



State Initiatives to Battle Predatory Lending May 2002

States are implementing a number of initiatives to identify and eliminate predatory financial practices within their borders. Although state laws designed to curb abusive lending practices are frequently preempted at the federal level or through interpretations of federal regulations, state banking departments have pursued a variety of approaches to address this important public policy issue.

Such efforts include: educating consumers, conducting targeted examinations, and enforcing state laws and regulations that have not been preempted. A summary regarding some of these initiatives follows.

- I. **Education Programs** - Many State Banking Departments are utilizing financial education as a tool to attack predatory lending within their borders. The impetus behind the programs is a growing belief that when consumers understand the lending process and their rights and responsibilities, they are less likely to sign agreements that are not in their best interests.

Connecticut

The Connecticut Department of Banking is implementing an educational program that will involve among others, neighborhood assistance groups, officials of Fannie Mae and the Connecticut Department of Consumer Protection. The first phase of the educational program should begin in the fall of 2001 with a seminar geared for consumers and professionals/companies that provide financed services to consumers, such as home improvement contractors.

The program will include an overview of the state's new statute prohibiting abusive home loan lending practices. The organizer's hope to advise consumers of the new protections the statute provides (effective 10/1/01) and plan to inform firms affected by the statute of the new restrictions. The Department will also

create or modify existing literature (in both English and Spanish) to educate consumers, promote financial literacy, and enhance borrowing savvy.

Delaware

The Office of the State Bank Commissioner has created a new position, the Deputy Commissioner for Consumer Affairs, to focus on consumer education and outreach issues. The new Deputy joined the Department in January 2001 and is developing a comprehensive consumer outreach and education program that includes coordination with Delaware-based community groups, churches and consumer advocates. The Department has also developed information, including two brochures, intended to facilitate informed banking/financial services decisions.

Idaho

The Idaho Department of Finance continues its active involvement in the Idaho Financial Literacy Coalition (IFLC). The IFLC is comprised of individuals from government, education, all segments of the financial industry, and non-profit organizations. The mission of the IFLC is to improve the quantity and quality of information and educational programs related to personal finance by providing resources and instruction to educators, youth leaders, and others who are in need of assistance or at financial risk.

Department personnel also volunteer as speakers in Idaho high schools, assisting in the introduction of basic financial concepts including investing, financial planning, and consumer credit information. These speakers specifically address how consumers can avoid lending and investment fraud and other abusive financial practices. In connection with these efforts, the Department created specific child/young adult educational content on the Department's web site. Finally, in cooperation with "Financial Literacy 2001", the Department made available to teachers across the state a free teaching guide to use in the financial education of Idaho's junior high and high school students.

Indiana

The Indiana Department of Financial Institutions has developed a program for high school government and economics teachers to help them inform their students about consumer credit. The Department's objective is to encourage curriculum enrichment to insure that basic personal financial management skills are attained during the high school educational experience. Curriculum topics include budgeting, choosing a credit card, purchasing an automobile and guarding

against fraud. The program also includes specific details on various consumer protection statutes such as the Equal Credit Opportunity Act and the Fair Credit Reporting Act.

Massachusetts

The Massachusetts Division of Banks maintains a toll-free mortgage hotline to assist homeowners who have questions about potentially unethical and unlawful lending practices. The hotline will also help consumers determine whether loan terms are predatory or risky and will direct consumers to other sources of information and assistance. Although the Banking Division administers the hotline, the effort is a joint initiative involving the Massachusetts Bankers Association, The Massachusetts Community and Banking Council and the National Consumer Law Center.

New Jersey

The New Jersey Department of Banking and Insurance has worked successfully with the New Jersey Department of Education and others to highlight financial education as an important way to fulfill the State's core curriculum standards. The goal of the program is to provide every New Jersey public school student with a grounding in basic banking – including an understanding of credit management, the types of loans available, how to critically assess the true cost and other relevant features of various credit instruments, and how to successfully manage one's finances. The Department has also promoted financial education through public appearances, distribution of materials, and through participation with various groups that encourage financial education.

