Legislative History for Connecticut Act

Act Number:	08-176	
Bill Number:	5577	
Senate Pages:	5058-5151	94
House Pages:	5474-5553	80
Committee:	Banking: 215-339, 353, 370-373, 384-403, 426-470, 472-476, 492-494, 522-527, 529-533, 536-537, 541-546, 549-550, 552-565, 570, 572, 574, 585-587, 590-603	139
	Page Total:	313

Transcripts from the Joint Standing Committee Public Hearing(s) and/or Senate and House of Representatives Proceedings

Connecticut State Library

Compiled 2014

S-573

CONNECTICUT
GEN. ASSEMBLY
SENATE

PROCEEDINGS
2008

VOL. 51
PART 17
5058-5352

like to mark Calendar Page 19, Calendar 431, Senate Bill 702, and at this point also one additional item, Calendar Page 19, Calendar 447, House Bill 5646. Thank you, Mr. President.

THE CHAIR:

Thank you, Senator Looney. Mr. Clerk, would you please commence with the Call of the Calendar, starting with the Order of the Day?

THE CLERK:

Calling from Senate Calendar for Wednesday, May 7, 2008. Calendar Page 11, marked Order of the Day. Calendar 549, File 114, a Substitute for House Bill 5577, An Act Concerning Responsible Lending and Economic Security, as amended by House Amendment Schedule "A" Favorable Report of the Committees on Banks, Judiciary and Finance, Revenue and Bonding.

THE CHAIR:

Senator Duff.

SEN. DUFF:

Thank you, Mr. President. Good afternoon.

THE CHAIR:

Good afternoon, Sir.

SEN. DUFF:

Great to see you.

THE CHAIR:

And you also.

SEN. DUFF:

Mr. President, thank you. I move the Joint Committee's Favorable Report and passage of the bill in concurrence with the House.

THE CHAIR:

The question is on passage and concurrence, acceptance and passage and concurrence with the House. Senator Duff, will you remark, Sir?

SEN. DUFF:

Thank you, Mr. President. Mr. President, this bill's title actually explains the bill very well. It's called An Act Concerning Responsible Lending and

Economic Security. And I believe that today we're on that path towards really defining responsible lending and economic security for the State of Connecticut and with a problem that is plaguing the entire nation.

And I'm very proud of the fact that Connecticut is debating this bill today and moving forward on what is a very progressive and comprehensive and balanced, probably one of the most balanced bills that we'll see in the nation.

Mr. President, this bill has five parts. Let me explain them very briefly. The first part, Mr. President, has to do with a regulatory piece that actually defines, puts a definition on sub prime loans. It actually calls them nonprime in the bill, but we finally have a definition of sub prime bills.

And it states new duties for lenders. It has new protections for borrowers, such as it eliminates prepayment penalties, collects escrow payments, provides numbers for counseling and many, many other

protections for borrowers who are coming in, who may be in the sub prime or nonprime category.

It also sets, Mr. President, the second part sets up a mediation process, which I think will help our consumers in the state very much. And I think it will also help the banks quite a bit too because, as we know, no bank likes to foreclose on a loan. And if we can get people in a setting where there's foreclosure mediation that is a good thing.

What we do is we set up a foreclosure mediation process in each judicial district, and that helps borrowers and lenders really kind of work things out before we get to the point of no return. So I think that that's really a strong part of this piece of legislation and will go a long ways in helping both banks and also consumers.

Third is we have some money, some funding that will help struggling families in this state. What we have right now is we have the Connecticut Families

Program, which is the Governor's initiative last year, after the sub prime taskforce, which will be about $40 million, which allows borrowers and families in the State of Connecticut to help refinance some of their loans.

And that's been, certainly, something that's been worked out and improving day by day. And we feel that this will be an integral part of any process that we go forward with on this issue.

We're also putting in $30 million for what's called the HERO Program, which, actually, CHFA will buy. Connecticut Housing Finance Authority will buy loans from banks at a discount, and get people back on their feet again.

And I think that this HERO Program is going to help people who are not qualified for the Connecticut Family Program, but will help people stay out of foreclosure. And let me just remind the Circle that it does no good for anyone to have their neighbors in

foreclosure, to see boarded up homes, to see houses that have not been cared for does not help anybody's property values.

So these programs, the CT Families and HERO Programs really do a good job, and will do a good job. And CHFA will be developing the HERO Program once we pass this bill.

We also have $64 million for the Emergency Mortgage Assistance Program, which will now become a revolving fund. And there's some people in the Circle who may remember in the past that we had the Emergency Mortgage Assistance, I believe, with $5 million. Now we're going to be having $64 million with revolving. Before, it was not revolving. And this has actually been expanded to help families.

Mr. President, one of the other pieces that is vitally important, I believe, to this bill is a provision that actually allows the workplace incorporated in other workforce development to help

people who are unemployed or underemployed, and get back on their feet again.

Again, we don't want to get the people where they're to the point of no return. If we can help people back into job training and help people back into unemployment or underemployment, that's exactly what we want to do.

We want to move people back into employment so they don't get into the process where they're in a foreclosure problem.

Our U.S. Senator, Senator Chris Dodd, who is Chairman of the Banking Committee in Washington, who is working very, very hard and diligently on this issue, has always said, and when I was an intern for him, he used to always say the best social program is a job. And I think that's one of the reasons why this provision is extremely important.

The last piece is that we have a provision in there that says that the Connecticut Housing Finance

Authority will develop and implement a program in which they can buy houses that have already been foreclosed.

Unfortunately, we know that we're trying to help a lot of people, but we know that we can't help everybody. There will be some foreclosures, as we've already seen. And we're asking CHFA to implement and develop a program that will allow them to purchase homes that have already been foreclosed for affordable and supportive housing.

So I think that's kind of where we are with this. I will also say too that we can take great pride in the fact that we have put together a bill, in ten weeks, here in this Legislature, that I think is, again, one of the best bills probably in the nation. Hopefully, it will be a model.

And, unfortunately, our Congress is still a year and a half, and we've done in ten weeks what they haven't done in a year and a half. And we also can

take great comfort in the fact that not one of our Connecticut chartered banks or Connecticut chartered credit unions were involved in the sub prime crisis.

But we're moving forward. We're going to make sure that we're incorporating everybody, and we're holding everybody to the same, high standard. So again, it's a comprehensive and very progressive bill.

And I also, I'd be remiss, before I sit down and take some questions, if I didn't thank some people who worked so tirelessly on this issue.

And that would be my Co-Chair in the House, Representative Ryan Berry, Senator Rob Kane, who's really been invaluable on this whole issue, Commissioner Howard Pitkin and his staff, the Governor's office, our LCO staff, CHFA, of course.

And our colleague, Senator Coleman, has been very helpful, Senator Gomes, Senator McDonald, and, really, I think this is one of those issues where this has been a team effort. And when we have the problem that

we have with sub prime and foreclosures, this is one of those instances where the team effort is what it's all about, and it's what is going to carry the day in helping as many people as we can help.

So with that, I move that we pass the bill, send it off to the Governor, and begin the process of keeping our economy stable. Thank you, Mr. President.

THE CHAIR:

Thank you, Senator Duff. Will you remark further on the bill? Senator Coleman.

SEN. COLEMAN:

Thank you, Mr. President. Good to see you up there.

THE CHAIR:

You also, Sir.

SEN. COLEMAN:

I have a question for Senator Duff.

THE CHAIR:

Please proceed, Sir.

SEN. COLEMAN:

Thank you, Sir. Senator Duff, just to clear up some ambiguity that may be read into the bill, particularly around Line 612 of the bill as amended, it makes reference to a homeowner seeking mediation and the requirement that that homeowner must file a request for mediation, along with an appearance, within 15 days after the return date.

It allows the court to extend the date for filing the application and appearance for an additional ten days. And then because of the wording in Line 612 of the amendment, it may appear that the bill is also prohibiting any defendant in a foreclosure action, including one not necessarily seeking mediation, from filing an appearance more than 25 days after the return date.

Am I correct that this language, the language that refers to restricting the filing of an appearance is 25 days after the return date? Am I correct that

that only refers to a defendant who is seeking to be involved in the mediation process?

THE CHAIR:

Senator Duff, do you care to response, Sir?

SEN. DUFF:

Thank you, Mr. President, through you. Thank you, Senator Coleman. Yes. That is correct.

SEN. COLEMAN:

Okay.

THE CHAIR:

Senator Coleman.

SEN. COLEMAN:

Thank you, Sir. And the second question, probably briefer, am I correct that nothing in the bill restricts the Superior Court judges from exercising their existing equitable powers when they preside over foreclosure actions, through you, Mr. President?

THE CHAIR:

Senator Duff. Thank you, Senator Coleman. Senator Duff.

SEN. DUFF:

Thank you, Mr. President, through you. Yes. That is correct.

THE CHAIR:

Senator Coleman, you have the floor, Sir.

SEN. COLEMAN:

I thank Senator Duff for his responses to my questions, and I'd just like to make some brief comments regarding the bill as amended. First of all, to commend Senator Duff, I know he put in a lot of hours and a lot of effort in bringing the proposal to the state where it is.

Hopefully, it will help both lenders and consumers in the State of Connecticut with their interests with respect to foreclosure actions. I think we all are a little distressed, more than a little distressed and alarmed at the rate of

foreclosures that are occurring nationwide, but particularly in Connecticut.

And I think this bill is a step in the right direction toward addressing the situation that's resulting from nonprime or sub prime loans and the crisis that's surrounding that particular situation.

Whatever we can do to preserve people's ownership of their homes, I think we ought to do. This piece of legislation seems to be remedial in that respect. And the bill, to me, is a very important piece of remedial legislation, at a time when real economic crisis for homeowners is occurring.

It is my hope that the judges who hear foreclosure cases will apply this bill in a way that allows this remedial purpose to be carried out. Thank you, Mr. President.

THE CHAIR:

Thank you, Senator Coleman. Senator Handley.

SEN. HANDLEY:

Thank you, Mr. President, and thank you. Through you, I'd like to speak in support of Senator Duff's proposal, and to thank him very much for the very hard work that I know he and Representative Ryan have put into it.

I find it appalling. I have lived in my neighborhood, in the house I'm in, for 40 years. And I've never seen a foreclosure sign in my neighborhood in those 40 years. Right now within half a mile of my house, there are three foreclosure signs.

This is the situation that we're dealing with, in an older, really very stable community, to find three such signs, such demonstrations of a society that is in deep trouble.

And while I'm sure there is much more that needs to be done, and all of us are going to be working on other areas as the time goes on to prevent this from happening again, to ameliorate the situation right now is absolutely necessary.

We can't have children and their families with children essentially out on the street. And that's what it looks like could happen to three families in very close circuit of my house. So thank you. Through you, Mr. President, thank you, Senator Duff.

THE CHAIR:

Thank you, Senator Handley. Will you remark further? Senator Nickerson.

SEN. NICKERSON:

Thank you, Mr. President. If I may, through you, a question to the proponent.

THE CHAIR:

Please proceed, Sir.

SEN. NICKERSON:

Thank you, Mr. President. If I may, Senator Duff, I want to refer to a provision in the OLR analysis of the bill, which refers to the bill's requirement that CHFA transfer to DECD $40 million of CHFA's pre-1986 bond sale proceeds.

And the analysis goes on to indicate that the bill requires that this money be used for the I'll call it R-e-a-l, Real, and H-e-r-o, HERO Programs. Now here is the question that the analysis raised. I'm reading now.

It is unclear whether this action may violate CHFA's bond covenants to use those proceeds, that is the bond sale proceeds, for the purposes specified in this bill, end quote.

Do we have an opinion of counsel, so that the Legislature can be confident that the issue raised in the OLR analysis, with regard to the potential bond covenants, need not be a worry, and that we are confident that in enacting this bill there is no potential for violating those covenants, through you, Mr. President?

THE CHAIR:

Senator Duff, do you care to respond, Sir?

SEN. DUFF:

Thank you, Mr. President. Yes. Through you, to Senator Nickerson, we feel very comfortable, when we were negotiating this bill that this will not violate any covenants or effect the bond rating over at CHFA. As a matter of fact, when we were writing this bill, they were in the room with us.

I've signed off on the language, and that issue was brought up, prior to the writing of the final language of this legislation. So from their standpoint and our standpoint, we all feel very confident of the fact that this will not affect CHFA in any kind of negative way.

We also mentioned that the Connecticut Families Program, which was part of the Governor's initiative, was $50 million, and for the HERO Program it's $30 million.

We're cutting back CT Families to $40 million. It's all the same [inaudible] money that is sitting at

CHFA right now, which will not affect their bond rating in the least, through you, Mr. President.

THE CHAIR:

Senator Nickerson.

SEN. NICKERSON:

So the answer is we do not have an opinion of counsel? You didn't mention an opinion of counsel. So my question was do we have a written opinion of counsel to the effect that the enactment of this bill and the use of the proceeds does not violate CHFA covenants?

THE CHAIR:

Excuse me, Senator Nickerson. The Chair is having a real hard time hearing Senator Nickerson and the question he is attempting to pose to Senator Duff. If the Chamber could come to order, please, and give your attention to the two gentlemen who are engaging in colloquy on this bill. Senator Nickerson, you have the floor.

SEN. NICKERSON:

Thank you, Mr. President. If I may, I'll kind of step back, and start the question again. Thank you, Mr. President. Bond covenants are very technical provisions, and they are a contract between the state and the bondholders.

The potential, even the possible potential violation of a bond covenant is, of course, a very serious event. Bonds could be called into default, and that could have ripples and ramifications. I'm not suggesting that I know at all that is the case. I don't know that.

But what I am a little concerned about, if I heard your answer correctly, is we do not have a legal opinion of bond council, addressing the question raised by OLR, to assure us that there is no violation of covenants.

I know you said you feel there isn't, and you may well be right. But wouldn't it be much better to have

a legal opinion of bond council, which I gather we do not have, through you, Mr. President?

THE CHAIR:

Senator Duff.

SEN. DUFF:

Thank you, Mr. President. Through you, well, I think the feeling was that since the Governor had the initiative of the Connecticut Families Program and the HERO Program is using the same pot of money that there's the precedence to do that. Of the $40 million for CT Families, $30 million for HERO, it's the same pot of money.

There's a precedence that the Governor used when she announced the CT Families program. So, therefore, there's a precedence for doing that. And, again, in discussions with CHFA, we did ask them if this would violate or impinge their bond rating, and the answer was no.

THE CHAIR:

Senator Nickerson.

SEN. NICKERSON:

Thank you, Mr. President. Well, okay. I remain concerned. I don't know how concerned, and I'll have to think about that. But I remain concerned that we don't have a legal opinion of bond council responding to the issue raised, not by me, but by the OLR bill analysis with regard to a question.

We can't help reading what the bond analysis says, excuse me, the bill analysis. And it says there may be a covenant issue. Further down in the analysis, in a subsequent paragraph, there's reference in the bill analysis to a question as to whether this legislation could be in violation of the contract clause of the United States Constitution in that the enactment could be in conflict with bond covenants.

