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MASSACHUSETTS CREDIT UNION LEAGUE, INC.

DIVISION OF BANKS AND LOAN AGENCIES
PUBLIC HEARING
September 19, 2000

STATEMENT IN SUPPORT OF PROPOSED AMENDMENTS TO 209 C.M.R. 32.32

<u>HIGH COST MORTGAGE LOAN PROVISIONS</u>

On behalf of the Massachusetts Credit Union League, Inc. ("League") and its member credit unions, this statement of support is provided relative to proposed amendments to 209 C.M.R. 32.32, *High-Cost Mortgage Loan Provisions* ("Proposed Regulations"). The League is the state credit union trade association, serving 280 state and federally-chartered credit unions that are cooperatively owned by 1.8 million consumers as members, and operating as part of the Credit Union National Association ("CUNA").

A. Credit Union Industry Overview

The thrust of the Proposed Regulations is to prohibit predatory mortgage lending practices. The Massachusetts credit union community condemns

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the predatory lending practices that some mortgage brokers and mortgage lenders in Massachusetts and across the country use to harm consumers. Predatory practices, such as excessive prepayment penalties, unilaterally accelerating on borrower's indebtedness, encouraging a borrower to default on a loan when refinancing, failing to disclose the risks of a high-cost mortgage and willfully neglecting to take into account the borrower's ability to repay the loan, are types of consumer abuses that must stop. At the same time, careful attention must be taken to safeguard consumers by not hampering legitimate mortgage programs or consumers' access to credit for home purchases. Balancing these critical public policy goals is a challenge for Congress, the Legislature, the regulators and the industry in a collaborative effort. The importance of this topic and its meaning for the credit union movement are highlighted in the April 10, 2000, *Banker & Tradesman* editorial, submitted by Gene Foley, President and CEO, Harvard University Employees Credit Union, and attached to this statement as Appendix A.

Eliminating predatory lending practices is a top priority for CUNA and the League. In an effort to set an example and to be a beacon for ethical lending in the mortgage market, CUNA and the League have developed model mortgage lending standards for credit unions, which are attached to this statement as Appendix B. These standards have been distributed to

CUNA and League credit union members, nationally and in Massachusetts, with a request to adopt similar mortgage loan and home equity lending standards and ethical guidelines that underscore credit unions' concern for consumers. As member-owned, democratically controlled financial cooperatives, credit unions want to help protect consumers from abuses of predatory lending in the financial marketplace, even though credit unions themselves offer products that are fairly priced with reasonable terms and conditions.

These guidelines are designed to emphasize credit unions' strong tradition of serving their members and protecting members' financial interests. They clearly condemn lending practices that utilize unconscionable rates and conditions to deplete a borrower's equity in his or her home. Legitimate products, such as risk-based loans recognized by fair lending and fair credit statutes that allow financial institutions to price loan products by taking into consideration the risk to the institution in making a loan, are specifically excluded from the list of abuses the guidelines address.

These guidelines also emphasize member education and support efforts of other organizations in the home mortgage marketplace, such as the Federal Home Loan Mortgage Corporation and the Federal National Mortgage Association, to improve home lending products for consumers. These organizations have developed their own standards which have been incorporated into these guidelines.

Massachusetts credit unions also operate in accordance with an industry directive released by the Massachusetts Division of Banks and Loan Agencies ("Division") relative to subprime lending issued on December 10, 1997. This directive underscores the financial, legal and compliance risks associated with subprime lending and unequivocally states that predatory lending practices will not be tolerated.

On the federal level for credit unions, the National Credit Union Administration ("NCUA") regulates and insures federally-insured credit unions and has also been active in the area of predatory lending. Last year, the NCUA Board unanimously adopted a stance against predatory mortgage lending practices and dedicated itself to work against such practices in cooperation with state credit union supervisory authorities.

In adopting its Predatory Lending Resolution ("Resolution"), the NCUA Board recognized that credit unions are generally recognized as part of the solution, not a part of the problem, of predatory lending. The Board also pledged to help determine the extent, if any, that credit union members are victimized by predatory mortgage lenders and to determine what, if any, regulations may be warranted at the state or federal level to more effectively regulate the possibility of predatory mortgage lending by credit unions. NCUA also agreed to explore the ability of credit unions to provide alternative mortgage programs to alleviate the need of credit union members to utilize services of those who engage in predatory lending practices. The Resolution is attached to this statement as Appendix C. In response to its review of its regulatory scheme and credit union mortgage practices, NCUA voted at its June 6, 2000 Board meeting not to release additional rules for credit unions to address predatory lending practices as they are not warranted at this time.