New York

The New York State Banking Department has been instrumental in developing and distributing educational materials regarding predatory lending abuses to New York consumers. Their efforts include a video designed to showcase types of abusive lending practices that consumers should be watchful for and avenues available to consumers who believe that they have identified such practices. The video is available and accessible to consumer groups, the elderly and the general public through the Department's website at www.banking.state.ny.us. The Department has also developed brochures and has distributed them to many communities, including non-English speaking communities. Additionally, the Department has worked with community groups and has held educational outreach programs in the evenings and on weekends.

The New York State Banking Department, in cooperation with the Long Island Housing Partnership Inc., hosted a forum on June 21, 2001 on Long Island to discuss predatory lending practices and responsible subprime lending. More than 100 representatives from the public, private and not-for-profit sectors participated in the forum.

Wisconsin

The Wisconsin Department of Financial Institutions created the state's first "Institute on Financial and Economic Education" (Institute) to promote financial literacy among Wisconsin students. The Institute is a weeklong graduate-level training program that provides financial instruction for Wisconsin high school teachers. Announced in April of 2001, organizers plan to provide in-depth curriculums, teaching tools, and lesson plans to help teachers integrate financial education into their classrooms. The weeklong training course will be offered in a college setting, with private grants defraying most program costs. Participants also earn graduate credits. Additional details about the Institute are available at the Department's website located at www.wdfi.org.

II. Examination & Enforcement – In addition to educational outreach, Departments are sticking to core regulatory fundamentals by conducting targeted examinations to identify and prevent predatory lending and unfair and deceptive practices. Many states have worked successfully with their legislatures to attain increased funding levels to surgically attack predatory lending. A few examples of recent developments and programs follow.

In March 2002, the states of Arizona, California, Florida, Illinois, Massachusetts and New York, along with the Federal Trade Commission, reached a settlement in a lawsuit filed against First Alliance Mortgage Company (FAMCO) and its primary shareholders, founder Brian Chisick and his wife, Sara Chisick, which arose from the deceptive lending practices employed by FAMCO from 1992 to 2000.

Approximately 18,000 borrowers were impacted. One settlement provision mandates that the Chisicks will personally contribute \$20 million to the redress fund- an unprecedented payment in the residential mortgage banking industry. Investigations by several states revealed that FAMCO used deceptive sales practices throughout the country to deceive targeted borrowers into entering into mortgage loans without the borrower knowing the true cost and terms of the mortgage loans.

California

In January 2002, the California Department of Corporations reached a \$12 million settlement with Household Finance Corporation and its sister corporation, Beneficial, Inc. in a case involving allegations of violations of consumer lending statutes. The subprime lender must set up an office in CA where examiners from the California Department of Corporations can view its files of loans made in the state. The settlement is more stringent than those in which consumer finance lenders have merely agreed to exams. Household will face constant and ongoing scrutiny in California. The action is the result of extensive targeted examinations which suggest that Household was charging excessive fees in violation of California lending statutes.

Idaho

The Idaho Department of Finance reorganized last year in part to address the increased importance, in Idaho and nationally, of consumer finance issues. The Consumer Finance Bureau was formed to oversee mortgage brokers and bankers, collection agencies, and regulated lenders, including payday and title lenders. The priorities of the new Bureau are examinations and addressing consumer complaints. The Bureau therefore initiated routine examinations of mortgage brokers and bankers, and is on-target to examine approximately 40% of their Idaho offices each year, as well as participate in multi-state examinations. The Bureau is also committed to examine the office of every Idaho payday and title lender each year.

During fiscal year 2001, the Consumer Finance Bureau initiated 66 administrative actions against mortgage brokers/bankers for a variety of issues including improper conduct, unlicensed activity, and license application and bond deficiencies

Kansas

The Banking Department recognized the need to expand their ability to conduct robust examinations of mortgage lenders and brokers. The Department organized a new Consumer and Mortgage Lending Division and has strengthened its examination and enforcement activities this year through an increase of eight new staff positions for this important area.