And there's a citation of a U.S. Supreme Court case that held, in that case, that the nature of the

bill enacted by a state did impair contracts and covenants. It's called *Home Building vs. Loan, 1934.*

The key phrase following that reference to the analysis is as follows, quote. It is not clear how that ruling, the Supreme Court ruling, would affect the bill in question, end quote.

My question, through you, Mr. President, is do we have a legal opinion that the contracts close of the United States Constitution is not violated by this bill?

I ask, of course, not because I raised the question, but because the OLR bill analysis before us this afternoon raises the question, through you, Mr. President.

THE CHAIR:

Senator Duff.

SEN. DUFF:

Thank you. Senator Nickerson, I thank you for your question. Your point that you raise, I believe,

comes from the bill analysis of the file copy, not from the bill analysis of the amendment, and the amendment is a strike-all of the bill.

The issue that you raised is when, in our first bill, we were taking that money from CHFA and putting it towards DECD. We don't do that any more. All this is now housed in CHFA. Those issues are now resolved because we're not transferring the money from the Connecticut Housing Finance Authority to the Department of Economic and Community Development.

THE CHAIR:

Senator Nickerson.

SEN. NICKERSON:

But is it not the case that it may not be the case? You may help me on this. Is it not the case that CHFA will be using the same bond proceeds internally within CHFA as would have been the case under the file copy, had the funds been transferred to DECD?

Thus, if the use of the proceeds is for the same purposes, though in a different organizational framework, the same questions would arise, would they not, through you, Mr. President.

THE CHAIR:

Thank you, Senator. Senator Duff.

SEN. DUFF:

Thank you, Mr. President. Through you to Senator Nickerson, the issue is moot after we decided not to move the money from CHFA to DECD. Once the money stayed in CHFA, and I believe that that's what the file copy will say, is that that issue is now resolved because of the fact that we were not taking money from CHFA and moving it over to DECD.

That was the big issue is that taking the money out of the Housing Finance, the pre-omen money, and moving it over, that was where the constitutional issue came in. And we've resolved that by keeping the

money at the Housing Finance Authority, through you, Mr. President.

THE CHAIR:

Thank you, Senator. Senator Nickerson [inaudible].

SEN. NICKERSON:

Well, I appreciate those answers to those questions. I won't say I'm not persuaded, but I can't say I am persuaded. I do think there's a continuing concern, which warrants looking into, as to whether the use of proceeds, though within the CHFA organizational framework does or does not, and it may not, raise the same issues with regard to bond covenants and constitutional impairments.

And I'd certainly feel more comfortable if we had, you know, a legal opinion to that effect. I appreciate your point in that by not utilizing the DECD framework, there may be a lesser potential or no potential for a conflict.

But there may be. And I'd just like some more information on that. But I appreciate your answers, Senator Duff, and will now subside. Thank you, Mr. President.

THE CHAIR:

Thank you, Senator Nickerson. Senator Kane, do you seek the floor, Sir?

SEN. KANE:

Thank you, Mr. President. Good afternoon.

THE CHAIR:

Good afternoon.

SEN. KANE:

Mr. President, I have had concerns about this bill since the beginning, having been the Ranking Member on the Banking Committee, and especially with the monetary piece of the bill.

However, working with Senator Duff, Representative Barry, Representative Ryan, in the House, I think we've molded what seems to be and what

is a pretty good bill. This is a major issue that is facing the State of Connecticut, facing the nation, I guess.

The whole country is dealing with this. Every state, if you look, is facing this very same issue. And coming up with ways to achieve a bill that can work for the constituents, for all their states, for the banks, let me mention, as Senator Duff said, that the banks were not involved in any of these sub prime mortgage issues, all our Connecticut banks, our Connecticut credit unions.

What is also does is there's a regulatory piece that sets mortgage brokers to the same high standards that banks will be set, and I think that's a good idea. The mediation process, although not perfect, is very good because it will get people to maybe stay in their homes a bit longer and help them stay in their homes.

But I think we need to do something. Whether Democrat or Republican, I think we all feel that way. And in working with the Chairs and working with the interested parties, I think we did come up with a very good bill.

And I am happy to support this bill, and I will be voting in favor of this bill because I do think we need to do something in this particular crisis that's effecting our state and is effecting our economy. Thank you, Mr. President.

THE CHAIR:

Thank you, Senator Kane. Senator Stillman.

SEN. STILLMAN:

Thank you, Mr. President. It's a pleasure to see you on the [inaudible].

THE CHAIR:

Always good to see you, Madam.

SEN. STILLMAN:

Thank you. I rise in support of this bill as well. I was very pleased when I sat down with Senator Duff, and he outlined some of the major points of this bill. And we reviewed it somewhat closely. I do have a couple of questions, which I'll get to. I don't think anything too difficult, Senator Duff, but just for clarification.

But it's interesting that we would be taking up this bill today, when *The Day* newspaper in New London has one of their lead articles about foreclosures up more than 50% in the state and the county. So it's a very disturbing headline.

You know, for those of us who do try and stay in touch with what's going on in the world, and we listen to the pundits on Wall Street. Some of them are saying, oh, the worst of it's over. Well, I disagree. And I think many of us in this Circle and many of us who are a little closer to what is going on would disagree as well.

And, certainly, seeing a heading such as this today, in *The Day* paper, is disturbing. It shows that [inaudible] foreclosure filings in New London County were up over 54%, and that a total of 407 foreclosures were started in the past quarter, which is almost double what it was in the previous quarter.

So I believe that this bill, I hope it will, and I think it's a great start in making sure that we can try and get a handle on what's going on, provide opportunity for people so they don't have to lose their homes, move.

And we all know that there are probably some people who are in this position, and many of us think should have been a little wiser when they went down this path. But we also know that there were people who put their trust in a system that didn't work. And that's very sad that we are at this point today, and it's an indication of all the problems in the economy.

I'm very pleased with the section on making some of the housing stock available for affordable and supportive housing. If there are houses out there that are viable homes, in terms of providing a good roof over the head for someone who is in that position, I think it's a great way to reuse our housing stock.

Sadly, someone has to move out for someone else to move in. But I do have one question about the workforce portion of this bill, the Mortgage Crisis Job Training Program.

And through you, Mr. President, I'd like to ask Senator Duff how that will work, as a member of my local Workforce Investment Board. I'd like to know if the five investment boards around the state would be involved in this, or are we talking about an entirely different workforce investment program?

So I'd appreciate it, Senator Duff, if you could share with us how that will work and how that will help folks. Thank you.

THE CHAIR:

Senator Duff.

SEN. DUFF:

Thank you, Mr. President. Through you, and thank you, Senator Stillman, for your kind comments on the bill and your support. This provision, actually, was brought to us by people from The Workplace, Inc. And it allows them, with other regional workforce development boards and one-stop centers to establish mortgage crisis job training programs.

And, again, it helps people who are unemployed, underemployed, those who need re-job training. We wanted to make this throughout the entire state. It was originally brought to us as maybe just doing a pilot.

But we felt because of the fact that there are so many more foreclosures in the state as compared to a year ago, the fact that this is an essential piece, to have a job training piece in this bill was an important component of any kind of foreclosure or sub prime component that we needed to make this a statewide initiative.

So this will be done through The Workplace, Inc., in cooperation of all five workforce boards, and everybody will have an equal share of this, an equal say, through you, Mr. President.

THE CHAIR:

Senator Stillman.

SEN. STILLMAN:

Thank you, Mr. President. Through you, to Senator Duff. Could you explain to us exactly how this will work for an individual? What do they have to do? What will they have to do to access this job

training that they may need in order to create a better life for themselves and their family?

THE CHAIR:

Senator Duff.

SEN. DUFF:

Thank you, Mr. President. Well, Mr. President, specifically, a lot of that is going to get worked out with the workforce boards, and they're going to have a certain amount of leeway in how to fix that best, to their own parts of the state.

We're not legislating exactly how that has to work. However, I will say that Connecticut Housing Finance Authority is having lots of fairs around the state, and they're going to be working with the workforce boards to refer people from that way.

One of the things that we did in this bill is not to have various silos so that entities were not working together. One of the, for me, anyway, I know

for my Co-Chair as well and Senator Kane, was to make sure that everybody was working together.

So we certainly envision this where CHFA, through the CT Families, through HERO, through EMAP, will be working closely with the workforce boards and vice versa, also through the mediation process. So I see this in a number of different ways.

I know the workforce boards, and you probably know better than me, sitting on one of those boards, will certainly reach out to the community as well, work with community parties to make sure that people have the ability to access this.

And one of the issues also is that, federally, they are a federal board, and they have some federal money, and that they are only allowed to work with people at a certain income level, based on federal laws.

The reason why this is important is because of the fact that this will allow the workforce boards to

work with people who are probably our middle class, who are struggling, who are possibly under foreclosure and who need a hand up to prevent them from foreclosure.

Because, again, the most expensive thing that would happen in this entire process is foreclosure. And we have a number of different safeguards here to try and steer people away from that process, and keep them in their homes.

And I will tell you that we had some stories. Actually, after we had our initial press conference on our bill, the first go-around, before public hearing, we had a number of calls come in, throughout the state, based on people who are getting foreclosed on. And that still continues.

Since these programs have been starting to come out there, and people are learning more about it, and things are out there, and CHFA is under new leadership now, we're finding that we're able to help people, not

necessarily always based on what we're writing here in this law, but based on the fact that we're giving all these agencies and entities lots of flexibility in order to help people in the best way that we can help them, and not say that, sorry, you don't qualify for this program because of X, Y, and Z.

We want people to be part of this, and we want people to stay in their homes. We actually had a success story where somebody was actually losing their home. They contacted CHFA. They were able to get their mortgage reset.

And the person had called back and said, you know, thank you so much for helping us. Not only you kept our family together, you kept us in our home, and you kept us in the State of Connecticut. So that's, I think, if we can replicate that success story, many times over, which I think we will because of this legislation, we'll have done our job.

THE CHAIR:

Senator Stillman, you have the floor, Ma'am.

SEN. STILLMAN:

Thank you, Mr. President. Again, I would like to thank Senator Duff for his leadership and Representative Barry and all the other people who worked on what is an extremely difficult and emotional issue. And I look forward to hearing about more of those success stories. Thank you, Sir.

THE CHAIR:

Thank you, Senator Stillman. Senator Prague, you have the floor, Madam.

SEN. PRAGUE:

Thank you, Mr. President.

THE CHAIR:

You're welcome.

SEN. PRAGUE:

Mr. President, through you, I'd like to ask Senator Duff a couple of questions.

THE CHAIR:

Please proceed.

SEN. PRAGUE:

Thank you. Senator Duff, can you tell me, simply, how somebody who is facing foreclosure would use the legislation that hopefully will pass today to get some help? Do they go to a bank? Where do they get this help to pay what they need to pay in order to stay in their home?

THE CHAIR:

Senator Duff, do you care to respond, Sir?

SEN. DUFF:

Thank you. Through you, Mr. President, thank you, Senator Prague, for your question. Your question is really the basis of this bill. There are a number of different ways in which people can go and get help. One of the ways is they can, if they contact CHFA, they will then get routed to the Connecticut Housing Finance Authority.

They'll get routed to wherever they need to go, if they contact them. They can contact the Banking Commission. They can contact their state Legislature. CHFA is holding a series of fairs around the state with community groups. There are community groups that are actually going out and speaking to people.

One of the best parts about the foreclosure mediation program is that if somebody's getting a summons for foreclosure, then on top of that summons will be a notice of availability of mediation.

If they check off the box, and use the mediation, then the mediator will then have to avail the borrowers or the mortgagors of all the services that are available to them, whether it's community resources, whether it's EMAP, whether it's HERO, whether it's CT Families, whatever the issue is, there are lots of different ways in which people will have the ability.

But if somebody's going into foreclosure, part of the, oh, also the Emergency Mortgage Assistance Program that the banks are mandated to notice to their borrowers, especially if they're on the road to foreclosure, they are mandated to notice them that there is the existence of the Emergency Mortgage Assistance Program, which will then put them in contact with CHFA.

They house all three of these programs. They'll have the ability to [inaudible]. We tried to be as proactive as possible, in a number of different ways, so that people who may be facing the worst, who may want to be in denial about it, that they have, in front of them, exactly the resources they need to make the decisions for themselves.

THE CHAIR:

Senator Prague.

SEN. PRAGUE:

So, Mr. President, thank you, through you, just to Senator Duff, Senator Duff, most people out there don't know about CHFA, but they do know about the bank from which they borrowed the money to buy their home.

So you're saying that the bank will have to stay on top of these mortgages that they have given out, and if they see that somebody is not paying the mortgage payment that they're to notify these people as to how they can get help?

through you, Mr. President, Senator Duff, is that what I heard you say, that the banks are going to take on some of this responsibility to help their borrowers?

THE CHAIR:

Senator Duff.

SEN. DUFF:

Yes. Thank you, Mr. President. Through you, the answer is yes.

THE CHAIR:

Senator Prague, you have the floor, Madam.

SEN. PRAGUE:

Thank you, Mr. President. That's really a good thing because most people don't understand CHFA or mortgage lenders, but they do understand, if they have a mortgage from the bank, and the bank says to them it looks like you're facing some trouble here, this is how we can help you, that's really, that's very good. And I'm pleased to be able to support this. Thank you.

THE CHAIR:

Thank you, Senator Prague. Senator Kissel

SEN. KISSEL:

Thank you very much, Mr. President. Great to see you up at the [inaudible].

THE CHAIR:

Welcome, Sir.

SEN. KISSEL:

Well, I want to commend Senator Duff and Senator Kane and all the others in the House of Representatives and any of my colleagues here in the Senate that worked on this.

I would, at the outset, acknowledge some of the concerns raised by previous speakers, especially regarding that LOC concern regarding the constitutionality, regarding the underlying bond covenants. But, hopefully, that can all be worked out.

This is not unusual. When our nation and our state has faced certain crises in the past, we've stepped into the breach, as we should. Clearly, people have had a concern regarding the sub prime mortgage crisis for quite a while.

Above and beyond its ramifications on a local Connecticut level, it has had a devastating effect on our national economy. It has shaken people's fundamental belief in our financial institutions, and

it brought up the specter of something that's always out there, in one form or another but, really, we haven't seen, to this extend, in my recollection, since the 1980's.

I remember that wonderful movie called *Wall Street*, where there was that critical speech within the movie , where it was stated that greed is something good. Greed is something that moves our economy forward. It is greed that separates the winners and the losers.

Now I think in that movie, when that speech was made by Gordon Gecco, it was being used to juxtapose himself and his avarice versus what's good in a society.

In speaking to some of my constituents, in particular those very familiar with mortgage lending practices, what has come to my mind is that when you start peeling away the skin of this onion to try to get to that heart of how it's really affecting people

on the ground, it's not always the situation that one might assume.

When one talks about the sub prime mortgage crisis, typically, one conjures up an image of an individual that probably shouldn't be in a home and probably only has the income to be a renter or lease property or something like that.

