incentive to a broker for adding harsh terms, slamming borrowers into taking a POA loan or other adjustable rate mortgages with higher interest rates, only delayed. The YSP is not added in cost for HOEPA triggers and the higher interest rates are not revealed or subject to the initial thresholds for HOEPA. However, if you did a basic amortization on what this type of loan would cost, comparing it to the 8% cost of fee trigger of a HOEPA loan and you would agree that this is much more costly. The interest rate caps on these loans are set just under HOEPA triggers and with floating indexes they quickly rise to that maximum level. In addition, these loans come with an extra bonus for lenders. Compounding interest on ever-increasing balances. The fact is the majority of borrowers who take these loans do so for lower monthly payments promised by the lender. This is the main selling feature presented thereby assuring the lender of negative amortization. Prepayment penalties are used to lock borrowers into these loans when they figure out they have just committed financial suicide and as a tool to recoup compensation paid to brokers.

The YSP and PPP is a fee financed into the transaction or collected on the back end. I would suggest amending HOEPA to include these items as part of the finance charges. Additional broker fees of any kind are not acceptable in combination with a YSP should not be acceptable but is common practice. Broker compensation based on "certain loan terms" has to be removed altogether.

Consider the havoc these loans are creating as resets happen and consider the future if you don't adopt strict regulation for the use of these loan products. The regulation for these loans should include enhanced disclosures with no prepayment penalties allowed. A person must qualify at the highest possible payment rate thereby eliminating the use of these loans for lower payments aimed at cash strapped borrowers. DTI and LTV ratios must be prudent. Advertising for this type of loan needs to be VERY CLEAR and STRICTLY REGULATED to ensure the lender or broker is not using a misrepresented teaser rate, and a false misrepresentation of savings and appreciation to lure in borrowers. All the terms disclosed must be crystal clear and accurate.

CRIMINAL PENALTIES

This industry is not new. They know what prudent underwriting is. The industry has proven they can't police themselves. If the FED chooses the guidance approach, I would suggest that the industry agree to very severe penalties for violations. Much worse then anything in place now. Including making certain conduct criminal. Holding everyone in the chain of the transaction responsible including; the broker, the underwriter, the appraiser, the lender, the final holder of the note. If the industry is truly committed to fixing the problem and doesn't want mandated increased regulation, then they should accept the harsh consequences of any illegal actions. Civil fines need to be increased substantially and applied in a way that borrowers do not have to go into bankruptcy or be part of a class action to get them. Good laws exist but for a borrower trying to get help it is almost a futile effort. The lenders hire the best law firms in the country to defend themselves and few lawyers are willing to take them on. The only caveat, even with those kinds of defensive advantages, lenders are still losing in epic numbers when challenged. I don't know of one federal action or Attorney General action that has failed against any lender. Truth is hard to fight. The evidence is often overwhelming against them. However, is it right that a practice is challenged against one lender and another is still doing it? One makes a settlement and another slides by. One Attorney General defends his state's victims, while another Attorney General does not. Even worse large settlements have been reached and the same companies have gone back to the same practices because the fines don't reflect the crimes. Proof of this can be found in Ameriquest and Chicago Title to name a few. How many strikes before you are out? Or, in corporate America does crime pay?

LEVEL THE PLAYING FIELD

Many of the items we are talking about are occurring because of the imbalance of power that lenders are holding over borrowers. The way they control the entire transaction is crucial to solving the problem. First, it should be mandatory that the appraisal be given to the borrower at the same time it is given to the lender. The borrower should be given the opportunity to look it over and do they're own evaluation. If they see that the comps aren't reasonable, or features have been added to inflate value, they can contest it and if they choose not to use that lender due to misconduct they should receive and refund of appraisal fees paid. Brokers can't be given obscene incentives based on rate sheets with a laundry list of items a lender wants to sell the borrower on. Brokers need education, screening, and licensing. They need to be facing criminal penalties and harsh civil penalties for misconduct. Agreement for pay between brokers and borrowers, or brokers and lenders, need to be clear and in plain language. If a borrower is being given a prepayment penalty so the broker can be paid $7000 by the lender then they deserve to know that. Then they would be free to negotiate the broker's fee and ask what they are getting in return. Lenders need to offer loan products, rates and fees, based on formulas of income, LTV, and credit scores. Not based on gender, race, and overall level of intelligence of the borrower. Programs for sub prime borrowers need to be based on a leg up, not setting people up to fail. The borrower, who needs help the most, gets the worst deal possible fraught with rampant fraud, corruption and overcharges. This is the sub-prime experience. Wall Street can offer increased prices for certain loan products as long as the borrower is not steered or slammed into these loans in the name of GREED.