Maryland

Last year the Maryland legislature enacted strict new laws with respect to examinations of mortgage lender licensees, strengthened the minimum qualifications for licensed lenders, required continuing education for mortgage lenders and granted the Commissioner enhanced powers against lenders operating without a license. The Banking Department also received four new examiner positions to focus on compliance and to investigate complaints. Additionally, the Department's staff was expanded to include two positions to focus on investigations and an attorney position to support the enforcement requirements of the statute.

To date, the Commissioner has substantially increased the number of charges filed against licensees for a variety of infractions, pursued several unlicensed lenders, revoked the licenses of three mortgage companies, worked in alliance with HUD and Postal Inspectors on mortgage "flipping", the practice of refinancing a mortgage even though the new loan has no reasonable net benefit to the borrower, and fined licensees \$375,000 for various statutory violations in FY 2001.

Massachusetts

The Massachusetts Division of Banks has worked closely with the Attorney General's Office on several egregious cases arising from the Division's licensed examination program. In one case, a lender charged 17 points to a borrower having a debt-to-income ratio of 109%. In another case, a non-bank lender was charging 10 points to consumers – a violation of state regulations that prohibit charging unconscionable rates or terms.

In the latter case, the federal court determined that the company was engaging in unfair and deceptive trade practices and ruled that the company could not charge more than five points. Since that case, five points has been an important threshold when reviewing the practices of lenders in Massachusetts. Lenders that charge more than five points face stricter regulatory scrutiny during examinations by the Massachusetts Division of Banks.

The Division of Banks also issued an industry letter in 1997 on subprime and predatory lending issues warning Massachusetts banks, credit unions and non-bank lenders about the unique financial, legal and compliance risks associated with subprime lending. It also unequivocally states that predatory practices will not be tolerated.

Washington

The Department's leadership believes that no amount of new laws addressing predatory lending can replace the need for aggressive enforcement. During 1995 through 2000, the Washington Department of Financial Institutions (DFI) executed more than 100 enforcement actions to correct abusive practices and forced the return of over \$1.2 million to Washington consumers.

The DFI evaluates not only loan files but also investigates lending practices including investigating consumer complaints through a team of individuals who understand predatory practices. The Department's leadership also believes that criminal sanctions against deceptive practices are the most effective deterrent to abusive lending.

A California mortgage lender has been ordered to return more than \$712 thousand to 120 Washington state borrowers. The order by an administrative law judge in Olympia was issued to Nationscapital Mortgage Corporation of Orange, California, which conducted business in Washington in the late 1990s.

The order also levies fines of nearly \$495 thousand against the corporation and \$245 thousand against its owner, Jamie Chisick, also of California. In addition, the order prohibits Chisick from conducting the business of a mortgage broker in Washington for 20 years and his top officers for five years.

Consumer complaints led to an investigation by the Department of Financial Institutions (DFI) in June 1997. The investigation spanned several months, culminating with the Department charging Nationscapital with deceptive practices, failure to make proper disclosures, and imposing prohibited overcharges.

The DFI has also distributed materials intended to help Washington state examiners identify deceptive and predatory mortgage practices. For example, some predatory lending schemes involve deception about the loan type the consumer actually receives. Loan type deception is generally related to the sale or delivery of an adjustable rate mortgage (ARM) instead of a fixed rate mortgage, that the borrower desired. In some cases, the borrower is unaware that they received an ARM at closing because the ARM's initial rate approximates that of a comparable fixed rate mortgage. The memorandum also provides examples of practices involving deception regarding loan cost and monthly payments.