Or if they were able to own a property that because of the effects of sub prime lending, individuals got in over their head regarding property that was valued far in excess of what they could afford.

I would suggest to my friends and colleagues here in the Senate that that is not always the case. And I'm not even sure if that's the case in the majority of instances.

Because the story that has been told to me is that very group of individuals that are out to make money as go-betweens between lenders and borrowers

that somehow interjected themselves into the marketplace, fairly unregulated, and what they did is they made offers to individuals that seemed almost too good to be true.

And at the time, in the last two, three, four, five years, with the marketplace hot as anything in real estate, continuing to shoot up, people got caught up in that sales pitch.

And so what I'm saying is that I believe probably a majority of the individuals affected at the grassroots level, by the sub prime mortgage crisis, were individuals that otherwise had strong credit and probably could have acquired a loan through traditional means, at a fixed rate, through would have put them not in jeopardy during a downturn in the economy and the real estate market.

In other words, it is a mistake to blame the borrower for this financial crisis. I firmly believe that there are other actors in the marketplace that

preyed upon unwary individuals, and took advantage of them.

That is not to say that the best buy word to utilize, when going out to purchase anything, to acquire a service, to obtain a loan, is not caveat emptor, buyer beware. It's always good to take a step back, and be cautious.

Nonetheless, given the environment that we've had, especially regarding real estate in the last five to ten years, the powers of the marketplace, the powers of the American dream, the powers of people's desire to try to get the most for their dollar, I think, lulled a huge portion of our society into accepting these loans, these mortgages that when there was a slight tipping of the scales and a downturn, or when what they didn't think was going to happen happened, the balloon came due, the variable rate shot up, all of a sudden, they were faced with owning real

estate where there was no equity in the property to speak of.

They had huge payments due, and their income did not keep up with their payment schedule. It doesn't mean they didn't have a good job. It doesn't mean they don't work hard. It doesn't mean that they can't afford to live in a home.

It means they got boxed into signing a mortgage agreement that ultimately had the deleterious effect of having them have to face foreclosure. Nothing can be worse, to my mind, other than having a physician give you a really bad assessment and say maybe you've got a disease.

I mean, there's a lot of bad things. Things can happen to your family, your children. But, I mean, your home is right up there with those. And to think that you're losing your home is a huge, huge tragedy for so many in our society.

So what I'm saying is it is perfectly reasonable for the State of Connecticut and this Legislature to step into the breach, and cobble together as much of a response as we practically can to address this issue, and not blame the borrowers and not say, oh, you should have been smarter.

And I would say look to Manhattan. Look to New York City, in particular. Look to the massive structures, the towering skyscrapers of those magnificent lenders, who ultimately benefited dramatically from these what I would consider predatory practices by the merchants on the ground that made these incredible deals, and then we don't even know where they are anymore.

Bear-Stearns comes to mind as the poster child. There are huge financial institutions that knew this was going on, bundled up all these sub prime mortgages, and then began trading them, almost like stocks and bonds.

And then when the musical chairs stopped, and all of a sudden one of these large financial institutions found out, oh, oh, we're left holding the bag, we've got the hot potato, all of a sudden, on a national level, on a federal level, the powers that be, the great financial wizards of the United States sat down, and very quickly came up with solutions.

We'll allow the utilization of tax dollars, we'll free up money from the Fed, we'll have this incredible institution buy out this other institution, and everything happened in a swirl. And at the end of the day, I'm not so sure because it happened so quickly, we got the best value for our federal tax dollars that we've allowed to enter into the marketplace to buoy up these giant financial institutions.

And the public isn't stupid. They opened up the paper and they say I'm about to lose my home. And now all of a sudden, the federal government will jump

through an incredible amount of hoops to actually take care of these gigantic financial institutions.

So what I'm saying is this. For anybody looking at this legislation, is it perfect? No. Is it a tremendous work product, cobbled together after weeks and months of hard work by Senator Duff and Senator Kane and our friends and colleagues in the House? Yes.

Is it absolutely necessary, and will it do good? Yes. Will we probably, God willing, some of us are back here next year, we will probably have to modify and fix it a little bit? Yes. But we owe it to the borrowers. We owe it to the people whose houses are on the pages of the newspaper being foreclosed.

We owe it to them to do as much as humanly possible as our federal government has seen fit to do for those gigantic financial institutions that got caught holding the bag. This is a real tragedy for so many in our society.

But to the extent that we cannot let those giant financial institutions fall, we cannot let these borrowers fall either. For that reason, Mr. President, I strongly support this legislation. Thank you.

THE CHAIR:

Will you remark further on the bill? The question is on passage in concurrence with the House of Representatives. Senator Harp has the floor.

SEN. HARP:

Thank you. I'm going to make this really quick. I just want to commend Senator Duff and Senator Kane and the Members of the House for working on this very important bill. I think that housing, a decent home, is something that is really a core, American value.

And when we have financial systems that interfere with that, and, basically, institute insecurity for people in our communities, on an issue that hereto now has been largely a federal issue, and the state has

stepped up to the plate, through this legislation, it's very important to mark that. It's very important that it's bipartisan. And, again, I commend you for your hard work.

THE CHAIR:

Thank you, Senator Harp. Senator Nickerson, for the second time.

SEN. NICKERSON:

Thank you, Mr. President. Speaking for the second time, I do not have a question for Senator Duff, but I do want to put on record that after our colloquy of a few moments ago, I did some further research, some further thinking, and I accept his answer.

And I share his believe that by retaining the funds within CHFA and by providing, as the file copy now does, as amended, that the CHFA funds shall be used in a manner consistent with CHFA covenants that I share his belief.

It is my belief that there is not an issue, as there might have been under the original file copy, with regard to bond covenants and with regard to the contracts clause in the U.S. Constitution. So I didn't want to leave his answer on the record without my opportunity to make clear that I accept his answer. Thank you, Mr. President.

THE CHAIR:

Thank you, Senator, for that clarification to the record. Senator Debicella.

SEN. DEBICELLA:

Thank you, Mr. President. Mr. President, through you, a question to the proponent of the bill for purposes of legislative intent.

THE CHAIR:

Please proceed, Sir.

SEN. DEBICELLA:

Thank you, Mr. President. In Sections 29 and 30 of the bill, the bill lists out some lending

provisions where A person who has gotten a mortgage, the lender has a responsibly to make sure that they have the ability to pay it back.

And Sections 29 and 30 detail a little bit of the recourse that that person then has, if they go bankrupt or are foreclosed on, or their house is foreclosed upon. And the question, through you, Mr. President, is my reading of this bill is those damages that a banker or bank is liable for is capped at $1,000.

And, through you, Mr. President, I just want to make sure that I'm reading that section correctly, through you.

THE CHAIR:

A question has been posed for purposes of legislative intent. Senator Duff, do you care to respond?

SEN. DUFF:

Yes. Thank you, Mr. President. Mr. President, through you, that is correct. It is $1,000. Actually, it says it established a private right of action for violations of Sections 22 through 29. It must be brought within three years of the date of closing, for the greater of actual damages of $1,000 and attorney's fees, unless, and there are a couple other provisions there.

One is within 90 days of the closing and any time before that there's a noncompliance issue, and also, secondly, is if the lender is able to show that noncompliance was unintentional, and, lastly, if the lender and borrower each reach a mutual agreement and cure to the action. So through you, Mr. President, hopefully, that answers Senator Debicella's questions.

THE CHAIR:

Thank you, Senator. Senator Debicella, you have the floor.

SEN. DEBICELLA:

Thank you, Mr. President. I would like to thank Senator Duff for his answer. Mr. President, I rise with very mixed emotions about this bill. I actually find my ideological side and my practical side in conflict. And I believe I'm going to let the practical trump the ideological today, and vote for this bill.

But my worry about this is that the provisions of this are, essentially, rewarding risky behavior. At the end of the day, the bonding that is done is going to be used to buy non-performing loans from banks, to renegotiate with new interest rates for those sub prime mortgages.

Andy my worry, Mr. President, is we are helping out banks who made loans to people who couldn't afford them. And we are bailing out individuals who bought more home than they could afford. And so from an ideological standpoint, I have a problem with that.

I wouldn't call this a bailout bill or anything like that. I don't think it's that expansive. I think Senator Duff and Senator Kane have done a very good job crafting a moderate bill. But there is still something, Mr. President, that bothers me about us using taxpayer money to fund the banks and the individuals who made poor decisions.

I also worry a little bit about the lending restrictions, which, again, are not super-onerous, but could have the effect of not allowing some people to get loans. Credit could be tightened, especially for those on the margins of whether or not they could get those loans.

But, Mr. President, all those ideological concerns, I think, are trumped by the practical side of this, which is if we could go back in time and fix this, we could or we would. But in actuality, we can't have tens of thousands of people having their homes foreclosed on throughout the state.

The practical implications of that for our families and for society as a whole, bearing the costs that would be associated with all those foreclosures, is really not an attractive alternative. So, Mr. President, I just wanted to get my concerns about this on the record.

But I will be voting for this bill today. And I want to thank, again, Senator Duff and Senator Kane for crafting a very moderate bill, which I think takes into account enough things that, for once, my practical side has trumped my ideological side. So thank you, Mr. President.

THE CHAIR:

Thank you, Senator Debicella. Senator Cappiello.

SEN. CAPPIELLO:

Thank you, Mr. President. I rise for a few questions, through you, to Senator Duff.

THE CHAIR:

Please proceed, Sir.

SEN. CAPPIELLO:

Thank you, Mr. President. Most of my questions, I think, are for legislative intent and for clarification, Senator Duff.

Through you, Mr. President, in Sections 12 and 13, when it talks about the ineligibility of the program, and I'm looking at the summary, it says that increasing the limit on the number of times a person can be more than 30 days in arrears to 4 or more times in the previous year, from 2 or more times in the previous 2 years, before the person is ineligible for the program.

When we're talking about someone being in arrears four or more times for their mortgage, there are differences in how the credit rating agencies rate lateness.

For instance, if someone is 30 days late for a mortgage or for any payment, but then they have what they call a rolling 30-day late, where they're just

one month behind, and they continue to be one month behind, after 4 months, I'm assuming would mean that even though they were simply 30 days behind constantly that that would make them ineligible for this program. Is that correct, Thank you, Mr. President?

THE CHAIR:

Senator Duff.

SEN. DUFF:

Mr. President, I'm just asking the Senator to please reframe your question.

THE CHAIR:

Senator Cappiello, would you please rephrase?

SEN. CAPPIELLO:

Thank you, Mr. President. There are differences in late payments, when it comes to either mortgages or credit cards or anything dealing with your credit history. For instance, if you're 30 days late in your mortgage, it's marked a 30-day late. You get a two on your credit report instead of a one.

If you're 60 days late, meaning you're 60 or more days behind, so 2 payments behind, you get a 3. And then there are different numbers that you get. If you're 90 days late, usually, after being 120 days late is when foreclosure proceedings might begin to occur. So that would mean being four months behind. In essence, you are late four times.

But there's a big difference between that kind of lateness and then being late once 30 days, but always being behind 30 days. So you keep getting twos on your credit report. And you're simply 30 days behind, but you haven't caught up yet.

It's much better, according to the credit agencies, to be 30 days late and continue to be 30 days late, than to have say, one time where you're 4 months late. So through you, to Senator Duff, are those two issues equivalent, or do we treat it differently, whether you have what they call a rolling 30 day late or being 4 months behind in your payments.

THE CHAIR:

Senator Duff.

SEN. DUFF:

Thank you, Mr. President. Through you, my sense is that is not specified out in the bill, and the CHFA will have to come up with, we've authorized them to, obviously, come up with procedures and regulations on EMAP, and that is something that they will have to contemplate as they move forward with this new, expanded Emergency Mortgage Assistance Program.

I will say though that from Senator Cappiello's idea, my just first brush of this would be that they would probably not be too terribly interested in helping somebody who's just merely 30 days late. They probably want somebody who is a little bit more severely behind in their mortgage payments, before they were to qualify for the Emergency Mortgage Assistance Program because, again, there's those finite resources.

But I, in any of the discussions we've had while crafting this bill, that example did not come up. So I can't quite give you an answer to that at this moment.

But with the limited funds that we have, I would imagine that we would have to use the money as sparingly as possible, and help people who truly are in need, not just somebody who may just be 30 days behind, through you, Mr. President.

THE CHAIR:

Senator Cappiello, you have the floor, Sir.

SEN. CAPPIELLO:

Thank you, Mr. President. And I would just suggest to Senator Duff and the folks that are putting these guidelines together that we might want to consider helping someone who is consistently 30 days behind because all they need is really help with one payment, frankly, to catch up.

And, again, it's not looked upon as poorly by the credit rating agencies when you're simply, consistently 30 days behind. They don't like it, but it's better than being 60 days behind, caught up, 60 days behind, caught up. There are differences in how the credit rating agencies treat those situations.

Another question, if I may, through you, to Senator Duff, if he could just explain what the difference between a sub prime loan is and this new definition of nonprime loans, through you, Mr. President.

THE CHAIR:

Senator Duff.

SEN. DUFF:

Thank you, Mr. President. Through you, in Section 21, I believe, I'm just looking for the definitions right now. We actually have two different definitions that create a, we don't call is sub prime loan. We call it a nonprime loan. And if the Senate

can just stand at ease for a second, let me just find the definitions.

THE CHAIR:

The Senate will stand at ease, Sir.

[SENATE AT EASE]

THE CHAIR:

Senator Duff.

SEN. DUFF:

Thank you, Mr. President. There are actually two different definitions of nonprime loans that we use in the bill at Section 21. And it says that the United States security note, you have to have, having comparable [inaudible] of majority is either equal to or greater than three percentage points on the first mortgage or five percentage points on the second mortgage loan.

So there's collars that we're using as definitions. And there's also an and. And it says that nonprime loans are those where the difference

between the APR for the loan and the conventional mortgage rate is either equal to or greater than 1.75 percentage points, if the loan is a first mortgage, or 3.75% if it is a second mortgage.

Additionally, we do give the Banking Commissioner some powers to raise the first collars that I mentioned, up to a half a point, and then we'll revisit that next year, during the Legislative Session.

But these are actually definitions that are used in North Carolina and have been advanced by some of the advocacy groups that have been used in other states dealing with this issue.

So we feel very confident in the fact that in defining these nonprime loans that we have been very careful to put collars around these high interest rate loans, but not to include in the prime loans as well, through you, Mr. President.

THE CHAIR:

Senator Cappiello.

SEN. CAPPIELLO:

Thank you, Mr. President. Thank you, Senator Duff. I'm glad that there is a strict definition of a nonprime loan. Because I know that when this issue began to occur over the last couple of years, the term sub prime loan has been thrown around quite a bit.

And I don't know if there was ever any one definition, or maybe I missed it, if there was a definition. But I think it's being used to blanket a number of scenarios for lenders. So I think it's important to be able to have this in statute, so we know exactly what a nonprime loan will be.