Together with industry guidelines and regulatory developments, a variety of legislative proposals are also pending in both the U.S. House of Representatives and U.S. Senate to address predatory lending. The credit union community recognizes and supports H.R. 4250 and S. 2415, *The Predatory Lending Consumer Protection Act of 2000*, introduced by Senator Paul Sarbanes (MD) and Representative John LaFalce (NY). Based upon North Carolina law, the only state to enact legislation intended to address predatory lending practices and upon the New York Banking Department's proposed regulations, these proposals provide a critical first step in the process of balancing sound public policy goals and targeting abusive predatory lending practices by expanding the federal consumer Home Owners Equity Protection Act enacted in 1994. To date, eight states have introduced legislation or a regulation to address predatory lending practices during their 2000 sessions. In Massachusetts, Senate 2202, *An Act Prohibiting Abusive Practices in High-Cost Home Mortgage Lending,* was the subject of a public hearing before the Joint Committee on Banks and Banking ("Committee") on June 15, 2000 and remains pending before the Senate Rules Committee.

B. Proposed Regulations, 209 C.M.R. 32.32, High Cost Mortgage Loan Provisions

The League supports efforts to end predatory mortgage lending practices. It remains our position that local credit unions have an enviable record relative to predatory lending and further regulation exclusively for credit unions is unnecessary. Of paramount concern is to address real abuses in mortgage lending while preserving and encouraging consumer access to credit, meaningful consumer choice and competition in the deliver of financial services to low and moderate-income families.

In testimony provided to the Committee on Senate 2202, the League urged a comprehensive review of existing laws and regulators prior to the enactment of new provisions on this topic. The Massachusetts credit union community applauds the efforts of the Division in continuing its campaign against unscrupulous and unconscionable lenders. Moreover, the League believes that the current statutory and regulatory framework enacted by the Legislature is sound and enthusiastically commends the Division for initiating enhanced measures under the existing regulatory structure to further regulate any abusive high cost loan practices. The League notes that such practices remain the target of Senate 2202 and are more appropriately addressed through the Proposed Regulations promulgated by the Division. The League applauds the commitment of the Division to this issue, as evidenced by its expanded public hearing process on the Proposed Regulations in three locations across the state, thorough and timely drafting of the Proposed Regulations and legislative testimony on Senate 2202. In addition, the League welcomes the Division's distinction between predatory lending and subprime lending, the latter of which may be performed responsibly to assist consumers with impaired credit histories due to past financial difficulties or are in need of temporary financial relief to help avoid bankruptcy or foreclosure.

The League generally supports the Proposed Regulations in their entirety. By lowering the existing interest rate and loan fee thresholds for high rate loans, extending the regulations to address open-end credit transactions and by prohibiting "flipping", negative amortization, post default penalty interest rates as well as loan modifications, deferral fees and balloon payment mortgage loans with terms of less than seven years, the rules are significantly and appropriately strengthened to combat predatory lending.

With respect to the Proposed Regulations, the League expresses a particular interest in the definition of high cost loan as it relates to the index used to determine a high cost loan, as it may be misleading when applied under current market conditions. The League notes that the proposed margin of eight to nine points permits certain flexibility in first and junior mortgages, respectively. Recently, however, the U.S. Treasury Department began to decrease the supply of 30 year bonds due to budget surpluses and debt reduction. This type of diminished supply has resulted in an increase of the price of such securities. The resulting impact has been lower than expected yields. For example, a 10 year rate of 5.728% and a 30 year rate of 5.710% have been published recently as current U.S. Treasury rates. This may be viewed as a flat or slightly inverted yield curve which would create essentially the same benchmark rate for both 10 and 30 year mortgage loans. Traditionally, lenders seek a larger return for longer term loans. Notwithstanding comparable provisions applicable at the federal level, the League encourages the Division to propose flexibility into the definition of the index and suggests that an alternative may be to review the FNMA rates for 15 and 30 years conforming mortgages. Such an alternative is a clear and conspicuous, widely published index associated with mortgage lending to which an appropriate margin may be added.

Finally, the League embraces the provisions of the Proposed Regulations relating to financial counseling. At the national level, the credit union industry has maintained a strong alliance with the National Foundation for Credit Counseling. At the local level, the overwhelming majority of credit unions support and have established relationships with their local consumer credit counseling agencies, as well as independent consumer financial education programs and endeavors.