New York

The New York State Banking Department (NYSBD) conducts ongoing examinations in order to identify and halt incidents of abusive lending practices. Among the tools at the Department's disposal are the ability to revoke mortgage bankers' licenses and the ability to impose fines. The Banking Department recognizes that active enforcement is required if strong laws and regulations governing residential mortgage lending in New York State are to achieve their purpose fully. In one recent enforcement action, a lender, acting in a broker capacity, charged brokerage fees that were not reasonably related to the work done, or the services provided. This action was brought on the basis of the licensee's character and fitness. In many of the loan files, between 8 and 10 points were charged even though the banker/broker did not complete the application and did not process the loan application. This is the first time that a New York entity lost its license because of the fees it charged.

In a second matter, the Banking Department entered into a settlement agreement in which the company paid in excess of \$200,000 in consumer restitution and \$70,000 in fines. The lender often failed to provide required notice of the right to rescind and even more often failed to return fees when the borrower did rescind the loan.

In the third action, two employees of a mortgage broker allegedly conspired with loan officers at two lenders to mischaracterize broker fees as home improvement costs so that the loan skirted certain state-based lending provisions. The matter was brought to the attention of the Department by one of the lenders who discovered the problem during its review of one of the loans. Ultimately, the broker surrendered its license with prejudice and left New York, the lenders made approximately \$300,000 in consumer restitution and a criminal referral has been made to the United States Attorney for Western New York. The lenders, although they did not knowingly make Part 41 loans, had to provide the consumer refunds so that the loans actually would be below the Part 41 thresholds since the original terms were not in compliance with the regulation.

Another Part 41 case arose from the Banking Department's examination findings. The lender, when calculating points and fees, excluded title and appraisal fees from the calculation. However, such fees must be included in certain circumstances, such as, in this case, when the fees are paid to an affiliate. When the fees were included in the calculation, the thresholds were exceeded and the loans should have been treated as Part 41 loans. In order to cure this situation, the lender will be required to pay a fine and to make refunds to the borrowers to bring the cost of the loans below the Part 41 thresholds.

In May of 2001, the NYSBD revoked the mortgage banker license of East Bay Funding Corporation, for failing to comply with five provisions of the New York State Banking Law and Regulations. One of the key issues that led to the revocation was the Department's finding that the institution charged fees that were not reasonably related to the work and services performed on behalf of borrowers. The Department also imposed a fine of \$100,000.

Previously, in February of 2001, the Banking Department revoked the mortgage banking license of Anvil Mortgage, Ltd., and worked with the New York Attorney General to obtain \$1.1 million in restitution for consumers who paid a \$500 fee to Anvil, but received no services in return. In late 2000, the Department revoked the mortgage broker registration of Homer Funding for engaging in fraudulent activities and misappropriation of consumer funds. This matter was referred to the Nassau County District Attorney who obtained an indictment against the owner of the company. In September 1999, the Department, in conjunction with the United States Department of Justice and the New York Attorney General, entered into a settlement with Delta Funding Corporation that called for millions of dollars in consumer restitution.

Wisconsin

In June of 2001, the Wisconsin Department of Financial Institutions fined a mortgage broker and loan originator for failing to disclose pre-payment penalties to borrowers, for failing to include debts of the mortgage applicant, and for failing to establish an escrow account despite their contractual obligation to do so, per the agreement executed with the borrower. All events violated Wisconsin law. Fines totaled approximately \$7,000.

Connecticut

As indicated previously, Banking Departments routinely utilize license revocation as a tool to assure reputable and lawful business practices among their mortgage bankers and brokers. In March, the Connecticut Department of Banking revoked the mortgage broker lender license of Homefn Mortgage Corporation because the company failed to file a bond with the Commissioner as required by Connecticut law. Many states require mortgage bankers and brokers to maintain a bond in the event that the institution encounters difficulty and the Department must refund monies or take other actions to protect consumers.