Also, Mr. President, if I may, through you, to Senator Duff, I introduced a bill this session. For any of you who don't know, my other job is being a mortgage loan officer, working for financial institutions and banks.

And we're a job that does not have to be licensed right now. And it is one of the largest financial transactions a person will ever make in their life, for most people, the largest financial transaction somebody will ever make.

And they're dealing with people who, for the most part, do not have a license. And they don't have to have any training or any background, any educational requirements. And while I think most loan officers are good people, I think that there are going to be, like in every other business, some bad apples.

So my question, through you, to Senator Duff is there is a section regarding licensing of loan officers. But can you explain, through you, Mr. President, to Senator Duff, exactly how this is going to promote the licensure of a loan officer?

THE CHAIR:

Senator Duff, do you care to respond, Sir?

SEN. DUFF:

Thank you, Mr. President. Mr. President, through you, yes, Senator Cappiello, a provision that we have been working very closely on with the Banking Commissioner here in the state is a nationwide mortgage licensing system.

And, actually, that's a very exciting system that has, obviously, through it's name, national licensing that will bring people who do mortgages kind of under one program because of the fact that, obviously, people who write loans aren't just in Connecticut. They could be across the country.

And there had not been, previously, this opportunity to have this system where if somebody from California is loaning to somebody in Connecticut, we'll have some information about them.

So this system is not up and running yet. We do believe that it will be up and soon. We actually did pass legislation last year. We've made some tweaks to

it, based on the recommendations of the Banking Commissioner.

But I do think that this nationwide mortgage licensing system will be very successful and will help consumers. And I know it's going to help the Department of Banking as well.

THE CHAIR:

Senator Cappiello, you have the floor, Sir.

SEN. CAPPIELLO:

Thank you, Mr. President. Just one more question, through you, to Senator Duff.

THE CHAIR:

Please proceed.

SEN. CAPPIELLO:

Thank you, Mr. President. In Section 23, with regards to the ability to pay section, it talks about the requirements for lenders with regards to making nonprime loans, and the criteria that they will have

to use with regards to whether they believe that a person has the ability to repay this loan.

My question, through you, I mean, it has sections dealing with current and expected income, current and expected obligations, as disclosed by the borrower, etc., homeowner's fees, condo fees, employment status and other financial resources.

My question, through you, to Senator Duff, Mr. President, is are there going to be exact ratios that are used in determining the ability for someone to repay the loan? Right now there are conforming standards for Fannie Mae, Freddie Mac, the guidelines that are used to see whether someone is going to have a conforming loan and if they're a conforming borrower.

Will there be direct and exact standards put into place with regards to someone's ability to pay so that a lender can then put all this information into place

and say, okay, we believe that the borrower will be able to pay back this loan?

THE CHAIR:

Senator Duff.

SEN. DUFF:

Thank you, Mr. President. Mr. President, in my reading of the bill, the answer would be yes.

THE CHAIR:

Senator Cappiello.

SEN. CAPPIELLO:

Thank you very much, Mr. President. Thank you, Senator Duff, for all of your answers. I would also like to state that I am very happy that Senator Duff and Senator Kane and others have worked on this very important piece of legislation.

And it was stated, it might not be a perfect bill. But I know, when dealing with such a large issue in this building, with all the different

conflicting personalities and points of view, it's very difficult to, in one term, have a perfect bill.

What I would like to say is that, you know, I've worked for a number of banks and financial institutions, one of which, last year, shut its doors. And I think there were a lot of people who were affected by them shutting their doors, including the employees that worked for this particular institution, people who didn't get their paychecks because of hiding behind bankruptcy law, people, some of them were secretaries, some of them were commissioned workers, employees.

They had lost their insurance overnight, and those are just the employees. Then, of course, there were the people who were affected, who were in the midst of getting a loan with the institution. So some of these lending institutions have had serious, serious, negative, adverse impact on our entire country and economy, including here in Connecticut.

I would like to see the Banking Committee look at tweaking this bill next year to try and make it a little bit cleaner, and fix some of the ambiguities that might appear in the bill and to make sure that no one gets caught up and no one is being played, no one is getting, you know, gotchaed because of this legislation.

I also want to make sure that we're not trying to keep people who normally could not get a mortgage from getting a mortgage. I mean, really, that is the American dream, to be able to own your own home, live in your own house, raise a family in your home.

And I don't want to see legislation passed, and I don't think that is this kind of legislation, but legislation passed that would stop someone from living the American dream, regardless of how wealthy or not so wealthy that they are.

Finally, with regards to the licensing issue, I'm glad that that provision is in here, regarding the

National Licensing Board. But I do think it would be important in the future to then have provisions in place with regard to how to pull someone's license if they are acting in a disreputable manner.

I think that we should look at continuing education requirements because, again, someone like myself or anyone else doing that job is helping someone with the single, biggest financial transaction of their lives, in most cases. And we should be able to know exactly what to tell them, in giving them advice, when it comes to getting their mortgage, so they are not being adversely affected.

But, again, Mr. President, I rise in support of this bill. I want to thank all of the members that contributed to its creation. Thank you, Mr. President.

THE CHAIR:

Will you remark further on the bill? Senator Russo, please proceed, Sir.

SEN. RUSSO:

Thank you, Mr. President. I want to rise in support of this bill. As a real estate attorney, unfortunately, I've seen too many times in the past where this has really become necessary.

I really enjoy my work because I not only get to help people make one of the largest financial investments, but I'm also, in many cases, helping them make a large emotional investment.

But too many times in the past year, I've had people come to me that have been suffering under predatory loans, and they've needed relief. Fortunately, in many cases, we've been able to help people get into safe, solid loans that they could afford. But there have been a few instances where people, there have just been no options for them.

And I think that this bill is going to help address this. I think this whole sub prime crisis reminds me a little bit of the Internet bubble that

happened about ten years back, where people were getting advice from professionals that maybe were overly optimistic, and, frankly, dangerously optimistic in their enthusiasm.

And their enthusiasm, unfortunately, led to a lot of people that gambled with their investments. And, unfortunately, this gambling has caused a lot of people to lose their homes. And so I'm hoping that this is the sort of regulation that government really needs.

We need to make sure this doesn't happen again. This crisis has cost our economy a lot of money, a fortune, frankly. But it's also cost a lot of people the core of their very families, their houses. So I'm hoping that this bill will not only help to clean up what has happened in the past, but will also help to prevent it from happening any further in the future.

I'd like to thank Senator Duff and Senator Kane for their hard work. And I look forward to supporting this bill. Thank you.

THE CHAIR:

Will you remark further on the bill? Senator Fasano.

SEN. FASANO:

Thank you, Mr. President. Mr. President, first of all, I want to thank Senator Kane and Senator Duff, and particularly Senator Duff for giving me the time yesterday to sit down to go through the bills, or through the bill, I should say. And let me ask my question, so I can better understand the bill.

Mr. President, as a result of tonight being the last day of session, I'm going to make my comments brief. And I believe that this bill makes a large step to achieve the purpose of helping those, in Section 1, that have been harmed by virtue of the sub prime.

I had some concerns about Section 1 and the HERO program. And those concerns are, if you would, real life. If someone has a first mortgage, and it's in arrears, and by the time they get around to looking for help, generally, they've already gotten into trouble and have a second mortgage or lien.

And the only way this Section 1 works is if CHFA makes a deal by buying out the mortgage and going to first position, which would require subordination of the other folks below the first mortgage.

I guess CHFA could go ahead and buy the other mortgages out as well, but my concern is it hinders the number of people you can help because by the way it's drafted, you're buying out the first, releasing the first, and substituting it with an agreement.

So anybody who has any other mortgages, even if they're, especially if they're nonconsensual mortgages, such as a mechanic's lien or a judgment

lien, you would need a subordination agreement in order for this to work.

That just gives me a little pause in that we should have a mechanism that allows either a way to get around that subordination, which we could do as a matter of law or statute or take into account that problem.

Mr. President, I also have a concern about the word borrowers must be ones who live in the property. Frequently, these folks are people who have mortgages at a high rate and maybe don't have the best credit, and, therefore, they have a co borrower.

That co borrower may not be a family member who lives on the property. It may be a family member who doesn't live on the property, maybe a friend. Under the rules or the statute, CHFA could not come in and help that individual out or that problem out because the borrower and not the people live in the property.

I understand, conceptually, why we have that. But on the other hand, I would have liked to see a mechanism that would have said as long as one borrower is in the property, CHFA can help out, or something to understand that the reason why the person was on the loan the first time wasn't that everyone believed the person was going to live there, just that the credit was poor of the person who moved in.

So once again, if you take the pool of people that can be helped by this bill, we keep reducing the numbers that we can help. Mr. President, those are the concerns that I have on the CHFA section.

And as I said, in understand that in this building, when you're trying to come up with legislation in a short session, when you're doing 100 things, and you have certain interest groups calling you pushing for this, pushing for that, you have to give and take or nothing happens.

So I don't fault the bill. I don't fault the drafters. I don't fault the sponsors. That's just the way this building works. I just hope that maybe some of the comments that I'm bringing out today, we can deal with.

And I'd love to do it in a Special Session on this issue because it's that important. But, certainly, next session, I hope we revisit some of these issues.

Mr. President, some other concerns that I have deal with the nonprime home loan. And while I understand what it means, its definition gives me some trouble because it talks about interest rates above a certain level.

The problem I have with that, Mr. President, is generally people that look for nonprime are going to have higher interest rates because their risks are higher. What do I mean?

When you buy a car, you get one rate if you have good credit, another rate if you have excellent credit, another rate if you have poor credit. So when they do these loans, there are certain interest rates.

Now what we said is that you, lender, are going to be responsible to make sure that you review all the economics, all the factors to sort of guarantee the person can make the payment. And if they can't make the payment, you're subject to a lawsuit.

And what I don't believe I've ever seen in law is this twist. If you are a lender, and it's in default, the borrower can say that you unreasonably lent me the money. You should have known that I couldn't pay for this money. That's what the lawsuit would say.

The evidence flips. And when I mean the evidence flips is, it's now up to the lender to prove, by preponderance of evidence, that he reasonably made the loan. Now sometimes we call that in law a rebuttable

presumption that it is unreasonable to lend if someone goes in default.

In this case, we don't even use that language. We just say that we're flipping the burden of proof upon the lender. I don't fully understand that. I understand what it's driving at, but what's the downside? A borrower is in default.

Taking my hat off as a Legislator, and let me put my hat on as a lawyer, a mortgage or note that goes in default because I can't afford to pay for it, this law says I have a right to sue the lender, and the lender has to prove to me that he was right in lending me the money.

It's an absurd first time I've seen this as some type of legal precedent, if you would, for this type of law. And I don't understand it. That gives me trouble. I think we need to work on it. I'll tell you why.

With the [inaudible] philosophy or no [inaudible] philosophy, it has a chilling effect upon lenders to lend the money because now a lender says if I lend the money, and I do it reasonably, even if I do it in good faith, reasonably, they think I've got all my Ts crossed and Is dotted, I'm opened up to a lawsuit.

I'm not going to lend the money. If there's that bit of doubt, if I believe there's something, the economy is great, and maybe next year the economy's not going to be as good, if there's that bit of doubt, I'm not going to lend the money.

And if I'm not going to lend the money, the people that need the money most can't get the money. So you'll say the more money you have, the more people want to lend you money. The less money you have, less people want to lend you money.

So that's the problem I have. I am going to vote in favor of this bill. I am because I think it's a

good start. In a short session, I think it's a good start.

But I want us to review this. I want us to take a look at these principles and see whether or not we can strengthen this bill. I thank you, Mr. President.

THE CHAIR:

Thank you, Senator Fasano. Will you remark further on the bill? Will you remark further? Senator McKinney. Senator Duff will have the floor first. Senator Duff.

SEN. DUFF:

Thank you, Mr. President. Real quickly, before Senator McKinney, I just wanted to clarify an answer I gave to Senator Cappiello regarding Section 23. The answer, I misunderstood his question.

And in learning a little more about what it was, and, again, from misunderstanding it, the answer was no, not yes. But I wanted to make that clarification for the record. Thank you, Mr. President.

THE CHAIR:

Thank you for the clarification, Senator. Senator McKinney, you have the floor, Sir.

SEN. MCKINNEY:

Thank you, Mr. President. I rise in support of the legislation before us. Mr. President, as is often the case, we are here on the last day of session, in many ways, dealing with one of the most important issues facing the people of the State of Connecticut.

Given our time constraints, I will keep my remarks very brief. I want to first thank Senator Duff and Senator Kane for their hard work on behalf of this Circle on this bill, and just especially note that Senator Kane, who is no longer our rookie, but still new to the Circle, when assigned to the Banks Committee, I think, had no idea that as the Ranking Member of the Banks Committee would get to work with a fine gentleman and bipartisan Legislator like Senator

Duff, but also on an issue that is extremely critical to the people of the State of Connecticut.

In many ways, part of the American dream is home ownership. And for so many people in the State of Connecticut, especially many in our inner cities, that dream is turning into a nightmare.

And while I understand the philosophical objections and the legitimate questions that people who have played by the rules, followed the rules, struggled, cut, scrimped, and saved to make their mortgage payments in tough times.

The bottom line is that we, as a state, would be worse off, both financially and in every other way possible, if we are to allow this problem to cause hundreds, if not thousand of people to lose their homes.

And at some point, that bill will come due. And I believe this legislation, on balance, addresses that

important issue. While it does cost money, it will cost us less than if we don't deal with the problem.

And I just wanted to get those thoughts out on the record. It is, on balance, a good bill. It is an unbelievably important issue for so many people out there.

Mortgage foreclosures, home foreclosures are at, I believe, an all-time high in the State of Connecticut, and that is something that should concern all of us. So I appreciate the time, Mr. President, and thank you.

THE CHAIR:

Thank you, Senator McKinney. Will you remark further? Will you remark further on the bill? Senator Duff.

SEN. DUFF:

If there's, oh, yeah. Let's have a roll call vote.

THE CHAIR:

A roll call will be ordered. Mr. Clerk, would you please call the roll.

THE CLERK:

An immediate roll call has been ordered in the Senate. Will all Senators please return to the Chamber.

An immediate roll call has been ordered in the Senate. Will all Senators please return to the Chamber.

THE CHAIR:

The question is on passage of the bill and concurrence of the House. The machine will be open. Have all the Members voted? Senator Handley is coming in. Take your time, Senator. Seeing all the Members have voted, the machine will be closed. Mr. Clerk, please announce the tally.

THE CLERK:

Motion is on passage of House Bill 5577, in concurrence with the action of the House.

Total number voting, 36; necessary for passage, 19. Those voting "yea", 36; those voting "nay", 0. Those absent and not voting, 0.

THE CHAIR:

The bill is passed in concurrence. Senator McDonald.

SEN. MCDONALD:

Thank you, Mr. President. Mr. President, for a change of marking.

THE CHAIR:

Please proceed, Sir.

SEN. MCDONALD:

Mr. President, on Calendar Page 14, Calendar 186, Senate Bill 590, An Act Concerning Renewable Energy, that that might be marked Go.