MONITORING CONDUCT AND FORECLOSURES

The most hideous fact I'm uncovering is the industry new tactic of forcing foreclosures. Many homeowners are being railroaded into foreclosures. On one side lenders are telling the government they will work with borrower, but absent of any standard, they are doing the exact opposite. I have uncovered this dirty dealing with more then one lender in more then one state. The industry is in a cash crunch. The value of non-performing loans is lost and they need the liquidity back. The only way to resolve that is to foreclose and turn that 30-year note into liquid cash. The government is not watching this practice. The dirty secret is if they are caught holding a loan, which has predatory lending issues they may be, forced to modify that loan and hold it at a reduced non-profitable rate. They may be forced to now hold a non- performing loan which they were forced to buy back from an investment pool. The more then can turn over the better for their cash flow. After huge settlements and government actions some lenders now have auditors monitoring their business going forward. No one is watching this back end problem. For the most part when lenders are asked for statistics on loan products sold and level of defaults, they simply answer they don't know. Right now I don't feel that any checks and balances exist due partly to the number of players that are involved in a transaction and no mandate for submitting information. This way lenders can quietly foreclose with no red flags popping up anywhere. Many foreclose under MERS so the lender's name is not revealed. I was very encouraged to hear that a National database is being launched to track problems and problem people in the industry. Identifying problems early will save many from abuses.

PREPAYMENT PENALTIES

Prepayment Penalties – Should be allowed only if the borrower is truly given a reduced rate in exchange or fully understands the purpose for which they are being charged this penalty. They should not be used as a tool to trap people into bad loans. They also should never be allowed if not disclosed on the Good Faith Estimate. I would suggest that the industry not use this tool as a way to compensate brokers. The borrower would be much better off paying the broker a .5% or 1% origination fee which could be financed into the loan up to a maximum amount that should have a cap. This would eliminate the incentive-based YSP prepayment penalty. If the borrower "chooses" to have the lender pay the broker a fee for accepting a prepayment penalty, I just don't see how that benefits the borrower or the lender. This sort of incentive based industry practice has been created as nothing more then a way to "offer a kickback" in exchange for a loan at the borrowers expense. If no one could offer such incentives then the playing field would be level. This is the type of issue regulation will help if it applied to everyone. The borrower should be offered in writing as part of the initial disclosures the rate of the loan without a prepayment penalty and the rate offered with one as some lenders are adopting. My only argument would be if the amount is no longer going to the broker, then it should be pretty much the same rate. To pay it out up front and then get it back in the event a borrower exits a contract early means the borrower is paying that incentive based commission to the broker. In states that have banned the prepayment penalty they found virtually no change in loan rates. If it is approved for continued use, it should be included as part of the fees included in HOEPA triggers.

UNDERWRITING

No Doc/Stated Income Loans - The problem is not the individual product but the layering of risk. This is the one component that substantially increases risk when combined with other loan features and is an invitation for brokers and borrowers alike to commit fraud. So the regulations I'm suggesting have to do with underwriting standards which do not allow for certain combinations of products. Some lenders have already adopted changes in standards for many items, but this is another area where regulation would level the playing field making it the standard for all lenders. An example are loans with: Adjustable rates which the borrower is only qualified at the initial rate 100% LTV or 80/20 loans or in some cases 125% LTV No Income Documentation Low FICO Scores These risk factors anyone would say don't go together, yet this does represent the kind of loans that were made everyday. These items by themselves with other good mitigating factors can still be viable formula for home ownership. Together they spell sure disaster. So I would suggest not limiting programs or products available, but issue strict underwriting guidelines that certain combinations can't be used without significant mitigating factors. For a 100% LTV loan a borrower should be able to provide proof of a six-month cash reserve, in investments which are temporarily not liquid. Any mitigating factors would have to be well documented and checked, not just stated. If a low FICO score is due to a documented illness which caused someone to fall behind on his or her bills should be accepted as a mitigating factor. The no doc stated income loan was used as a tool for brokers because they knew the borrower couldn't qualify under what they made. The regulation for no-doc loan would simply state; it can't be used, no exceptions, with 100% LTV or 80/20 products. This creates a no verifiable income/no assets formula- a deadly combination. A minimum standard for a no-doc loan could be at least a

