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By Hand Delivery

Thomas J. Curry, Commissioner
Division of Banks
One South Station, Third Floor
Boston, Massachusetts 02110

Matter: Comments Upon Proposed Amendments to High Cost Mortgage Loan Regulations

Dear Commissioner Curry:

This firm is counsel to The Clover Trust (ML#0193) and Sanford Financial Trust (ML#1281), both of which entities are private mortgage lenders which engage in responsible forms of subprime mortgage lending. At the request of our clients, we have reviewed the proposed regulations and are providing comments with respect to several provisions, which, in the judgment of our clients, may have the effect of making needed credit unavailable to many of the very consumers which the regulations are designed to protect. Some of these comments were included in my oral presentation at the September 19, 2000 hearing in Boston, over which you presided.

In promulgating further regulations, the Division of Banks should be mindful of the fact that consumers have a variety of reasons for seeking mortgage financing and those reasons many times involve a need to access home equity to pay for needed home repairs, medical bills, education expenses and a variety of other personal needs which consumers may seek to satisfy. The difficulty with the proposed regulations is that the regulations will serve to prevent lenders from making loans which consumers may want and which may provide substantial benefits to these consumers, in order to make it more difficult (but not impossible) for unscrupulous lenders to engage in predatory lending. The net result could very well be that more consumers will lose their homes due to the unavailability of credit, than will lose their homes to predatory lending practices.

The areas of concern which my clients wish to identify are as follows:

1. 209 CMR 32.32 (5) Prohibited Acts and Practices. This section prohibits a lender from making a high cost mortgage loan unless the lender reasonably believes at the time the loan is consummated that the borrower will be able to make the scheduled payments to repay the loan based upon a consideration of their current and expected income, current obligations, employment status and other financial resources (other than the borrower's equity in the dwelling which secures repayment of the loan). This provision would appear to prevent consumers who are in financial distress from obtaining a new mortgage loan which would allow them to access the equity in their homes to stay in their home or to arrange for an advantageous sale of property.

Consider, for example, the fairly common scenario as follows:

a. The Borrowers are in foreclosure on their existing mortgage(s) because of a job loss, health problems, divorce, death in family or whatever reason.

b. The Borrowers have poor credit or are in bankruptcy such that they can only qualify for a high cost mortgage loan. Their income is not sufficient to service a new mortgage loan on a current basis, other than on a short-term basis.

c. The Borrowers have significant equity in their home, but they can no longer afford to service the debt on their home. They would like to access their equity by selling their house at an advantageous price without the threat of foreclosure hanging over the property.

d. The existing lenders will not suspend their foreclosure proceedings to allow an orderly sale at an advantageous price.

e. A subprime lender is willing to make a new loan to pay off the existing financing in order to allow the Borrowers time to sell their property. However, it is unlikely that the Borrowers could service the new loan for a long period of time, if the property does not sell.

f. The proposed regulations would appear to prohibit such a loan.

Under those circumstances, the Borrowers would be unable to protect the equity in their home by refinancing the underlying mortgages to provide breathing room to sell the property at an advantageous price. As a result, the Borrowers would lose all or a significant portion of the equity in their home as a result of the forced sale of their home at foreclosure or under the threat of foreclosure.

My clients would suggest retaining the existing language, so that occasional loans can be made by lenders for the purpose of helping consumers under the circumstances described above, without being concerned that every loan will be individually scrutinized for compliance with this provision.

In addition, the concept of examining what a creditor reasonably believes about the likelihood that a borrower will be able to make the scheduled loan payments is also troubling. While a creditor would like to believe that every borrower will be able to repay their loan, every creditor knows that statistically a certain percentage of their borrowers will not be able to repay their loans. If a creditor knows that a significant percentage of borrowers (such as 10%, 15%, 25% or more) meeting a certain credit profile are likely to be unable to meet the loan repayment schedule, what level of probability of default is a creditor allowed to reach before it ceases to reasonably believe that an obligor will be able to make the scheduled payments to repay the loan? The proposed regulations provide no guidance in this area.

Similarly, if borrowers over optimistically state on the loan application that they have or expect to have a certain amount of income which supports the loan and then for whatever reason the borrowers do not achieve that level of income, the creditor is potentially subjected to scrutiny over whether the creditor was entitled to believe the representations made by the borrowers about their income, in order to demonstrate that the making of the loan was not a prohibited act or practice. This provision seems to undermine the well-established rules that require borrowers to truthfully fill out loan applications, and that creditors are entitled to rely upon the truth of the representations made by borrowers in a loan application in order to determine whether to make a loan. Instead, under the proposed regulations, it is appears that the creditor cannot just rely upon the borrowers' representations about their income in their loan application, but now must also show that the creditor verified the borrowers' income sources, and, then, after verifying that income, the creditor must have reasonably believed that the borrowers could make the scheduled loan payments. Clearly, the requirement that creditors verify income and make the determination that the borrowers can meet the scheduled loan repayment schedule, places a substantial and unfair burden upon creditors and should be deleted from the proposed regulations.