THE CHAIR:

[inaudible] Mr. Clerk, would you please call the item?

THE CLERK:

H-1030

CONNECTICUT
GEN. ASSEMBLY
HOUSE

PROCEEDINGS
2008

VOL. 51
PART 17
5418-5742

Questions on acceptance and passage. Would you explain the bill please, Sir.

REP. BARRY: (12th)

Mr. Speaker, the Clerk has an Amendment, LCO Number 5938. I would ask the Clerk to please call the amendment and that I be granted leave by the chairman to summarize.

DEPUTY SPEAKER GODFREY:

The Clerk is in possession of LCO Number 5938, which shall be designated House Amendment Schedule "A". Will the Clerk please call.

CLERK:

LCO Number 5938, House Amendment Schedule "A", offered by Representative Barry, Senator Duff, Representative Cafero, Ryan, Senator Kane.

DEPUTY SPEAKER GODFREY:

The gentleman has asked leave of the Chamber to summarize. Is there objection? Hearing none please proceed, Representative Barry.

REP. BARRY: (12th)

Thank you very much, Mr. Speaker. House Bill Number 5577 will bring about a new era in mortgage

lending within the State of Connecticut. The bill creates a safer, more defined and regulated lending environment.

It offers more protection from consumers entering non-prime loans. It gives the Banking Department the regulatory tools needed to properly supervise mortgage lenders and it allows homeowners in the foreclosure process an equitable and fair chance to redeem their home.

A major step forward will be taken when we allow the banking department to become part of the nationwide mortgage licensing system that will keep online records of every lender in Connecticut and their record, including their criminal history.

The issue of sub-prime lending and how it has affected Connecticut is a daily topic for the media. There are economic problems today that we want to do our best to avoid causing socioeconomic problems.

It is unfortunate that our state has an extraordinary number of foreclosures and thousands of sub-prime mortgages in default with more coming just around the corner.

The number of foreclosures is on the rise here in Connecticut. In January 2006, there were almost 900 foreclosures in our courts. A year later there were over 1,100 foreclosures in our courts and in February of this year there were 2,129 foreclosures.

As for sub-prime loans, only 11% of all loans outstanding in the State of Connecticut are sub-prime loans, yet sadly enough, sub-prime loans represent sixty percent of all delinquent loans in this state. We can sit by and do nothing.

We can sit and watch people going through the foreclosure process, broke, ending up homeless, homes being boarded up or we can give them a hand up, preserve a home where kids can grow up under normal circumstances.

Today we have an opportunity to help resolve a problem, to prevent further economic consequences from gripping our larger cities, Bridgeport, New Haven, Hartford, and every town hammered across this great state.

The mortgage relief programs contained in this bill, HERO and EMAP, complement the Governor's

Connecticut Families Program and does even more to help distressed homeowners stay in their homes.

These programs are not giveaway programs. They are a way to address a pattern of lending that victimize our citizens and unless corrected would lead to decay in our neighborhoods, broken families and further decline in the value of homes across Connecticut.

Some of you will ask why we should provide assistance to troubled borrowers that may have made a financial decision that was either wrong or that they did not understand. When an economic problem involves the homeownership of so many, it strikes at the heart of our economy, our family and our neighborhoods.

The people of Connecticut have made thousands of calls for help to the Connecticut Housing Finance Authority, to the Connecticut Department of Banking and to all of us legislators.

Some have been helped by the Connecticut Families Program but many have not because of past due payments, prepayment penalties, or a lost equity. These people will be able to get assistance from the

Emergency Mortgage Assistance Program and then get a mortgage from the Connecticut Families Program, or HERO.

Money will not be given away. It will be secured by the property. A critical component of this bill is the establishment of a foreclosure mediation program. Each judicial district will have trained mediators employed by the judicial branch and trained to help borrowers who are in the foreclosure process.

The mediators will be in a unique position to bring both the borrower and a lender together to work together for their own best interests.

No amount of marketing is going to get a borrower who has missed mortgage payments and who is worried about losing their home to reach out to the lender to discuss their options. The mediation program will serve the purpose of identifying people who can be helped and directing them to the right resources to keep them in their home.

While putting together this ambitious bill, we have been very careful not to do things that might

have unintended consequences and have a chilling effect on responsible lending.

We want to protect consumers' rights and keep families in their homes without freezing up credit. I believe this bill will help many, many people and we will have carried out our public trust if we pass it into law and I urge my colleagues to support this measure. Thank you very much.

DEPUTY SPEAKER GODFREY:

Question's on adoption of House Amendment Schedule "A". The distinguished Ranking Member of the Banks Committee, Representative John Ryan.

REP. RYAN: (141st)

Good Evening, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Good evening, Sir.

REP. RYAN: (141st)

And by the way, I just want to commend you in advance. I think we always have Representative Fritz in the Chair when we do exciting, dynamic, interesting banking bills but I have confidence in you, Mr.

Speaker. I just wanted to let you know that right at the beginning.

DEPUTY SPEAKER GODFREY:

Okay.

REP. RYAN: (141st)

Through you, Mr. Speaker. A question or two to the proponent.

DEPUTY SPEAKER GODFREY:

Go ahead, Representative.

DEPUTY SPEAKER GODFREY:

And to the distinguished Chair of the Banking Committee, who I probably should admit that I have spent far, far, far, far, far too much time with in the last few weeks, along with Senator Duff and Senator Kane and a whole bunch of other people, and I appreciate the means by which we've gotten this done. We didn't throw any food and we didn't have any screaming matches, even though it took hours, but a number of questions.

First being, through you, Mr. Speaker, to the distinguished Chair, we had a lot of fun between the two of us, Representative Barry, explaining the moving

parts of this bill and would I be correct that the three major moving parts of this legislation are, in no particular order, one, the regulatory part that the Commissioner of Banking likes to call his, two, the money part, meaning the programs for EMAP and HERO and then three, the part that we've loosely called the foreclosure or the mediation part.

Would that be a good way of summarizing our three big chunks here? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker, yes. Great answer, we're going to do fine. Thank you.

DEPUTY SPEAKER GODFREY:

I just know I'm going to get confused between the Ryan and Ryan, but Representative Ryan.

REP. RYAN: (141st)

That's why we do so well with Representative Fritz. I couldn't pass that up, through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

As long as it's not Sawyer, Sawyer, which completely tongue-ties me. Okay, go.

REP. RYAN: (141st)

Through you, Mr. Speaker. If we could talk about the first part, which is namely the regulatory part. It's not the first part in the bill.

Would I be correct that if we're trying to do what in the days when Representative Cafero took a trip to the back country with his family and they gave you a thing from the AAA called a Trip Tick, which would I be correct that the regulatory piece is Sections 21 through 32. Is that probably where we're talking about?

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. Representative Ryan, it is Sections 21 through, well, 30, and then begins the National Mortgage Licensing provisions that carry out the balance of the bill, with the exception of a few sections at the end of the bill.

DEPUTY SPEAKER GODFREY:

Representative Ryan.

REP. RYAN: (141st)

Thank you, Sir, and I thank the gentleman for his answer. Through you, Mr. Speaker. Would I be correct then that the regulatory part is basically intended, and I hope you'll expand upon this, to address the issues that you made initially in your comments about defining what a sub-prime loan is and why we need these particular provisions. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. Yes, a sub-prime loan has never really been, it hasn't been defined in Connecticut law in statute or in common law.

Banking regulators consider it generally to be a loan that is given to someone with a FICO score of lower than 660 and someone who has two or more 30-day delinquent payments in the past year, have been foreclosed upon in the last two years, have had a bankruptcy in the last five years, have a debt to

income ratio of over fifty percent and have a limited ability to cover living expenses.

There are probably a number of ways you can define what a sub-prime mortgage is. What we did in this bill after hearing a lot of testimony from the effected interest is after hearing from our Commissioner of the Department of the Banking, Howard Pitkin, we defined a non-prime loan in the same spirit as how it was defined in North Carolina's Bill dealing with this same matter.

We have called a sub-prime loan a non-prime loan really. Right now currently in our statutes we have prime loans and we have high cost loans and we just created a third category of loans called a non-prime loan.

REP. RYAN: (141st)

I thank the gentleman for his answer and through you, Mr. Speaker, and I should caution everyone, although I know this is an extremely exciting topic, I know it's the sort of thing that keeps Representative Stripp awake at night, but we're not going to go line by line.

But am I correct, starting at Line 721 with that Section 20 and probably through the next hundreds and hundreds of lines until we got to Section 30, am I correct through you to the distinguished Chairman of the Banks Committee that the idea is we're saying what this sort of bad loan is and how it can be defined and what ways the Commissioner can deal with these types of loan in the future. Is that a good overgeneralization? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry, is that a good overgeneralization?

REP. BARRY: (12th)

Through you, Mr. Speaker. That is a fair characterization of what a non-prime loan is and what those sections from section 20 and on are intended to do.

DEPUTY SPEAKER GODFREY:

Representative Ryan.

REP. RYAN: (141st)

Thank you, Sir, and through you, Mr. Speaker. So if I'm somebody who for purposes of legislative intent

is trying to read this exciting stuff and I start at Line 725 and go through several pages of definitions, I should be able to figure out what sort of loans are good and what sorts of loans are not favored by the banking policy of the State of Connecticut. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. That is correct.

DEPUTY SPEAKER GODFREY:

Representative Ryan.

REP. RYAN: (141st)

I thank the gentleman for the answer and also through you, Mr. Speaker. Someone might be concerned that we might be regulating ourselves to death here.

So for instance, if we in this legislation and specifically directing your attention to, and I'll find it in a second, but is there an exemption in here for our own Connecticut Housing Financing Authority? We're not intending them to comply with these

definitions in making loans themselves, are we? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. There is an exemption for where loans are not CHFA loans, correct.

REP. RYAN: (141st)

I would probably be right if I'm around Line 773, does that sound like it's correct to you? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. You are exactly right.

REP. RYAN: (141st)

And just to take us through the next section very briefly, which is Section 22 at Line 852. Is our policy intention here that because we heard a great deal of testimony at the public hearing about bad things that lenders, and specifically mortgage brokers, did we came up with the Statement of

Practices that we don't think lenders and mortgage brokers should do. Is that the idea of Section 22? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. That is the idea, correct.

DEPUTY SPEAKER GODFREY:

Representative Ryan.

REP. RYAN: (141st)

Thank you. Through you, Mr. Speaker. On to Section 23. We also had concerns on a policy basis in the past about someone going in to apply for a loan and perhaps thinking that the person they are giving the information to is on their side, to use a bad, non-legal term, and is going to be taking information and processing a loan for them.

Do we make a policy effort starting at Lines 873 to address the sorts of things that these people should do in processing and making these loans?

Through you, Mr. Speaker. That was a long sentence, I apologize.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. I can answer that compound question without objection. Yes, we do. We indicate that lenders can't make non-prime loans unless it reasonably believes that, unless the lender reasonably believes that the borrower will be able to repay. This provision does not apply to FHA loans who have their own strict guidelines.

They have to take into consideration the ability to make payments to repay the loan and also to pay escrow items including real estate taxes and insurance premiums. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Ryan.

REP. RYAN: (141st)

I thank the distinguished Chair of the Banks Committee for that answer, and we haven't just focused

on those people who you see when you're trying to make a loan.

We've also made an extensive effort to talk about the responsibilities of mortgage brokers and would I be right, through you, Mr. Speaker, that if I'm looking at Section 29, Line 1025, is that what that section is about?

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Section 29 deals with mortgage broker duties. We had a long discussion about this in establishing a reasonable care standard for mortgage brokers for all mortgages, to make sure that the mortgage brokers act with reasonable care, skill and diligence and good faith that they are dealing with borrowers, mortgagors and that they take reasonable good faith efforts to secure a mortgage for that person that is in the reasonable best interest of that person, that they ensure that the cost of credit is reasonably appropriate considering the borrower's level of creditworthiness and other underwriting concerns.

If more than one mortgage is to be made by different lenders, the mortgage broker would have to notify the other lenders of the payment obligations before the closing.

DEPUTY SPEAKER GODFREY:

Representative Ryan.

REP. RYAN: (141st)

Thank you, and through you, Mr. Speaker. I know someone will interpret this as a shameless effort on our parts to pat ourselves on the back but have these sort of duties ever been defined in the statutes previous to this legislation for mortgage brokers and mortgage lenders? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. No, they have never been statutorily set forth.

DEPUTY SPEAKER GODFREY:

Representative Ryan.

REP. RYAN: (141st)

Thank you, and through you, Mr. Speaker. So would I be correct in saying that someone who has concerns about the bad things that we're saying make up the sub-prime crisis situation of people getting induced or otherwise involved in these loans, we have set forth in extensive language some of the duties and some of the responsibilities of people that are involved in these. Is that a fair characterization? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. It is fair.

DEPUTY SPEAKER GODFREY:

Representative Ryan.

REP. RYAN: (141st)

Thank you. Through you, Mr. Speaker. Representative Barry and I could probably keep folks here for an hour going through the regulatory section line by line which would be very useful for folks watching on TV who have trouble achieving somnolence late in the evening but I'm just thinking that it

might be a good idea for me to ask the distinguished Chair at the time we have these many days of negotiations, was the distinguished Banking Commissioner usually with us? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. The answer to that question is yes, he was usually with us either in the room or by phone or he always had an opportunity to put input into this bill and was critical, his years of experience in the Department of Banking, I think over 30 years, and his expertise in regulatory banking law came to bear in putting together this bill. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Ryan.

REP. RYAN: (141st)

Thank the gentleman for his answer, and through you, Mr. Speaker. While it is not our practice on the floor to vouch for legislation because a state

employee likes it or doesn't like it, would it be fair for me to say that the Commissioner vetted extensively every possible topic that related to his potential abilities to regulate these types of loans in the future? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. It is my belief that he did have that opportunity to do that.

REP. RYAN: (141st)

Thank the gentleman for his answers. Let me move on to a different topic here and I've just realized I'm proceeding backwards but if I direct your attention to Sections 15 to 20 of the proposed legislation, one of the big topics I refer to is the quote foreclosure mediation process.

Could I ask the distinguished Chair of the Banks Committee, through you, Mr. Speaker. Could you in a sentence or two summarize what we were trying to get at with that section of several hundred lines about

the foreclosure mediation process. Through Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. What we're trying to get at is to make sure that you know we can have all the regulatory provisions in place to make sure that the Commissioner has the requisite powers and duties to revoke licenses and exact penalties on mortgage brokers and lenders and then we can give or have available mortgage relief programs for consumers, homeowners, borrowers, but the mediation piece is critical to this piece of legislation because it allows, the purpose of it is to allow the person who has had a foreclosure commenced on them to be able to go to a place where they can have issues identified regarding their worthiness for help from the government or private sources.

We could have all the marketing in the world. I think the Governor's Task Force back in November recommended as one of its, maybe its first

recommendation, was to have a grand marketing event to market the fact that borrowers and lenders should work together to try to modify loans to try to keep people in their homes.