90% LTV with at least a 620 credit score, and two months of cash reserves. 100LTV and 80/20 This tool was used by brokers and lenders to put people in houses who had no money to put down, and no cash reserves. This isn't a problem as long as income is stable and interest rate is stable and housing prices go up. The majority of loans created in the past few years are the opposite of this scenario. Real estate is going down, interest rates are going up and whether or not income is stable is not known due to the no doc qualifying. Because markets were increasing for a time this was not a problem, but still it wasn't prudent underwriting. For the long-term buyer who has a career that will give them an upward trending salary and can weather the real estate market ups and downs this loan makes sense. For someone who has a good job and can verify his or her income and job stability, this loan makes sense. This person may not have had sufficient time or ability to save for a home down payment and may be paying the same amount in rent. This loan makes sense if the loan is within a correct DTI ratios on a house can truly afford. This loan should be at a fixed rate. So the regulation would read something like this. 100LTV or 80/20 loans can only be offered with a 5, 10 or 30 year fixed interest rate to a borrower with steady income and a DTI ratio of no greater then 40%.

ESCROWS
Not including escrows in a loan to a person who already has a sub prime borrowing profile is tantamount to negligence. Not escrowing taxes was used as a tool for flipping. After a six month to one year period the same broker calls the borrower when he knows the tax bills are coming due and refinances them to pay the taxes. Not escrowing is used to misrepresent a lower payment to a borrower. Not escrowing should only be allowed on loans to people with high credit scores and low DTI ratios. Considering most states do not require any interest paid on escrow accounts, it seems only a benefit to the lender to hold escrow accounts.

REFINANCING
Serial refinancing and the housing boom that went bust. Let's face it, the industry boomed thanks to the fast moving real estate market and refinancing. People were in and out of loans due to the onslaught of aggressive marketing. People bought and sold houses rapidly during the height of the boom. So lenders reacted in an irresponsible way. They turned what should have been a benefit of increased business and competition into a free for all at the expense of the borrowers, which now has created risk in the entire foundation of the economic system. The loose money and lax underwriting created and fueled the artificial boom. The artificial boom falsely inflated values of homes beyond a point where the debt to income levels made any sense. In short, no one could afford a home without a no-doc adjustable arm mortgage. So the industry encouraged and enabled everyone to buy homes they couldn't afford in the first place. You can see where this had to end at some point. It was unsustainable. When prices peaked at an unsustainable level and borrowers began defaulting on risky loans the unraveling began. Now we are dissecting the elements of the formula for disaster. People in homes all across the Nation paid more then they realistically could afford based on their REAL income, assets, and true value of that home. Serial refinancings have stripped many homeowners of any equity they had in their homes effectively depleting a staggering loss of wealth across this Nation. Where did that wealth go? To the lenders and brokers who perpetrated the fraud and the Wall Street investment houses who prospered during the boom. By my estimates about half of the equity went to transaction fees alone. Executives and CEO took not one million, but hundreds of millions in salaries during the boom. They didn't care how the loans were being sold, they just said keep them coming. Now they need to participate to set things back on the right path. For them to now be able to walk away with all the profits they took at the expense of the entire Nation is absurd. The regulation for this refinancing is very simple and many states have already adopted the standard of a tangible net benefit sheet. The regulation

must state what the minimum net benefit would be. Companion regulations need to include the tools used for the flipping, like lack of escrows.