III. Proposed Legislation/Regulation – Nearly 30 state legislatures are considering bills to restrict predatory lending within their borders. Some legislation has also been proposed at the city or county level (such as Philadelphia, Pittsburgh, Dayton, and Baltimore). The majority of the proposed bills seek to restrict predatory lending by restricting “predatory lending practices” on high cost loans (e.g., loans with an APR of 8% or more over the yield on the US Treasury securities index). States have identified predatory lending practices to include “flipping”, “packing” (the practice of adding ancillary products to the loan such as single premium credit life, disability or unemployment insurance), and encouraging default on existing debt. These practices have been banned in the majority of the proposed legislation. Proposed legislation in the majority of the states with pending bills also prohibits the extension of credit without regard for the ability of the borrower to repay, prepayment penalties, balloon payments, advance payments, and lending without home ownership counseling.

New York

New York State plans to ban the financing of single-premium credit insurance in any loan that is subject to its anti-predator regulation. The ban will be part of a wide-ranging amendment to a 2000 regulation, and will be proposed in April 2002. The 2000 regulation bars "high-cost loans" with certain features, including balloon payments within seven years of origination if more than twice the average of earlier scheduled payments. A loan is considered high-cost if the annual percentage rate is more than 8 percentage points above the yield on Treasury securities or if points and fees exceed 5% of the loan amount.

IV. Existing Legislation and Regulation – Although many anti-predatory lending bills are pending, as of last year fewer than ten states had enacted laws that specifically targeted predatory or abusive lending practices. Instead of specific anti-predatory lending statutes, many states used a variety of other existing state laws to combat unfair lending practices.

Additionally, a few states have either promulgated regulations or have passed laws that specifically target predatory lending. Examples follow.

California

The California Assembly narrowly approved a measure September 12 to restrict interest, fees and predatory practices in the subprime lending industry. An amended version of the bill (AB489) was approved by a vote of 41-27. The bill would limit fees charged on loans of less than \$250,000 secured by property to 8

points over similar-term Treasury yields or no more than 6 percent of the face value of the loan. The law bans penalty charges for early loan repayment; loans to consumers that are larger than they can afford; unwarranted refinancings; hidden fees; and steering consumers to higher-priced loans when they could qualify for a loan for borrowers with good credit histories. AB489 has already passed the state Senate and is supported by Gov. Gray Davis, who is expected to sign the bill.

Connecticut

The Connecticut Legislature passed the “Abusive Home Loan Lending Practices Act”. Effective in October 2001, the Act prohibits a series of terms including the following in high cost loans: balloon payments in mortgages with a term of less than 7 years; negative amortization; an increase in interest rate after default or default charges that are more than 5% of the amount of the default; a mandatory arbitration clause or waiver of participation in a class action. The Statute also prohibits the following acts by a lender making a high cost loan: payment to a home improvement contractor from the loan proceeds except under certain conditions; imposition of prepaid finance charges that exceed the greater of five percent of the principal amount of the loan or \$2,000, except for designated exceptions; making the loan unless the lender reasonably believes the borrower can repay it; recommending or encouraging default on an existing loan prior to closing on an additional loan. The Statute also authorizes the Commissioner to impose a maximum civil penalty of \$15,000 on any person for a violation of key sections of the Act. The statute also authorizes the Commissioner to impose a maximum civil penalty of \$15,000 on a Connecticut bank, credit union or officer or director of the Connecticut bank or credit union.

Illinois

The Illinois Office of Banks and Real Estate along with the Illinois Department of Financial Institutions promulgated and has adopted restrictions on predatory lending practices. The restrictions are effective on loans with an APR of 6% or more on a first mortgage, or loans that charge more than 8% on a junior mortgage over the yield on the US Treasury securities index. Restrictions also apply to loans with points and fees that equal the greater of either 5% of the total loan amount or \$800. The restrictions prohibit lending to a borrower without considering their ability to repay, “flipping”, prepayment penalties, negative amortization, balloon payments, advance payments, lending without home ownership counseling, fees over 6% of the loan amount and financing single-premium credit life, income, disability, unemployment or health insurance premiums.