But I think this is the best way to put people who are in foreclosure, who have been given foreclosure notices. They oftentimes don't respond to their mail. They have a pride issue, maybe sometimes their dignity doesn't allow them to respond to a complaint in the mail and the clock's ticking.

Now they go to court. The judge has them go to a mediation session or two perhaps they are able to avail themselves of something that could help them stay in their home.

So that was the purpose of this mediation piece, to provide a conduit between the borrower and his or her problems, vis-à-vis foreclosure, and the money that may be available to them through the three programs set forth in this bill.

REP. RYAN: (141st)

I thank the gentleman for his answer, and we'll get to the financing programs in just a second but

just so there's no confusion, through you, Mr. Speaker.

So starting at Section 15, Line 572, we set up some definitions for who a mortgagor or what the property of the mortgagee is and then specifically referring to Section 16, Line 591. We're setting up a new procedure.

You get a foreclosure writ summons and complaint and if I'm correct through you, Mr. Speaker there's a notice that has to be given so that the person who is getting foreclosed now knows there's a mediation procedure, knows what it is and knows what to do about it. Is that roughly what that new Section 16 is about?

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Yes, that is true. The notice is to be attached to the front of the foreclosure complaint along with a form, a foreclosure mediation request form. That is what that section is about.

REP. RYAN: (141st)

I thank the gentleman, through you, Mr. Speaker and just very briefly so the procedures then are spelled out, if anyone is interested in Section 16 and 17 it sets up a new mediation program.

We explain how you do it, we explain what the timing is and this is a new procedure that heretofore was not available under the statutes. Through you, Mr. Speaker. Am I correct?

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. That is correct.

DEPUTY SPEAKER GODFREY:

Representative Ryan.

REP. RYAN: (141st)

I thank the gentleman. And lastly, if I just could and I proceeded from back to front. I apologize for anyone who started out flipping through with section 1, but the perhaps major part of the legislation is to set up some funding vehicles for two different programs.

One is HERO, one is EMAP, and am I correct, EMAP, meaning the Emergency Mortgage Assistance Program very quickly is something akin to the program we had in legislation back in the early '90s.

It is designed to help people that are in trouble, that have financial needs or wants now and may be slipping into foreclosure and we then define the means by which they could apply, how they qualify, what the underwriting requirements as a banker would say for what the financing is and how we secure the money that would be loaned and administered through CHFA. Is that a fair summary of what the Emergency Mortgage Assistance Program is? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker, that is a fair summary.

REP. RYAN: (141st)

Just one or two more and I thank the gentleman for his indulgence. We also have a different program and it's called HERO, and am I correct that the idea

of that is that there are some situations where we can't just bail somebody out.

It might be a wise policy decision for CHFA to go buy the loan from the foreclosing party, the bank or whoever holds the paper or it might also be in CHFA's viewpoint a good policy to buy foreclosed properties.

And do Sections 3 and Section 4 and the following sections set up procedures for doing that? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (141st)

Section 3 in the LCO that I'm looking at, LCO Number 5938, deals with the raising the cap on CHFA's uninsured mortgages from $1 billion to $1.5 billion. That section really just allows CHFA to have a greater ability to loan money.

It won't have any detrimental impact on its AAA rating but because these are mortgages that are uninsured, there's no private mortgage insurance on these, that's what that section deals with.

Section 4 deals with a study that would be in concert with federal programs, CDBG monies, FHA monies to try to find a way, the CHFA to try to find a way to buy foreclosed properties, as you were talking about.

The HERO program is a little different. The HERO program is set forth to address situations where people have mortgages that are higher than the appraised values of their homes, which is a big issue in all of our communities and it allows the government to buy loans directly from a lender and then restructure the mortgage to a fixed rate, 30 year fixed rate, in an affordable way for the borrower. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Ryan.

REP. RYAN: (141st)

I thank the gentleman for his answers, and I think obviously we've been moving several hundred lines every few minutes here and others may have questions about the details of the EMAP or the HERO programs but directing your attention to just one last topic.

To the distinguished Chair of the Banks Committee, could we briefly explain where this money comes from. If I heard the gentleman correctly, we have roughly $70 million in one thing and $70 million in something else and I know someone will get confused.

It's the same $70 million. Through you, Mr. Speaker, could you just explain for the two different components where that money is coming from. Thank you, through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Set forth in this statute are three programs. CT Families which is the Governor's current refinancing program. There's $40 million in the bill for that. It's already on the books at CHFA.

It's money that they've had in the books for twenty or so years there and they have an additional $30 million of similarly situated money that they are also lending to the cause.

The HERO program is going to be funded by $30 million. Let me just backtrack here. We're obligated to fiscal note. It might be easier to go back to the fiscal note, $40 million from CHFA for the Connecticut Families Program, $30 million from CHFA to the HERO program and then there is a debt service.

CHFA's going to be raising tax-exempt bonds to the tune of $50 million to contribute to the EMAP program and there is a debt service of over $2 million and that will be paid for by a transfer or by the State Banking Fund and then there's going to be $14 million transferred to CHFA from the Banking Funds to implement EMAP.

And then there's going to be $2.5 million from the Banking Fund to the Department of Labor to implement the Mortgage Crisis Job Training Program, established by the WorkPlace Inc. and the other WorkPlace development boards that we haven't discussed yet tonight.

Then there's a $2 million mediation program. It's about $1.7 million plus fringe benefits equal to

about $2 million that is going to come from the State Banking Fund.

What I would say is that it is to help us make sure that we can do a responsible piece of legislation in a regulatory sense, but also in a fiscal sense, the Department of Banking has been very generous with the monies that they have in their State Banking Fund which comes into the Fund from fees and license fees, they come from bank examination fees and costs and they have a balance in there that exceeds the $21 million that they have generously put into these programs.

REP. RYAN: (141st)

I thank the gentleman for that detailed explanation, and just let me ask a summary question on the financing through you, Mr. Speaker.

So if I heard the gentleman correctly, one program is going to have $70 million roughly, it's going to be $40 million from CHFA's Connecticut Families Program and another $30 that conveniently happens to be on hand unused from CHFA and that adds up to $70.

Then we're going to take $21 from the Banking Fund, that nice little pot of gold that the Commissioner has for the Banks Department and $50 million in new bonding money from CHFA and that adds up to roughly $71 million so $70 and $71 if I were to oversimplify the fiscal note is roughly the numbers that we're talking about. Is that a good, accurate overgeneralization? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

As an overgeneralization it's a good one but it's not entirely accurate because there are three programs so the $40 million you're talking about is just for CT Families and the additional $30 million to make $70 million is just not a fair characterization of it but the $30 million would be for the HERO and then the $50 plus $21 million would go to EMAP and the other expenditures that are needed in this bill, if that makes any sense to you, Representative Ryan.

I understand your question, but for clarification purposes, I'm just detailing that answer a little bit more.

REP. RYAN: (141st)

Just one last through you, Mr. Speaker. The difference is that we've got funds for the two programs but there's also administrative costs and therefore some monies moved around for the administrative costs of the mediation and the other programs. That basically is what we're talking about. Thank you. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. That is true. That is accurate.

DEPUTY SPEAKER GODFREY:

Representative Ryan.

REP. RYAN: (141st)

Thank you, Mr. Speaker. I thank the distinguished Chairman of the Banks Committee. Maybe

there will be another question or two. It's an easy 3,100 lines and I appreciate the gentleman's answers.

DEPUTY SPEAKER GODFREY:

Thank you, Sir. To rebut Representative Ryan's use of his name, the gentleman from Weston, Representative Stripp.

REP. STRIPP: (135th)

Thank you, Mr. Speaker. Mr. Speaker, I had a chance to look at this about half an hour ago so I have several dozen questions but I'll try to cut it down in the interest of brevity and hit a few that jump out at me.

One of the things is the Banking Fund that was talked about and I've heard $30 million and I've heard $21 million. Through you, Mr. Speaker. Where does that money come from again and what is it normally used for? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry to the proponent.

REP. BARRY: (12th)

Through you, Mr. Speaker, to Representative Stripp. That money, the Banking Fund, is $21 million.

That's what the number is. I apologize for any misstatements before.

The money comes from the industry, Representative Stripp. It comes from the industry, it comes from settlements that the Banking Department may have had. It comes from licensing fees. It comes from banking examination fees and so forth. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Stripp.

REP. STRIPP: (135th)

Through you, Mr. Speaker. It's my understanding and I may be incorrect in this, but that Fund is also used for expenses that would be incurred if, in fact, the Banking Commissioner has to shut banks down, which does happen during a bad economic period of time.

And through you, Mr. Speaker, to the proponent, where would the additional money come from at that point in time?

Would the Banking Commissioner have to go back to the industry, which would obviously be during a very stressed period of time and hit them for additional

fees to pay for what might be an unfortunate expense of closing several banks as we had to do back in the late '80s and early '90s. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. It is true that the Commissioner has the discretion to use these monies in that way and I think I'd be overstepping my bounds I think in getting into the Commissioner's regulatory role in answering that question in any more detail. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Stripp.

REP. STRIPP: (135th)

I thank the gentleman for that answer. I have a few questions in terms of the regulation. I haven't done a residential mortgage in probably twenty years.

I'm a little rusty but I have concerns and through you to the proponent, Mr. Speaker, are there any regulations proposed here that would affect any other type of banking, such as commercial mortgages

and commercial transactions? Transactions that are not residential mortgages and one to four family houses. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. No, we were very careful to draft this bill to avoid that.

DEPUTY SPEAKER GODFREY:

Representative Stripp.

REP. STRIPP: (135th)

Thank the gentleman for that answer. Mr. Speaker, I have a couple of questions about what is a, I guess we're calling it non-prime loan. How are we defining that?

I think it was the southern state, North Carolina, South Carolina, I've forgotten now, how are we actually determining? What are the trigger indicators that we have a non-prime loan? Is it that the payments aren't being made, but of course we can't tell that when the loan is made so there must be some other triggers such as rate or spreads or indexes.

Is there any enlightenment that the proponent could give me on that regard? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. Yes, we have established what are called collars in the industry that you would be very well familiar with, Representative Stripp, I know. They are thresholds above which a mortgage is a quote, unquote a non-prime loan.

Under the definition that we have here to establish a non-prime loan the APR of the mortgage is equal or greater to three points higher than the relevant treasury, U.S. Treasury Securities rate for first mortgages and five points higher than the relevant t-bill rate for second mortgages.

There's a second a test. The APR of the mortgage is equal or greater to 1.75 points above the conventional mortgage rate for first mortgages and

3.75 points above the conventional mortgage rate for second mortgages. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Stripp.

REP. STRIPP: (135th)

I thank the gentleman for that answer, Mr. Speaker. Further in these regulations are there going to be any restrictions on commitment fees, points, prepayment penalty or the sorts of things that might or might not be part of a standard loan? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Yes, there are. If you looked at section 26 there's non-prime loans cannot contain, except in the instance where there's an FHA loan, cannot contain a prepayment penalty.

Also the interest rate cannot increase after a default except when a default results from failing to maintain an automatic electronic payment feature that

resulted in a rate reduction and the increase is more than the reduction.

As far as that's concerned with respect to there's other kinds of duties that are placed on the broker in this bill, but I think to directly answer your question that should suffice.

DEPUTY SPEAKER GODFREY:

Representative Stripp.

REP. STRIPP: (135th)

Thank you, Mr. Speaker. I thank the gentleman through you for that answer. Mr. Speaker I have a few questions about the actual programs, the HERO program. Let's look at that.

It's my understanding that they are purchased from the lender, somebody that has the mortgage now that's already loaned the money out and through you, Mr. Speaker, my question is would CHFA try to negotiate these or would they make the lender whole by giving them 100% of the dollars that they have loaned out, including perhaps other expenses like legal fees, etc., past due interest.

How would they determine how much the lender would be paid and would the lender made whole in that regard. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

The CHFA, this HERO program, would be doing its best to buy a loan at a discount and we have had conversations with CHFA. They are under new leadership over there.

They have a new executive director and buy them at a discount and then restructure them, make an attempt to restructure them to the satisfaction of both the lender and the borrower so that, you know, when you asked about costs and attorneys fees, I think that's all part of the negotiation process in a private setting.

Whatever makes sense in a private market between CHFA and the lender to consummate a deal and we'd leave it up to CHFA in their infinite wisdom to consummate that transaction. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Stripp.

REP. STRIPP: (135th)

I thank the gentleman for his answer. Mr. Speaker, I have a question of who in CHFA might be doing the negotiating.

Would anyone there or is it going to be a series of clerks doing this or just the head of CHFA or who has the ultimate responsibility of saying that's the best deal we can make and that's what we're going to strike the deal at and go forward. Through you, Mr. Speaker, to the proponent.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker, to Representative Stripp. Very good question. The people who will be doing the negotiations as far as I'm concerned, as far as I know and for legislative history purposes I don't think the names of the people are relevant but the positions.

People who, obviously the Executive Director can have oversight over the people underneath him or her at any given time but I believe there's a Director of Residential Lending who is terrific who has testified before a Committee a couple of times.

She is, I've spoken to her about the negotiations that she's had over the last several months since, I believe since May or December, I mean November or December.

Under her leadership she has modified over 1,100 loans and that's not dealing with the $50 million CT Families Program that was launched by the Governor December 10th I think it was but this is CHFA working with XYZ mortgage company and negotiating a deal and so I think the people over at CHFA, the leadership over there, have been there for quite some time.

They've run that operation, that quasi-governmental agency very well and that is made evident by their AAA bond rating and so I think that we're leaving it in very capable hands by leaving the discretion to those particular individuals to make the

right calls on these mortgages. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Stripp.

REP. STRIPP: (135th)

Thank you, Mr. Speaker. Mr. Speaker, through you. Are some of these loans no doubt going to be under water or defined in another way the loans will be more than the property's going to be valued at when CHFA picks the loans up and puts it in their portfolio? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker, to Representative Stripp. It is not my understanding that they would be buying loans that are under water. The whole purpose of this is to buy loans that make sense, to take reasonable risks and to make sure that credit is available to people that are creditworthy with respect to this particular program. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Stripp.

REP. STRIPP: (135th)

Mr. Speaker, I think I could go on for an hour or two more but I'd even bore myself with that point so I won't. But Mr. Speaker, I'm most likely going to vote for this bill but it makes me very nervous.

I think the answers I've received and what I know from the industry that we may be risking the credit rating of CHFA over a period of time. The bond rating that CHFA uses to borrow money to give to ordinary people that are looking for loans is, in fact might be, more expensive than it has been in the past if, in fact, they take on too many under water loans.

Although the proponent said they wouldn't but I think in these conditions they may find as property values go down, if they're going to help people they are going to have to so that's of great concern to me. The current rating of CHFA.

Additionally some of the regulations, which I don't fully understand yet, but if we make them too onerous there are people outside of the state that are putting money into mortgages into this state and, in

fact, if we make them too onerous this money will not flow in and we might just lock up the residential mortgage market in our state, which would be devastating to the value of real estate and might create exactly the thing we're trying to avoid.