APPRAISERS

Appraisers who received nothing more then their accepted fee were enablers to fraud. On each sale or refinance they were pushed by brokers and lenders to give them the number they were after. So with each subsequent refinancing or sale the values were pushed a little higher. You saw this in new home communities. The builders would raise the price every five to ten houses that sold. So if the house down the street appraised at $30,000 more then the one before, then the next one $30,000 more. On each and every one an appraiser put his stamp on the new value. Before you knew it your house in just a year or two was worth $100,000 more. ON PAPER. This was the key. It was all funny money. Regulations need to address the pressure on appraisers to inflate appraisals. Simply state that any appraiser who reports any broker for requesting or pressuring them to inflate or breaks the law in stating a value will immediately lose their license and face prosecution. The appraiser regulation needs to be just as harsh, if caught participating in these practices the appraiser should immediately lose a license and face criminal charges. These over-inflated values are one of the core issues facing the correction now. The underpinning of the real value of real estate properties and mortgages which secure them is at risk due to the inflated appraisals. I would also suggest an additional requirement for all appraisers. They should not only do a traditional appraisal with 3 comps, but that they must submit a separate sheet listing every property that has closed in a five mile radius in all price ranges. The underwriter and borrower would have the benefit of seeing the overall value ranges. Not just the select 3 properties the appraiser wants them to see.

TITLE INSURANCE & SETTLEMENTS

The obvious data is available that title insurance is one of the biggest rip offs in the settlement process. Lenders demand it and they share in the fee. Lenders choose the settlement companies and most borrowers don't know that an independent settlement agent could be their best line of defense. This is an area where the government could mandate total independence. If lenders couldn't choose the settlement agent or direct the borrowers to use one who is affiliated, then borrowers would stand a chance having someone whose total responsibility was to them. How many bad deals or illegal charges would that stop? Right now no checks and balances exist because the lenders control everything.

THE MARKET

The value wasn't based on a natural appreciation over time due to areas growing, salaries increasing, or improvements made to the property. They were based on a frenzy created by an overheated market, loose financing, and aggressive appraisals. Anyone can see this is a house of cards that has now begun to fall. I say BEGUN to fall because anyone who is looking at this realistically must see that this house of cards is still barely propped up by borrowers who are struggling more and more as interest rates rise and values decrease. The sheer number of adjustable rate mortgages people are in now, and rising foreclosures can't be ignored. If you do ignore where we are right now, and don't figure out a way to force the mortgage industry who created this mess to fix it, and to go forward in a way that makes sense, you are risking the entire system economic failure. This is like musical chairs. A lot of shuffling around needs to take place. The problem is now that people realize what has happened and that they can't afford the houses they bought at the new interest rates, they can't sell or refinance. They can't refinance to a fixed rate because now they are much higher then before and they couldn't have qualified for the fixed rate even when it was lower. They needed to buy a less expensive house to begin with. Now the house they did buy isn't worth what they paid for it, so they can't sell. What does this spell- FORECLOSURE EPIDEMIC.

How do you solve a dilemma of homeowners who were put in mortgages based on a value that really never existed except in the smoke and mirrors of deception? You can't force values back up. You can't get them out of the contracts they signed. You can't undo what has already been done with any legislation. The one thing you can do is hold the parties who perpetrated the fraud responsible. Every single borrower, who was the victim of any kind of fraud, misrepresented loan terms, or fraudulent inflated appraisals, deserves every right and remedy under the law. The lenders, brokers, appraisers, title companies, and end of the line investors should all take a portion of that responsibility. They all touched the transaction. If you go after all the players and each one is forced to contribute to solution, the capital may be available to help borrowers recover. In the end if something is set in motion that will stimulate the market back to moving again, the kinks will work themselves out. Hopefully, just like when a person is punished, we hope they've learned their lesson and don't do it again. But absence of any consequences across the board will leave no incentive for the players not to wait until the hoopla dies down and start all over again. Please do not fall for the argument that regulation will choke capital and prolong the real estate downturn.

The lesson I hope everyone has learned is that you can only push a market so far and then the very market you depend on for your sustenance is gone. It is the Federal Reserve's mandate to make sure that the new regulation will prevent further erosion of home ownership, which is so fundamental to the overall health and strength of our economy.

REMEDIES

The remedy for appraisal fraud would include fines to the appraiser or action against the appraisers Errors and Omissions insurance policy. Every Appraiser should be required to carry a substantial E&O policy. This money needs to go directly to the borrower to buy down his mortgage to the true value of the property. This may make it possible for a borrower to sell and get out from under a loan or enable them to refinance at a better rate. It may offset any arrears due on a loan.

The remedy for a YSP and additional fees paid to the broker is to force that broker and lender involved to credit that fee back to the borrower and "remove" the incentive terms that the broker was paid for. These terms could be the prepayment penalty and an adjustable rate mortgage.