2. 209 CMR 32.32 (6) (1) (a) Unfair High Cost Home Loan Practices. This proposed section prohibits a lender from making a loan where the fees and points

exceed 5% of the principal amount of the loan.[1] Fees and points are not defined in the proposed regulations, but would seem to include not only the origination fees (points) and mortgage broker fees which may be contemplated by the drafters, but also a large number of different fees which commonly appear in prime and subprime loans, and which are not related to the amount of the loan, including the following:

Legal Fees
Document Preparation Fees
Tax Service Fees
Processing Fees
Municipal Lien Certificate Fee
Plot Plan Fees
Underwriting Fees
Flood Certificate Fee
Wire Fee
Courier Fee
Express Mail Fee

In a prime loan transaction in which I was recently involved representing a seller of real estate, the total of the above charges was $1,934.25. If those charges were to apply to a $40,000 loan, where the lender charged 2 points and the mortgage broker charged 2 points, the fees and points would be nearly 9 percent, even if the loan were a conventional 30 year fixed rate secondary market loan made at a 7.5% interest rate. If those costs were applied to a high cost mortgage loan, the proposed regulations would bar such a loan transaction.

Since mortgage brokers often charge between 2 and 4 points on a loan, since our lender clients typically charge one or two points as an origination fee on a loan and since the legal fees and disbursements of any law firm on smaller loans can be the equivalent of several points, it appears that many smaller loans which are regularly made by our clients and other lenders can no longer be made under the proposed regulations. If those fees could no longer be charged, lenders would either cease to make such loans, which would deny credit sources to many hard-pressed borrowers, or those lenders would substantially increase their interest rate charges and prepayment

[1]The language which prohibits a lender from requiring a borrower to directly or indirectly finance any portion of the points and/or fees is confusing. The laws covering the disclosure of finance charges assumes that all of those charges are part of the finance charges, whether or not they are paid directly by the borrower or are financed by the loan proceeds. Accordingly, we read this provision as barring the charging of points and fees which exceed five (5%) percent of the loan amount.

penalties in order to produce an adequate level of return. For many consumers who borrow from subprime lenders, the absence of such credit sources would deny them the opportunity to obtain needed financing. The absence of such financing would also deny borrowers with poor credit the opportunity to reestablish their credit, which would have allowed them in the future to move into more advantageous forms of financing.

The proposed regulation would further restrict credit opportunities for many consumers, who are often unable to obtain financing, except through mortgage brokers. If the amount of points and fees which can be charged on loans is restricted to the extent set forth in the proposed regulation, many mortgage brokers will be forced out of business, since they will not be able to collect fees which would adequately reimburse them for their time and efforts.

3. 209 CMR 32.32 (6) (b). This language would prohibit a lender from charging points and fees in refinancing an existing borrower. If the term "fees" include legal fees and disbursements, then this would be a problem for many lenders, since it is customary for borrowers to pay the legal fees and disbursements in connection with a loan transaction. It is our understanding as well that many subprime lenders, who are selling their loans in the secondary market, would be unable to refinance and resell an existing loan without being able to charge points and fees. As a result, the lender would have no choice but to proceed with default remedies, including foreclosure, rather than restructuring the indebtedness in a way that was financially feasible for the lender and potentially more advantageous to the consumer.

In addition, there may be a drafting problem with the third sentence of this paragraph, since the sentence as currently drafted is unintelligible.

4. 209 CMR 32.32 (6) (f). This provision places the burden on the lender to demonstrate that interest rates or fees charged are based upon generally accepted credit worthiness, sound underwriting and other risk related standards or otherwise do not significantly deviate from industry standards or are not otherwise unconscionable. Given the fact that it is difficult for non-institutional lenders, such as my clients, as well as for the Division of Banks to determine what those generally accepted standards are, this provision seems to place an undue burden upon lenders. If this standard is to be established, then it ought to be incumbent on the Division of Banks, which regularly examines licensed lenders, to determine and publish those standards on a regular basis.

5. 209 CMR 32.32 (6) (m) Counseling Disclosure and List of Counselors. The provision requiring a borrower sixty years of age or more to complete a counseling program is rather burdensome for older borrowers. This is a particular concern if a borrower is facing imminent foreclosure and it is necessary to close their new loan immediately. If a counseling program is not immediately available, an elderly borrower could lose their home to foreclosure.

Another issue is the availability of these counseling programs and how costly and convenient it might be for an older borrower to have access to such counseling services. My clients suggest that the disclosure provision ought to be sufficient and the mandatory counseling requirement for older borrowers should be eliminated.

On behalf of our clients, we strongly urge the Division of Banks to withdraw the provisions described above from the proposed regulations for the reasons stated above. If you or any of your staff members would like to discuss this matter further with me or my clients, please feel free to contact me to arrange a convenient time. Thank you for your careful consideration of these comments.

Sincerely yours,

Clair A. Carlson, Jr.

CAC/pdb

cc: Lewis Lubar, Trustee
The Clover Trust

Nathaniel S. Mason, Trustee
Sanford Financial Trust