Kansas

In 1999 the Kansas consumer credit regulatory agency merged into the Kansas Office of the State Bank Commissioner and a new Division of Consumer and Mortgage Lending was created by the state's legislature. That same year the legislature substantially strengthened the state's consumer lending and mortgage laws to combat predatory lending practices. New enforcement tools included criminal penalties for violations of the law, the ability to issue monetary fines and administrative enforcement actions, subpoena powers, and restrictions on finance charges, fees, negative amortization and balloon payments on high rate mortgages. In 2001, lawmakers added new requirements to the existing lending statutes related to prohibited activities and also required mandatory continuing education for mortgage brokers.

Maryland

Maryland Democratic Governor Parris Glendening signed into law a bill to preempt the state's cities and counties from enacting their own predatory-lending legislation.

Though considered an industry-friendly law, it includes several rules that lenders must follow when originating certain loans.

For instance, they have to provide homebuyer education or housing counseling information and are barred from financing single-premium credit insurance into the relevant loans and from making the loans without considering a borrower's ability to repay.

The loans in question are those carrying an interest rate 7 percentage points higher than a Treasury security of comparable maturity or those with points and fees higher than 7% of the loan amount.

The Maryland law takes effect June 1, 2002.

Massachusetts

The Massachusetts Division of Banks has issued regulations intended to curb predatory abuses in the mortgage lending market for high cost loans. The regulation was effective on March 22, 2001 and is designed to address unfair and deceptive practices including: unconscionable rates and terms; unreasonable charges, oppressive mandatory arbitration clauses; requiring a waiver of participation in class action suits; "flipping"; "packing"; increasing the interest

rate after default and failure to report positive credit payment histories after the loan is made. The creditor must also consider the applicant's ability to repay and must disclose that the high cost loan may not necessarily be the least expensive loan available to the potential borrower. The new regulations also ban single premium credit insurance for all high cost home loans.

The regulations affect loans based upon two thresholds: fees/points and interest rates. For example, the regulations affect loans that feature points and fees that exceed either 5% or more of the total loan amount - or \$400. The regulations also cover loans with an APR of 8% or more on a first mortgage or more than 9% on a junior mortgage over the yield on the US Treasury securities index.

Minnesota

Mortgage lenders in the state must follow standards of conduct that include prohibitions: (1) on fees when no product or service is provided; (2) on false, deceptive or misleading statements; (3) on making residential loans with the intent that the loan will not be repaid and the lender will obtain title to the property via foreclosure; and (4) on making a higher cost loan than underwriting or credit scoring data would indicate the borrower is entitled to unless the borrower consents in writing. Regarding usury, Minnesota law was recently amended to require out-of-state lenders to comply with limits on real estate loan rates and charges.

Montana

A number of state legislatures have transferred responsibility for consumer loans, mortgage brokers and bankers to the Banking Department. For example, on January 1, 2002, the Montana Title Loan Act will become effective. The Act provides for regulation and examination of lenders of this type.

New York

The New York State Banking Department has adopted a regulation to address predatory lending abuses. Key features of the regulation include: a requirement that the lender must have due regard for a borrower's ability to repay the loan; a reduction in the thresholds that are set forth in HOEPA which characterize high cost loans, a prohibition on "flipping" and "packing" and an "unconscionability" standard. Also, lenders may not charge points and fees if the last financing was within two years and may not finance points and fees in an amount greater than five percent of the loan amount at any time. Finally, lenders must also provide a

counseling disclosure to all applicants along with a list of counselors approved by the Banking Department

The New York State Banking Department is also writing guidelines related to the securitization of subprime loans. The guidelines will focus on ensuring that all loans that are packaged by lenders and sold to investors meet sound underwriting and appraisal rules and comply with applicable federal and state consumer protection laws. The Department is drafting the guidance because although securitizations have provided greater access to capital which has benefited subprime borrowers, securitizations have also provided funds for abusive lenders.