So I leave that to the good knowledge of the Commissioner to try to steer through those reefs and shoals as we go forward.

Mr. Speaker, having said that and having looked at the fact that we're going to have what might be moderate risk or maybe serious risk and there are pitfalls here, we can't just pass this and walk away from it.

Everybody involved is going to have to carefully manage it as we move forward. But we have to do something and for that reason, Mr. Speaker, I will vote for it and with a certain amount of trepidation press the green button when the time comes.

Thank you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Thank you, Sir. For the second time, Representative Ryan.

REP. RYAN: (141st)

Thank you, Mr. Speaker, and I apologize. I've only got several gazillion pages of notes here. I had something I intended to ask and I whiffed when I was going from back to front. Just to put it in context, Mr. Speaker, it's one of those things that we refer to as a legislative intent question.

You know, there's courts and lawyers spend money on these things, God forbid, so if I might through you one last question to the distinguished Chair of the Banks Committee, Representative Barry.

I forgot in going through the regulatory piece you explained in your summarization of the bill that one of the things that we were also doing was melding this with last year's legislation about the mortgage licensing system and that one of the things we're doing, if you looked at this and saw pages and pages and pages of quote conforming language, there's a Section 41 starting at Line 1610 and if I could Mr. Speaker, through you to Representative Barry.

It's a section about exemptions because obviously this is a complex legislation and these entities are

highly regulated and from time to time there is concern about their various powers and what regulations are applicable to who, so directing your attention to Line 1614 it says a few lines above that the following are exempt from licensing under these assorted sections.

And it goes on to say, with your indulgence, Mr. Speaker, Line 1614, any bank, out-of-state bank, etc. etc. etc. and lists a few, are not exempt from licensure.

My comment is, English majors abhor this sort of thing, double negatives, but does this language mean that these operating subsidiaries of national banks and federal savings banks are exempt from this section, if you understand the question. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker, to Representative Ryan. Yes, clearly the intent of this legislation is that operating subsidiaries of all federal banks are exempt

from those licensing sections and the language which originally needed to be included in this bill to reflect the recent court decision in Waters v. Burke, I believe it was, that decided that certain federal banks' subsidiary employees such as mortgage originators don't have to be licensed through a state banking department. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Ryan.

REP. RYAN: (141st)

Thank you and I thank the gentleman for his answer. I'm sorry I left that out but sometimes in thousands and thousands of lines it's a good idea to explain for legislative intent why we have a specific provision and I thank the gentleman for his answer.

DEPUTY SPEAKER GODFREY:

Remark further on House Amendment Schedule "A". Remark further on House Amendment Schedule "A". Representative Dyson.

REP. DYSON: (94th)

Thank you, Mr. Speaker. Mr. Speaker, just for, I have a few questions I'd like to ask, please.

DEPUTY SPEAKER GODFREY:

Please proceed, Sir.

REP. DYSON: (94th)

Thank you. They will not necessarily be well organized but nonetheless I'd like to try and get some clarification on a few things.

I'm looking at Line 2984 and the line says one appointment by the minority leader of the Senate who represents a nonprofit organization which advocates for people affected by predatory lending.

Through you, Mr. Speaker I'd be interested in knowing what, does such an organization exist and is there any idea who that organization would be and how do you determine that they represent the interest of people who are affected by predatory lending. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. Representative Dyson, that is a very apt question because when the Speaker's Task Force was formed, one of my initial complaints

and we've come a long ways since that day back last summer, was that I believe that the Governor's Task Force did not have enough representation of people who were of low income or subject to predatory lending.

I thought it was very industry based and what this would be, an example of a nonprofit organization which advocates for people affected by predatory lending. There are a number of them that testified before the Banks Committee and I could set forth them for you on that House Floor I guess.

There's the Connecticut Fair Housing Center, there's the Coalition to End Homelessness, there's probably the Center for Responsible Lending. Representative McCrory indicates to me that there's ACORN, so there's a number of nonprofit organizations which advocate for people affected by predatory lending. Thank you for that question.

DEPUTY SPEAKER GODFREY:

Representative Dyson.

REP. DYSON: (94th)

Through you, Mr. Speaker. If there are a number of them, is there any particular criteria that would

be used other than advocates for people affected by predatory lending that an organization would be selected? If there are a number of them, the appointing authority use what to determine which one? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. I think that would be the discretion of the appointing authority.

REP. DYSON: (94th)

Thank you. Let me to go 2987. It says something similar about federally chartered banks. I assume there are more than one. How does the appointing authority make that decision? Would it be done the same way? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. I thought you said 297. Are you talking about 2987 and 2988? Okay, I see the language here. Yes.

DEPUTY SPEAKER GODFREY:

Representative Dyson.

REP. DYSON: (94th)

Thank you, Mr. Speaker. Mr. Speaker, the bill indicates, it uses the terminology on Line 2989 all appointments to the task force. Is the Commission the task force? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Ryan. Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. Yes.

DEPUTY SPEAKER GODFREY:

I knew I was going to do that.

REP. DYSON: (94th)

So the Commission is the task force? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. Yes.

DEPUTY SPEAKER GODFREY:

Representative Dyson.

REP. DYSON: (94th)

Thank you. Now on line, starting at Line 2992, the administrative staff of the joint standing committee of the General Assembly shall serve as staff of the task force. Is that correct Mr. Speaker? Through you.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. That is correct as it is written, yes.

REP. DYSON: (94th)

Through you, Mr. Speaker. I make the assumption and I would have the proponent correct me if I'm wrong, I make the assumption that there will be a need for information to be exchanged.

People with the particular skills related to banking and I'm just curious as to whether or not it might be better that the staff of the Banking Commission would be staff to the task force rather than the administrative staff of the Banks Committee, assuming that's it. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. This provision was, this is all about establishing a commission on nontraditional loans and home equity lines of credit and it's something that's very important that we have to look at going down the road.

This commission/task force will be reporting back to us in January of '09 and the Department of Banking Commissioner has reviewed this bill line by line with his entire team of administrative staff and legal staff. It has been vetted out with us here in the General Assembly and at no time did I ever receive any type of a red flag concerning this particular provision.

So I'm not sure that it makes any sense to impose a burden on the Department of Banking that can be handled within the confines of this building and in the committee that has cognizance of matters relating to banks.

DEPUTY SPEAKER GODFREY:

Representative Dyson.

REP. DYSON: (94th)

Thank you, Mr. Speaker. I would go to Section 4 and I know that Section 4 was referencing CHFA and that there's a report that's going to be due January 1, 2009, regarding the development of, support of the housing.

I get the distinct impression, through you, Mr. Speaker, that information is being requested and an agency is supposed to provide. Clearly they have the expertise that you need and yet on the other hand when it comes to the staffing of the Commission, the same reasoning does not apply.

I wonder, Mr. Speaker, if there's a particular reason why Section 4 does not adhere to the same standard that we are applying to the other section dealing with the task force. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

This is a task force. This is a study that's not, that doesn't have people, appointees appointed by members of the General Assembly.

It's a task force that's put together or a study group that's put together by CHFA to discuss with their particular expertise in the area with the federal government way in which they, CHFA, can develop a program within the framework of their organization and pursuant to their statutory purposes to purchase and fund the Authority's purchase of foreclosed residential real property in the state to provide affordable and supportive housing, which is a great cause.

They are going to be examining ways in which they can do that within their existing framework at CHFA in concert with CDBG monies and FHA monies that may be coming in the pipeline to the State of Connecticut, but not just the State of Connecticut, to housing finance authorities throughout the state, including the Connecticut Housing Finance Authority. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Dyson.

REP. DYSON: (94th)

Thank you. Let me go to Section 14. Section 14 and the fiscal note, I assume that reflects the amendment itself, says that $2.5 million to the Department of Labor for crisis job training program established by the WorkPlace, Inc. and the other workforce development boards.

Through you, Mr. Speaker, does someone else designate the others because WorkPlace is named and I think there are five in the state. Will that decision get made by WorkPlace, Inc. or is it clearly understood that all the workforce development boards will be included in this. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

I believe that CHFA is going to be working with all the regional workforce development boards. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Dyson.

REP. DYSON: (94th)

Through you, Mr. Speaker. Then the five WorkPlace, Inc. was included here does not reflect on the other four workforce development boards and so therefore they are going to be treated equally, and while I'm at it, Mr. Speaker, how will the $2.5 million be divided up between the workforce boards? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

That is to be determined. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Dyson.

REP. DYSON: (94th)

Through you, Mr. Speaker. Who will determine it? It's through the Department of Labor from the Banking Fund going to workforce development boards. Who will decide? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

What's going to happen is, Representative Dyson, through you, Mr. Speaker, is that the WorkPlace, Inc. and CHFA are going to submit a report back to the General Assembly to the Banks Committee and the planning and Development Committee and in that report they will be shedding light on that. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Dyson.

REP. DYSON: (94th)

Thank you. Just one other piece regarding section 14. It deals with the $2.5 million that is going to be allocated from the Banking Fund. It says for mortgage crisis job training program. That the training is going to be provided. Is there some understanding as to how quickly this will happen?

If it's mortgage crisis job training, I make the assumption that we're talking about a particular skill, we're talking about a decision that's readily made as to who will receive and it's talking about

putting together a training program that's going to expedite matters.

Through you, Mr. Speaker. Has there been a discussion of a timetable as to how quickly this will happen?

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY:

Through you, Mr. Speaker. Yes there has and the fact of the matter is that CHFA right now does do job training and they have indicated to us through public hearings and other meetings that they have been effective and they could use the assistance of other willing and able parties to effectuate job training programs throughout the state. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Dyson.

REP. DYSON: (94th)

Through you, Mr. Speaker. Just an editorial note though. If CHFA has been doing this kind of stuff before, then to go to Workplace, Inc. and other

workforce boards, puts them in a position of having to learn what it is that needs to be done whereas CHFA already knows how to do this. I'll leave that for now.

Section 17 through 18, Mr. Speaker. It speaks to the Judicial Department establishing a foreclosure mediation program. Will there be any inclusion of additional staff people from the Judicial Department to do this? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Yes, there will be. Through you, Mr. Speaker, to Representative Dyson. There will be, in each Judicial District there is going to be a mediator that will be hired and also there will be court operations assistants that will be hired to assist the mediators, as well as six caseload coordinators and that should answer your question. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Dyson.

REP. DYSON: (94th)

Through you, Mr. Speaker. How much money is being set aside for the mediator, foreclosure mediation program? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

The cost is set forth in the following manner. Mediators, caseload coordinators and core operations assistants. That's thirty positions, would total $1.628 million and then other expenses including furniture and computers for these employees total another $81,000 and change so it's a $1.7 million expense plus fringe benefits so it rounds out to $2 million.

DEPUTY SPEAKER GODFREY:

Representative Dyson.

REP. DYSON: (94th)

Thank you. Through you, Mr. Speaker. Do you have any idea how long it would take to have these mediators identified, offices established and the other personnel selected before they are able to be fully operational? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. Yes. The Judicial Department indicates that they are going to able to do this by July 1st and because of the exigent nature of the circumstances their willingness to help out has been amplified by what's been going on in the industry and what they are seeing in foreclosure courts every day and they can model this after housing court.

When you look at housing courts you've got people that use housing courts that have a month-to-month lease, for instance, and they go to housing court and they get sent off to a mediator and they have that right to have a mediator to keep them from, or to give them an opportunity to speak with the other side, so to speak, in the litigation and to try to get a fair deal.

In this case I think this would parallel, this foreclosure mediation program, would parallel what goes on in housing court and I think for the amount of money and the positions that are going to be set up

and also for the Judicial Department's willingness to do this in such an expedited fashion, I think we should be very grateful as a deliberate body here. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Dyson.

REP. DYSON: (94th)

Through you, Mr. Speaker. I have two other questions I think and that would be it. I'm reading the fiscal note and the fiscal note, I'll read it. It doesn't have it by lines here but the fiscal note states if the reserve account fell below a certain level the state would be obligated to appropriate money from the General Fund to refill the account.

Through you, Mr. Speaker. I'm curious as to how that term appropriate is being defined. Will the General Assembly have to meet again to appropriate or are we talking about this being an automatic transfer of monies. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker, to Representative Dyson. If you, just to put this all in context, we're talking about it indicates that if a large number of these uninsured mortgages went into default, because they're not insured mortgages.

There's no private mortgage insurance on these. They are CHFA loans with a possible second mortgage of a down payment assistance program. Then it could potentially affect that agency's ability to meet its debt service liability.

Historically that hasn't been the practice. That hasn't been the practice at CHFA and then in such a situation the debt service payments would be made from the Reserve Account and then it says, well you quoted it, if the Reserve Account fell below a certain level the state would be obligated to appropriate money from the General Fund to refill the account.

It then says it appears very unlikely that this scenario would occur because CHFA is rated as AAA by the ratings agencies, which is higher than the State of Connecticut's rating.

CHFA's high rating indicates that the overall quality of the assets in its portfolio is considered to be very high and the overall level of default risk is low.

Thus in the unlikely event that a large number of uninsured mortgages went into default, CHFA would in all likelihood still be able to meet its debt service obligations with loan repayments from the remainder of its portfolio.

So taken in context, the CHFA has repayments going into their pot, so to speak, and this is a very unlikely scenario. However, OFA in their due diligence made note of this.

And to answer your question about the word appropriate, I think yes it wouldn't be an automatic appropriation, that we'd have to come back in another session and appropriate. This would take quite some time to go through the amount of money.

DEPUTY SPEAKER GODFREY:

Representative Dyson.

REP. DYSON: (94th)

Through you, Mr. Speaker. The reason I posed the question is because I'm unclear about how the term appropriate is being used and what's unclear to me is that it says appropriate monies from the General Fund. My assumption is you can't take money from the General Fund unless you act to do it.

And so implicit in that potential act is the CHFA's credit rate. It may be a triple A now, but it's entirely possible the rating houses could change that to double A instead of triple so we could have an impact on the fund and undermine the CHFA and commit an obligation on the part of the state to an amount of money that's going to be appropriated.

My last question through you, Mr. Speaker, is that when will this relief effort take place? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. The relief effort will take place beginning in July of this year. The foreclosure mediation piece begins July 1st so you can

file a complaint prior to July 1st, a foreclosure complaint, the lender can, but the mediation period would not start for particular complaints until after a return date of July 1st of 2008.

Everything is set up around the July 1st period for the EMAP assistance, for HERO. CT Families is an ongoing program right now and then also the mediation program would be at that same time period. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Dyson.

REP. DYSON: (94th)

Through you, Mr. Speaker, as a follow-up to the last question. I hope this is my last question and that is given the urgency of people who are confronted with foreclosure issues today, does the proponent of this amendment assume that we will have an apparatus in place timely enough to address the needs of those who are in need. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. That is a threshold question in this whole debate. The reason why we didn't put together a Committee to study this and come back to us in January and tell us how to do it was because we want it to be statutorily set forth as to when they're going to start doing it, how they can get ramped up and running, get CHFA to be able to be in a position to be able to receive applications for the various programs.