The borrower should be entitled to see the rate sheet provided to the broker for that day and understand the terms they may have received as a result of that YSP offered.

The assignee liable investor must be forced to share in the losses by offering to modify loan terms. The current 5 % loan pool modification rule must be increased to assimilate large numbers of possible defaults. I would argue that unless they act and save as many of these loans as possible the eventual downturn which reflects the underlying value of loan pools will have the be downgraded. Rating agencies will be forced to downgrade these investments from AAA rating and then loan pools will have to sold off, creating more havoc. If they refuse to try and mitigate the damages, then the future downward pressure of foreclosures will force the losses on them with much more carnage then taking the proactive approach and saving as many loans as possible now.

I think overall they will see a very short-term adjustment. My theory is if you get all the borrowers back to a place where they now have some options, many will begin to sell the properties they are in that they can't afford long term and look for something more sustainable using a fixed interest rate or long term arm product. As this occurs the market will slowly begin to move again and new loans will be created and liquidity will return. The new loans, if regulation or industry practices improve, will be more stable going forward. The enormous profits from crazy loan products and loose underwriting will not be available, and that is a fact that everyone will just have to adjust to. We have now seen the enormous damage and risk this combination has put in the system. If new creative loan products are developed they need to strike a balance between sustainability for the borrower and profit potential.

FIXING THE PROBLEM

I do know that in order to truly get all of this back on track we can't just focus on what we will do going forward, we need to fix what has already been done or the momentum downward will increase. Somehow the shuffle needs to take place. I have many ideas in theory, but the best heads need to be put together to iron out some real plans. I find it unfortunate that mortgage companies, brokers, title companies, and Wall Street who made excessive profits by bending the rules, ignoring the rules, and breaking laws, are not coming forward with any remorse, responsibility or even any acknowledgment that they were part of the problem. The same people who would benefit most from a healthy market returning seem stuck on pushing for inaction. You can call this denial. I call it fear of retribution. The lawsuits, are mounting and they will never admit or approve anything which remotely tries to place any amount of blame on them. They can't be part of the solution if they keep this stance. The market needs them to participate fully and openly in the solution.

A few have begun to voluntarily adopt loan modifications and tighter lending standards. But they don't want any additional regulations. This makes no sense because it will force everyone to play by the same rules. I would ask that legitimate, law abiding industry leaders come forward to champion an effort for federal standards to protect themselves from a repeat of the largely unregulated mess that we now find ourselves in. I would say to them, admit, acknowledge, and truly help plot a solution or else face severe retribution. The unsustainable market that was created has backfired on everyone. I'm a bit confused by any lender wanting to do the right thing, prudent underwriting and putting people in homes they can truly afford to make the payments on, fighting against strict laws and regulations. Many of the "bad actors" have already been driven out of the business, which should only serve to make the legitimate lenders stronger. Their market share will increase, the market can stabilize, and hopefully borrowers have learned their lesson and will buy only what they can afford to sustain, and the overall market will slowly recover.

Could it be that the "so called bad actors" were almost the entire industry? I've read articles in which even the CEO's of major companies have admitted, the industry went a certain way, toward lax underwriting, dangerous products, and aggressive marketing, and everyone was forced to go along or lose market share. Wall Street encouraged this by paying more for these dangerous loan products. All of the "bad actors" in this bad play, made obscene amounts of money at the borrowers expense. Meanwhile the statistics of the wealth they drained from the people who could least afford it is unconscionable. They drained equity from homes with every refinance, brokers with no education and little regulation made six figure salaries. Mortgage companies and Wall Street CEO's took obscene salaries and bonuses.

I say it's time they realize they will need to take some losses and stop the foreclosures, helping the borrowers they used as pawns in this game. The only way they are going to do that is for the government to step in and make them. At this point they are still fighting this every step of the way taking no responsibility. Risk vs. Reward a tale of Wall Street The lenders and Wall Street only cared about risk vs. reward. They are still gambling with the entire economic underpinnings of this Nation. They will ride the wave like they did in the dot.com boom until the ride is obviously over and the fallout begins. Then they'll search for the next opportunity for the most rewards and jump on that bandwagon.