An approach by policymakers, including both lawmakers and regulators, at every level, that is designed to increase awareness of the predatory lending problem and highlight credit unions' role as not-for-profit, consumer-owned financial institutions is welcomed by the Massachusetts credit union community. The League appreciates the efforts of the Division to achieve this goal.

ADVISORY BOARD

A Credit Union Call to Arms

By Eugene Foley

MORE AMERICANS THAN EVER before are riding the wave of home ownership. But the crest of this opportunity has come crashing down upon some of the naive and vulnerable, smashing their financial lives to pieces. With unemployment at its lowest ebb in 30 years, low- to moderate-income families stand at the edge of the American dream, looking out to a horizon of owning their own home. Unfortunately, too many of these families have been caught in the undertow of predatory lenders, who have dragged them unwittingly into a sea of debt and drown them in circumstances where everything is lost.

Last week, Federal Reserve Chairman Alan Greenspan announced the appointment of an interagency task force of the Department of Housing and Urban Development, the Federal Trade Commission, the Justice Department, banking regulators and the National Credit Union Administration to address the abuses of predatory lending. Specifically, this task force has been charged with crafting the language that will define illegal lending practices and draw the line between subprime lending and its ugly stepsister, predatory lending. While the Fed should be applauded for taking this action, a significant amount of damage has already been done.

According to HUD estimates, the subprime mortgage market has grown from $20 billion to $150 billion over the last five years. Feeding off the fat of this market, greedy and unscrupulous lenders and appraisers have posed as conventional mortgage providers while preying on susceptible borrowers with high-pressure sales tactics, misleading information, exorbitant fees, imposing terms and debt burdens that families could never repay.

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The predatory lender's tools include excessive commissions, balloon payments, falsified documents, unwarranted credit insurance costs and cannibalization of equity, but the real key to plying this trade rests solely on deception and borrower ignorance.

While legislative redress of predatory lending is much needed and overdue, the issue is complicated and prevention will take time to make its way into law. The proliferation of this problem requires immediate action, outreach and education. This is a case for credit unions. At a national conference in Washington, D.C., NCUA board member Yolanda Townsend Wheat called upon the country's 10,000 credit unions to become the front line in the battle against borrower victimization. Sighting the distinction that credit unions enjoy as financial service providers, Ms. Wheat observed that, " ... credit unions have traditionally viewed low-income and underserved communities as pools of potential, not pockets of poverty." Her remarks were a rallying cry for credit unions to attack the problem of predatory lending by providing services, education and outreach to vulnerable borrowers, before they lose their homes, life savings and self-respect to imposters.

Credit unions live in the same communities in which predators operate, but not by the same tactics. The challenge will be for this essential, yet unassuming sector of financial services to shed its traditional cloak of anonymity and to raise its own visibility so that more consumers know that it is a real and valuable alternative for borrowers otherwise abandoned by responsible competition. By waving its own flag a little higher, credit unions can arm more potential loan victims with the knowledge and financial options they need and in doing so, help lead the charge against predatory lending. ■

APPENDIX B

CUNA MEMBER CREDIT UNION MORTGAGE LENDING STANDARDS AND ETHICAL GUIDELINES

Issue: Homeowners across the country, seeking to borrow against the equity in their property, may be forced to pay excessive rates and fees, be subjected to other abusive borrowing activity, or be at risk of actually losing their homes, if they fall prey to unscrupulous lending practices known as predatory lending. Such borrowers are often elderly or other individuals facing significant financial demands who are anxious to have access to credit and thus, vulnerable to unconscionable demands and requirements of the predatory lenders.

Credit Unions Concerns/Interests

Credit unions have a proud history of service to their members and provide products that meet members' needs and are in members' best financial interests. As member-owned, democratically controlled financial cooperatives, credit unions want to help protect consumers from abuses of predatory lending in the financial marketplace, even though credit unions themselves offer products that are fairly priced, with reasonable terms and conditions.

Under the Federal Credit Union Act and/or regulations from the National Credit Union Administration, stringent rules apply to credit union mortgage lending. For example, federal credit unions are subject to a 15% usury rate ceiling, which may be adjusted up to 21% and now stands at 18%. Also, federal credit unions may not charge prepayment penalties. State provisions vary, but state chartered credit unions operate under similar limitations.