North Carolina

North Carolina's Predatory Lending Law was the first in the country that specifically addressed the issue of predatory lending. Since its passage, many other state legislatures have looked to key provisions in the statute as a model for possible approaches in their states. Specifically, the new law targets "high cost" home loans under \$300,000. The definition of a high cost loan under the law is a loan that includes:

- (1) An APR that exceeds the Treasury rate by more than 10 points;
- (2) Points and fees that exceed 5% of the total loan amount if the loan is \$20,000 or higher;
- (3) Points and fees of either 8% of the total loan, or \$1,000, whichever is less, if the loan is under \$20,000;
- (4) Prepayment penalties of more than 2% of the amount a borrower had prepaid on their home loan, and;
- (5) Prepayment penalty if the borrower pays off the mortgage later than 30 months after closing.

Elevated interest rates, points and prepayment provisions are not prohibited. The drafters did not want to limit access to credit. However, under the North Carolina statute, loans that fall within the definition of a high cost loan trigger a series of protections designed to prevent predatory practices. For example, the statute limits or bans practices that can have the effect of making timely repayment impossible. Some argue that such practices "set up" borrowers to default and thus lose their home. The statute specifically:

1. Bans call provisions, preventing the lender from accelerating indebtedness;
2. Limits balloon payments by preventing a payment that is more than twice the amount of the regular payment;

3. Limits negative amortization, prohibiting a payment schedule that causes the principal to increase;
4. Bans increased interest rates after the borrower defaults;
5. Limits advance payments, preventing requirements that more than two payments be consolidated and paid in advance;
6. Bans modification or deferral fees, preventing a lender from charging any fees to modify, renew, extend or amend a high-cost loan or to defer any payment that is due, and;
7. Limits "packing", preventing lenders from adding single premium credit life, disability or unemployment insurance to the loan amount.

The North Carolina statute also prohibits "flipping" and restricts the practice of recommending or encouraging default on an existing loan or other debt in connection with a proposed refinancing. The statute also prohibits high-cost home loans unless the borrower receives financial counseling. Additionally, the lender must reasonably believe that the borrower will be able to repay the loan. The law also bans the refinancing of prepayment fees or penalties payable by the borrower in a refinancing transaction.

The statute also prohibits loans that would allow unscrupulous home improvement contractors and lenders from collaborating to provide loans with rates and fees that were beyond the ability of the borrower to repay. Violations under the North Carolina statute trigger usury penalties, forfeiture of interest and return of twice the interest paid. Treble damages may also be awarded to the borrower.

Governor Mike Easley has also signed into law a new statute giving the state's banking commissioner broader authority to regulate mortgage lending. Included in the provisions of the law (SB904) is a requirement that mortgage lenders and brokers obtain licenses from the state. Previous law required only that the mortgage companies register with the state. The new law, which contains other provisions to deal with predatory lending, takes effect in July 2002

Pennsylvania

The Commonwealth of Pennsylvania passed the Mortgage Bankers and Brokers and Consumer Equity Protection Act on June 25, 2001. The substantive provisions of the anti-predatory lending statute apply to all lenders and brokers offering certain home equity loans in Pennsylvania. However, the act includes other provisions that apply only to depository institutions, and others affect non-depository institutions, including entities required to be licensed to originate or broker residential first mortgage loans.

Key provisions of the statute include the following:

- ?? Localities are prohibited from enacting and enforcing local banking laws that apply to state or federally chartered financial institutions.
- ?? Covered loans include closed-end home equity mortgage loans of less than \$100,000 made at a high cost, and involving property located in Pennsylvania. For the purposes of the Act, high cost loans are generally synonymous with HOEPA loans.
- ?? Prohibitions on loan terms such as: (i) balloon payments, (ii) call provisions, (iii) negative amortization, (iv) increased interest rate upon default, and (v) prepayment fees or penalties.
- ?? Prohibited practices include: (i) lending without regard to the consumer's ability to repay the loan, (ii) charging points on a refinancing if the most recent financing was within one year, (iii) refinancing a zero interest rate or low-rate loan made by a governmental or nonprofit lender unless the loan is at least 10 years old or the current holder of the loan consents to the refinancing, (iv) paying loan proceeds directly to a home improvement contractor, (v) selling single premium credit insurance in connection with a loan unless the borrower is given the option of purchasing all such credit insurance on a monthly basis.
- ?? Required practices include: (i) providing a notice of the features of the high cost loan to the borrower at least three business days prior to consummation of the mortgage transaction; (ii) a borrower must be notified, in writing, that the purchase of credit insurance is not a required condition of obtaining the loan, and that the credit insurance may be cancelled within 30 days of the date of the covered loan; (iii) lenders and brokers shall maintain records to facilitate the Department determining statutory compliance; (iv) a lender or its servicer must file quarterly credit reports with a nationally recognized consumer credit reporting agency; (v) lenders shall verify that each mortgage broker with whom it does business holds the required license to engage in business in Pennsylvania.

Virginia

Virginia's legislature passed the Commonwealth's Mortgage Lender and Broker Act in 1987. The statute supplements Virginia's "Money and Interest" laws and requires mortgage companies and lenders not affiliated with state or federal depository institutions to be licensed and supervised by the state. The statute also prohibits certain abusive practices and provides enforcement mechanisms against violators.

Through the statute, the Department has used a three-pronged approach to prevent predatory lending practices. Staff has assessed lenders' qualifications to enter the business and become licensed, monitored the overall business and performance of licensees, and executed enforcement actions to penalize violations, deter offenses, and remove repeat offenders, if necessary.

According to Commissioner Face, Virginia's laws worked well until recently, when a trade association of alternative mortgage lenders in Virginia utilized a 1996 Office of Thrift Supervision opinion that preempted state law under AMTPA. The U.S. Court of Appeals for the Fourth Circuit has ruled against the Virginia Commissioner of Financial Institutions, E. J. Face, Jr., blocking the enforcement of a Virginia law against predatory lending. The ruling, *NHEMA v. Face, Hancock & Earley*, upheld an earlier decision from the U.S. District Court, which found that Virginia's statutory limits on prepayment penalties do not apply to licensed lenders making "alternative mortgage transactions" under a 1982 federal law, the Alternative Mortgage Transaction Parity Act. The Virginia Bureau of Financial Institutions has argued that this law was not intended to preempt consumer protections such as bans on prepayment penalties, and has filed its appeal with the U. S. Supreme Court.

West Virginia

West Virginia's statute limits broker and lender fees, including yield-spread premium, to 6%. No yield-spread premium is allowed when the APR exceeds 18%. The statute also prohibits: (i) negative amortization; (ii) loan to value ratios in excess of 100%; (iii) prepayment penalties on subordinate loans and caps the penalty at 1% for the first three years on first mortgage loans; (iv) collecting fees not disclosed to the borrower; (v) coercing appraisers to give false appraisals; (vi) and lending based solely on equity of a house. Lenders and brokers must also document a net tangible benefit to the borrower before refinancing a borrower's loan within 24 months of the prior loan.

West Virginia also allows the Bank Commissioner to levy a penalty of up to \$1,000 for every violation of law. Brokers must obtain 7 hours of continuing education per year for each loan processor beginning in 2002. The statute also provides several consumer-specific protections. Consumers can receive attorney fees when suing for violations of the law; consumers must be given a copy of every document they sign at closing and interest rates are capped at 18% on second mortgages.

- V. **Conclusions Drawn** – CSBS has officially commented and taken the position that predatory lending is best attacked and prevented through: (i) educational outreach; (ii) rigorous examinations; (iii) collaboration among State Banking Agencies, Federal Banking Agencies, the FTC, the Department of Justice, HUD and related entities; and (iv) enforcement of federal and state laws (many of which already exist) that prohibit unfair and deceptive trade practices. CSBS commends and is encouraged by the growing number of State Legislators that have increased funding and resources to State Banking Regulators to better equip them to battle this challenging public policy problem.