The problem is what this gamble represents is different then any businesses success or failure. This gamble is with the families of this Nation and in many cases the only asset they owned. Who will pay when we have 2 million homeless broke families. The extension of that, two adults and two children or 8 Million displaced desperate people. This is a financial disaster of epic proportions. If more and more people default on loans, as we are seeing, the house of cards that has begun to fall, will collapse so fast with such speed that no amount of effort will be able to fix it.

A proactive approach is needed now to stop the obvious, foreclosures are rising. For Wall Street the underpinning of the value of the investment in MBS, the equity in the homes, is quickly disappearing. The phantom profits of pay option arm loans these NYSE traded companies are claiming, combined with over inflated appraisals to begin with, on now depreciating assets, will make their investments nothing more then worthless paper. It's all been smoke and mirrors. Not rooted in sound financial realities.

Everyone will be affected. I take offense at the people who think this doesn't affect them and take the position it isn't about me so why should I care. This will affect many people who never participated in it directly. The conservative consumer who bought a home they could afford with a low fixed rate, is right next door to someone else who took a out a crazy arm product on a house they couldn't afford in the first place and is headed for foreclosure. Dragging down the values of everyone's home. I think the statistical values you are seeing are not reflective of true market conditions, because houses simply aren't selling at any price. Some are sitting on the market, some are going into foreclosure, and others have been withdrawn from the market as people have just given up on selling them for now. How do you assess a decline in value for homes that simply are not selling? It makes sense that the value has decreased past what they owe on them to be able to sell.

Wall Street is playing with the mutual funds and retirement funds of many Americans. They are financing this debacle. They will pay if the underlying security of the investments is non-existent or way under the stated value. The government which in turn is the taxpayer will have to pay for all the social services all the retired and elderly in America will need after they watch all the hard earned money they saved disappear into thin air.

Which brings me back to the POA product lenders are selling as a solution to the problems everyone is having. Refinance into a Pay Option Arm loan to lower your payment. Recently I tried to help someone who was trying to negotiate a forbearance agreement and his lender was trying to refinance him to Pay Option Arm loan. This loan was designed originally for a sophisticated borrower to manage cash flow and to use funds to invest in higher yielding investments. So for a select few this type of loan can work. Very few. They industry is selling these loans to lower payments for cash strapped borrowers.

I do understand why Wall Street would buy them, extreme profits. They are banking on the underlying investment having enough equity to pay back the principal with interest on these loans. At this point I think that assumption will be challenged as many of these loans will go under when resets take place.

The FED needs to be aware of how many of these loans are out there and how many have already reset. When the reset happens what has been the result. Did the borrower start paying the full payment or did the borrower default? Did they refinance? These are questions that need to be answered. Now. If these loans could work in a strong real estate market, they certainly are very risky in a downward trending one.

If the reason for a homeowner taking this loan is to lower a payment, they serve no purpose. This lower payment comes with a high cost and is just a temporary fix with an even more damaging conclusion. The borrower pays higher then normal fixed and traditional arm interest rates, and even higher then HELOC rates. These products float with the indexes so they can increase every month. So this is a loan which is compounding interest on an ever-increasing balance. Much like credit card debt. These loan programs always have a prepayment penalty. So if the borrower gets into this loan and gets out of it in 2-3 years, as the industry knows they will have to, the loan will be repaid out of the equity in the home. However if that property stays flat or decreases in value, the investor is left holding a piece of paper that isn't worth what they are owed. Does this make any sense in this market?

For the borrower it is just another way the industry is using them as a pawn. Wall Street is willing to take this risk because the reward potential is great. The homeowner can only lose. The rate of appreciation they would need to achieve to walk away even is just not realistically obtainable to make this formula work. These loans come with steep interest rates negatively amortized into the loans. The borrower taking them to lower payments is not taking them to invest in something higher yielding. The borrower is not qualified on fully rate so when the resets happen they will have no means to pay. But lenders will continue to make these loans as long as Wall Street wants to buy them.

Is everyone in denial about where this is going just like the initial denial about the sustainability of real estate appreciation? The FED needs to consider the risk to the overall monetary system. The amount of *debt everyone is carrying combined with the lack of financial security in home ownership and equity that is* disappearing into thin air is not sustainable. Wall Street is playing with retirement and pension funds. PLAYING a dangerous game with entire monetary system in the name of GREED. Plain and simple.