Guidelines and Ethical Standards

The following guidelines are designed to apply to non-purchase money, closed-end home equity loans. Credit unions abhor predatory lending and seek to protect consumers from such abominable practices. Predatory lending includes home equity-stripping loan products with one or more of the following characteristics:

Interest rates that are significantly above market rates and which are not justified by the degree of risk involved in providing the credit;
Excessive balloon payments that require refinancing at a rate that is more than the rate on the existing note;
Lending without regard to whether the borrower has the ability to repay;
Requirements for frequent refinancings of the loan resulting in additional costs to the borrower and significant erosion of the borrower's equity;
Prepayment penalties, in excess of actual costs incurred and unpaid;
Exorbitant fees and insurance premiums that the borrower may be required to finance, further jeopardizing equity;
Misleading or false advertising.

Predatory lending does not encompass legitimate products such as reverse mortgages or risk-based lending recognized by fair lending and fair credit statutes that allow financial institutions to price loan products by taking into consideration the risk to the institution in making a loan.

Recognizing that predatory lending is fully inconsistent with the philosophy and principles unique to the credit union system, credit unions adopting these home equity lending guidelines and ethical standards agree to:

Emphasize Member Education

- Provide a copy of these standards to member/borrowers, as applicable;
- Educate members regarding the dangers and abuses of predatory lending by offering counseling and other useful information about the lending process;

  Inform members about the differences and advantages associated with credit union lending products, such as applicable usury ceilings, lack of prepayment penalties;

  Inform borrowers about all applicable lending products the credit union offers;

  Assist borrowers in understanding applicable loan disclosures, rates, fees and terms, including any rights of rescission.

Meet Members' Borrowing Needs

Ensure home equity loan products meet the consumer's borrowing needs and ability to repay, consistent with credit union loan policies and legal requirements.

Prohibit and Refrain from Abusive Practices

Exclude terms and conditions that are not justified by the documented risk to the credit union of extending the loan;

Exclude interest rates that are higher than market indices;

Prohibit refinancing of balloon payments at a higher rate than on the original note when not justified by market conditions or the risk of making the loan;

Exclude fees and insurance premiums from the amount to be financed;

Prohibit charging for or financing insurance products or unrelated goods or services without the consent of the borrower;

Ensure lending staff are well trained to avoid potentially misleading statements in connection with a loan transaction;

Prohibit loan "flipping", which is providing a loan to a borrower to refinance an existing home loan when the new loan does not have a net benefit to the borrower, taking into consideration the terms of both loans and the borrower's circumstances;

Exclude mandatory arbitration clauses that limit the rights of borrowers to seek redress in court should problems arise.

Support Efforts in the Marketplace to Prohibit Predatory Lending

Follow the FNMA and FHLMC anti-predatory lending guidelines, which include key provisions such as:

Loans purchased may not have points or fees that generally exceed 5%, excluding discount points;
Prepaid single-premium credit life insurance may not be sold in connection with loans purchased;
Lenders which sell to FNMA or FHLMC must report on loans they are servicing each month;
Waivers should not be allowed from the requirement that servicers maintain escrow accounts fro the payment taxes, insurance premiums, etc. for borrowers with "blemished" credit records.

RESOLUTION BY NCUA BOARD

The NCUA Board supports ongoing state regulatory efforts regarding the issue of predatory lending practices. The NCUA Board would like to commend the State Supervisory Authorities on making the elimination of predatory mortgage lending practices one of their top priorities for the Year 2000.

Although credit unions are generally recognized to be a part of the solution and not a part of the problem of predatory lending, the NCUA Board hereby states its willingness to support State Supervisory Authorities in their efforts to review mortgage lending practices of credit unions as they relate to other types of lenders in order for the states to determine:

> To what extent, if any, credit union members in their states are being victimized by predatory mortgage lenders;
> To what extent, if any, credit unions in their respective states can provide alternative mortgage programs to alleviate the need of members to utilize the services of those who engage in predatory mortgage practices; and
> What, if any, regulations may be warranted at the state or federal level to more effectively regulate the possibility of predatory mortgage lending by credit unions or what regulations, if any, may need to be revised or withdrawn that may conflict with the effectiveness of the individual state's efforts to prohibit predatory mortgage lending in their respective states.

In order to support the State Supervisory Authorities in this endeavor and to ascertain the information set forth above, the NCUA hereby states its willingness to work on a cooperative basis with the State Supervisory Authorities to review issues of mutual interest and concern related to effective regulation of predatory mortgage lending.