You can squeeze the American family only so much and then there is a breaking point. We are fast approaching that breaking point. Maxed out. Pay Option – Pick a Payment – Asset Builder Pay option Arm loans are the most damaging loans, which are proliferating in this market. As more and more homeowners become stressed financially they will succumb to the relentless advertising of these loans. The ads say we can lower your payment. The industry created and sold this product under the disguise as a tool for the sophisticated investor. To utilize cash flow for other investments. Then they turned around and sold it as an affordability tool for the general consumer. It lowers payments temporarily and then sticker shock like you've never seen in any arm product combines with a higher loan balance. If you think we've got a problem with foreclosures now, wait until resets happen on these loans, and homeowners owe 125% of the original balance and their homes have depreciated.

The other overlooked angle and danger to the overall economic system is the phantom profits these same lenders are counting on their books. Lenders are recording payments as full income even when in fact only 20-30% of the borrowers are paying full payments. What will happen to our economy and stock market when this party is over? Ratings agencies are hesitant to downgrade these securities because of the sell off that would ensue. Executives from Wall Street, mortgage companies and title companies, will have taken their hundreds of millions in salaries, bonuses and stock options, and who will be left holding the bag? Whose money are they playing with on Wall Street? The same individuals who created the mess will use their hundreds of millions to defend themselves in the many legal actions that will follow. Investor lawsuits like you are now will explode.

Countrywide's CEO Mozilo offends me greatly. Mozilo made hundreds of millions dollars off of borrowers in the past five years and his company has been implicated in illegal practices. The industry comment is, the market got crazy and anyone who wanted to prosper needed to go along with it. Mozilo has the gaul to blame regulators for attacking the Pay Option Arm loans. Is this government going to just take that type of rampant attitude, I dare you to try and stop me. I personally know a former Countrywide Branch Mgr. and former underwriter who told me of the training sessions for the Pay Option Arm loans. She called them misleading, and an outright fraudulent presentation of the benefits. She knew they were not good loans and refused to sell them. She was harassed and forced out of her job.

(Reuters) - **Chief Executive Angelo Mozilo** When they attacked the pay option and interest- only loans, that really put a dent in a lot of the product, which is perfectly good product." "The reason why people can't sell their houses is there is no buyers around," Mozilo said. "And there are no buyers around because they can't get the financing."

Okay, let's continue to do what has caused this problem in the first place to solve it? Make unaffordable loans to people who shouldn't get them in the first place? Artificially continue to inflate the real estate values and propel the industry forward so he can prosper?

Ameriquest CEO Roland Arnall was appointed by President Bush to be ambassador to the Netherlands, at the same time the justice department was investigating his company and reaching a $325 million dollar settlement. Outrageous. In this industry –apparently crime pays.

Ohio AT Mann has the right idea. He has halted all foreclosures New Century is trying to conduct in Ohio. He is also suing lenders for pressuring appraisers. He is defending the unwitting investors whose retirement funds have been used to finance this industry based on the fraud and misrepresentation of loans and of stock values. I also applaud efforts by other Attorney Generals, including Tom Miller and Lori Swanson. We need all states AT to get involved in this crisis.

Federal Preemption is just simply wrong. We need stronger Federal laws with no state preemption. Mortgage lenders incorporate in certain states like Delaware to take advantage of the laws of that state. So lenders can choose the laws of the state of incorporation or the laws of the state they lend in. This is unfair. If you choose Federal preemption then you must preempt this practice also and create National standards for foreclosures. People can't choose the laws of the state they want to be foreclosed under, and many states have less favorable laws then others.

Conclusion

To understand where the mortgage industry went you have to understand the motto – Target, Trick and Trap

To understand Wall Street you have to understand the motto – Greed is Good.

To understand the appraiser you have to understand the pressure- If you won't – then he will.

To understand the Lenders you have to understand the sentiment- If we don't – then they will.

To understand the lack of government intervention you have to understand the task of regulating- it was like the Wild West, everyone had a unregistered gun (unregulated creative loan program) and no one was afraid to use it. Everyone knew good laws existed, but they also knew the sheriff couldn't possibly easily enforce them.

To understand the borrower it is a simple truth – They wanted the American dream of home ownership

Thank you,
Paula Rush