They know it's coming. They've been part of the negotiations all along. They've indicated to us, the timelines reflect in large part what they've indicated to us and the timelines reflect also, in large part, what the Judicial Department has represented to us as timelines in which they can reasonably move to put together a comprehensive, well thought-out mechanism to handle what we are giving them in this bill. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Dyson.

REP. DYSON: (94th)

Through you, Mr. Speaker. I appreciate the responses from the proponent of the amendment. Thank you very much.

DEPUTY SPEAKER GODFREY:

The gentleman from Bridgeport, Representative Ayala.

REP. AYALA: (128th)

Thank you, Mr. Speaker. Good evening. I rise today in support of this bill. I want to thank the good Chairman of the Banking Committee for bringing this bill out and giving us the opportunity to debate the merits and talk about this issue that is so important, very important and especially to the constituents in my district.

I've had the opportunity to walk my district, drive through the many streets of my colleagues in the city of Bridgeport and even in the towns and cities of other people and one of the things that I see is I continuously see foreclosure signs going up.

You go one week, you pass the next week and you see another sign come up. You pass it another month later you see another sign come up. Oftentimes when

you stop and talk to these homeowners there's a sense of desperation in their voice.

Oftentimes it's a little bit too late to give them the assistance that they need and I hope that there will be the necessary outreach to get to these individuals that might be able to take advantage of this particular program.

I've had the opportunity to go to meetings, go to workshops, rallies with the different neighborhood organizations, ACORN being one of them, and standing there with people who have lost their home or were in the process of losing their homes.

You just want to do anything that you can to try to assist them, give them the information necessary so that they might be able to save their homes.

I'm glad that this body is doing this this evening. Hopefully my colleagues will support this measure so that we will have a tool to go back to our constituency and let them know that there is help for them, that there is something out there that might be able to assist them and prevent them from losing their home and I hope that my colleagues here in the House

would be able to support this measure because it truly is, as I just said, a tool that might be able to assist our constituents in preventing them from foreclosures.

To my colleagues I urge you please vote in the affirmative as I will be doing this evening. Thank you.

DEPUTY SPEAKER GODFREY:

Thank you Sir. The gentleman from Stratford, Representative Harkins.

REP. HARKINS: (120th)

Thank you, Mr. Speaker. Just a few questions to the proponent of the amendment.

DEPUTY SPEAKER GODFREY:

Please proceed Sir.

REP. HARKINS: (120th)

Through you, Mr. Speaker. Going through the bill I was just, I don't see any mention of co-ops. If someone had a cooperative unit that was in the process of being foreclosed or was in financial trouble, would they be able to avail themselves of this program? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. I just wanted to clarify, there are various sections of the bill and a lot of definitions of, definitions for each section of the bill. What program are you talking about? What section of the bill are you talking about Representative Harkins? I apologize.

DEPUTY SPEAKER GODFREY:

Representative Harkins.

REP. HARKINS: (120th)

Through you, Mr. Speaker. Section 7, Lines 327 through 331 point out the real property one to four family in a common interest community and I've been just going through the bill now myself, or actually the amendment, and I'm just trying to see if there's anywhere in here that mentions cooperative units. Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Through you, Mr. Speaker. No.

DEPUTY SPEAKER GODFREY:

Representative Harkins.

REP. HARKINS: (120th)

Through you, Mr. Speaker to the proponent of the amendment, how many people will this program actually help if this is passed in its current form? Through you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Representative Barry.

REP. BARRY: (12th)

Well, I can answer that. Nothing's purely scientific but I've gotten some numbers from the Connecticut Housing Finance Authority and in general what they have indicated to me in crunching the numbers and also actually OFA did this too, for me, and I know them off the top of my head but I can give you some exact numbers. Let me give them to you off the top of my head Representative Harkins.

The EMAP program is going to help about 1,000 people to 1,100 people given the average loan of about

$69,000. The HERO program is going to help about 250, I'm sorry households.

When I say people, homeowners. Could be seven people living in a home, but homeowners. And then HERO would help somewhere around 250 people and then the CT Families would help somewhere between 200 and 250 families.

DEPUTY SPEAKER GODFREY:

Representative Harkins.

REP. HARKINS: (120th)

Thank you, Mr. Speaker. Going through the amendment, and again I just got this a little while ago myself. It seems the underwriting guy might be somewhat stringent and that people that are in financial difficulty may not even qualify for any type of program that the State of Connecticut is coming out with.

One of the concerns I have and this as being a member of the Banking Committee, is the whole question of whether or not the State of Connecticut should be involved in a bailout.

Being in the real estate industry I see what went on, I witnessed the sub-prime lending fiasco. We don't see those types of loans being made anymore but again I think we showed up once again too late.

They've been made. People are undergoing foreclosure but I think the question we have to ask ourselves here tonight is as a state, what role do we play in the mortgage market.

We're talking about sub-prime mortgages today. Is it going to be credit cards tomorrow? Car loans tomorrow? The next day boat loans? The following day student loans? The day after when people have financial difficulty or made a mistake in their investments, they're going to turn to the State of Connecticut and say what about me.

I don't know if we as a state want to be in that position and quite frankly I don't know how much of an impact this bill will actually have on the current situation affecting our cities right now.

But I can tell you this. The one concern that's screaming at us all here today and Representative

Dyson had brought it up in some of his questions, was the effects it could have on our CHFA bond rating.

CHFA's a great program. It offers opportunities to first time homebuyers. It's a triple A bond rating. I'd like to see that continue as it has been doing, offering opportunities to people as opposed to being utilized for a bailout.

We could actually limit the amount of money available to new homebuyers and also risk the chance of having a reduction of the bond rating, depending upon how many people actually apply to this program.

The amendment does have some good provisions in it, however it's the bail-out part that I have a problem with and, Mr. Speaker, I will not be supporting this amendment this evening and I will be voting no, only because I don't believe the State of Connecticut should be bailing out people that are in trouble with mortgages. Thank you, Mr. Speaker.

DEPUTY SPEAKER GODFREY:

Thank you, Sir. Remark further on House Amendment Schedule "A". Remark further on House Amendment Schedule "A". If not, staff and guests,

please come to the Well of the House. Will the Members take their seat, and the machine will be opened.

CLERK:

The House of Representatives is voting by Roll Call. Members to the Chamber. The House is taking a Roll Call Vote. Members to the Chamber please.

DEPUTY SPEAKER GODFREY:

Have all the Members voted? Have all the Members voted? If so, the machine will be locked. The Clerk will take the tally. Will the Clerk please announce the tally.

CLERK:

House Bill Number 5577, as amended by House Amendment Schedule "A".

Total Number Voting	148
Necessary for Passage	75
Those voting Yea	124
Those voting Nay	24
Those absent and not voting	3

DEPUTY SPEAKER GODFREY:

The bill as amended is passed.

Representative Reinoso.

REP. REINOSO: (130th)

Thank you, Mr. Speaker. Mr. Speaker, just in one minute I'd like to bring to the attention of my colleagues that today is one of the most--

DEPUTY SPEAKER GODFREY:

Representative Reinoso, just a moment.

(GAVEL)

Thank you, ladies and gentlemen. Representative Reinoso has an announcement.

REP. REINOSO: (130th)

Thank you, Mr. Speaker. Today is one of the most important holidays for the Mexican-American community. As we know, the Mexican-American community has been living in this country for over five centuries. We can say California, Montana, Arizona, Texas, New Mexico and so on and so forth.

I'd just like to bring this to you because colleagues in different House of Representatives, the Speaker of the House in California is Mexican-American as is the Mayor of Los Angeles and I think you have diversity and I'm living proof.

JOINT
STANDING
COMMITTEE
HEARINGS

BANKS

PART1
1-289

2008
Index

Sorry. I didn't have my mike on. Good morning.

SB 220

COMM. HOWARD PITKIN: Good morning, Chairman Duff, Chairman Barry, Members of the Committee. My name is Howard F. Pitkin, and I am the Commissioner of the Connecticut Department of Banking.

I am here to testify in favor of two pieces of legislation, but first I would like to clarify an oversight in my testimony last week.

When I was speaking on Senate Bill 21, AN ACT CONCERNING MORTGAGE LENDING, I stated that 20% of sub-prime loans are seriously past due, and in likelihood of foreclosure. That actual number is about 8%.

I want to apologize to the committee. Hopefully, no confusion resulted. The two ratios I cited were simply different measurements, and I will respond to any questions on this matter.

Moving forward to the legislation before the committee today, House Bill 5577, AN ACT CONCERNING RESPONSIBLE LENDING AND ECONOMIC SECURITY is a bill designed to try and address the current mortgage crisis.

While the department appreciates the time and effort it took to craft House Bill 5577, the agency cannot support the bill.

Instead, we would like to ask the committee to endorse Senate Bill 21, AN ACT CONCERNING

MORTGAGE LENDING, a governor's bill in which the agency worked with our office in drafting.

I spoke in detail on this bill during last week's Banks Committee Public Hearing. I will not go into specific aspects of the merits of Senate Bill 21 again, but I did want to convey the agency has been working with other interested parties, and will be submitting substitute language on the bill, which we believe is acceptable to all involved.

This language should be provided to the committee by the end of the week. The agency would like to lend its voice to support Senate Bill 220, AN ACT REQUIRING A SALES AND USE TAX EXEMPTION for certain sales by Connecticut credit unions.

This bill would allow an exemption from the Sales and Use Tax for sales of tangible personal property to state-chartered Connecticut credit unions.

Currently only federally chartered credit unions benefit from this tax exemption. To level the playing field between the state and federally chartered credit unions, I fully endorse the elimination of this tax.

According to estimates researched by the agency, the loss in tax dollars to the general fund would be less than $500,000 per fiscal year.

This is a minimal loss to promote fairness in the private sector and continue to encourage

credit unions to choose a state charter over the federal charter.

Again, I encourage you to support the bill. I want to thank you for your attention, and I will be happy to answer any questions you may have on this or any other bills.

REP. BARRY: Thank you very much, Commission. I appreciate you coming here today to testify at our second public hearing. HB 5577

I was not here for the first public hearing when you did testify on your bill, SENATE BILL 21. I have had the opportunity to work with you.

I came in as Chair, I think, the same week or same month that you became Commissioner. I know that you've spent over 30 years at DOB, I believe.

You garnered a lot of respect there, and I know I appreciate your accessibility, your deep knowledge of the law, and your ability to, whenever we have questions, especially me, I have questions, to explain technical areas of law.

You're always available to do that, and have the level of competence to be able to do that. It has been kind of a rough and tumble year.

We've had some experiences with unscrupulous lenders. You've dealt with the MLN crisis, the Mortgage Lenders Network. I thought you acted admirably there.

I was glad to see that you refused to allow in-home capital to form and continued doing work. The previous owners of MLN, the guys that used to run that.

For those of you who don't know what happened in that mortgage lending debacle, the previous owners who had not funded loans and left hundreds of people without jobs tried to form another company and go to the Commissioner and do the same thing, offer loans and loan people money, but under a different name, and the Commissioner swiftly responded to deny them the ability to do that.

Just a quick question just in general, because I know that you said that you can't agree to support House Bill 5577 and going to continue sticking to your guns on Senate Bill 21.

Just in general, we've got three bills dealing with this general concept of how to deal with the sub-prime crisis: Your bill, the committee Chairs' bill, and then the Fair Housing bill.

My question to you would be what do you think the ultimate goal of such a bill would be, coming out of this committee? What would your ultimate goal be to see in that bill?

COMM. HOWARD PITKIN: It's my feeling that, and I'll speak to Senate Bill 21 and what we tried to do in that bill. There are two different constituencies here that in general we have to look at.

One is the mortgage industry itself, the non-bank mortgage industry. And then on the other side and of primary importance is the consumer.

We tried to build in a pricing structure for loans to determine which class they fell in, whether it was, you know, higher cost loans or not, and to shine the light where we felt the light was needed.

And it is in borrowers that are in a troubled financial condition that are applying for a mortgage loan. I have not heard any complaints about the prime mortgage market.

So being a believer in free enterprise, I think if it's not broken, don't fix it. In addition to providing additional foreclosure. I'm sorry, that's an awful word here.

In addition to providing additional disclosure of the terms of a loan, we built in a reasonability, a level of reasonability to the determination for a broker or a mortgage lender that if you approve a high cost loan, you have to reasonably believe at that time that that consumer can pay that loan under the terms you've structured.

In order to prevent steering, because there is some indication that there was some steering going on, these price collars identify a level at which all terms have to be disclosed, and you know, two different products would have to be offered to the customer if, in fact, they contain certain features.

I think there are two sides. One is regulatory, and we in Senate Bill 21 laid out our regulatory scheme for regulating this industry on a more high-touch basis, which is what we feel it needs.

We want to bring this industry up a level. We want the industry to adopt certain statements that the Conference of State Bank Supervisors worked on, on the risks involved with nontraditional lending, loan products, as well as sub-prime loans.

And we feel that there are key parts of those which build in some consumer protection. So we felt we came down both on the side of consumer protection as well as the regulatory scheme. And that was our objective.

REP. BARRY: Okay. Very well, I imagine part of your job is to make sure that consumers are protected and banks are profitable enough, lenders are profitable enough to be able to provide credit. Is that an accurate statement of what part of your job is, and kind of what we're here to do with this bill?

COMM. HOWARD PITKIN: Absolutely. And I would just add this to that to not enact anything, which is going to curtail credit in Connecticut.

I think there is one thing we can all agree on here that, you know, sub-prime lending is going to be reborn in some form. You don't want to shut off credit to anybody. You just want to increase the disclosures and the understanding on that transaction.

The success of the transaction is built on everybody understanding it.

REP. BARRY: What's your position on allowing borrowers to sue [inaudible]?

COMM. HOWARD PITKIN: Well, that's a very sensitive subject. I think that the secondary market in this country is key to the free flow of credit and money, and mortgage products are routinely sold into the secondary market by the mortgage industry.

I think we have to, if the committee is going to look at a [inaudible] liability, we have to do that very carefully.

In fact, I was just talking to someone a few minutes ago, and years ago the state of Georgia really stubbed their toe badly with that issue and had to convene a quick session of the General Assembly, because mortgage money had, I'm not sure it dried up, but the rating agencies would not recommend a higher rating for a Georgia loan.

So it's an issue that passes liability along to whoever comes in ownership to the loan, and it can have, unless it's very well defined and capped, it can have incalculable liability for the secondary market.

REP. BARRY: With respect to House Bill 5577, do you think that the definition of non prime in that bill, I know you may have some issues with other parts of the bill, but the definition of

non prime, do you think that's going to reach out and cover an adequate amount of sub-prime mortgages?

COMM. HOWARD PITKIN: I do. I do. What we're trying to do is 3 points above the relevant T-bill instrument would determine it's a prime loan. If you go over that, then you're in the middle class.

And those loans would, if it's over 3 points, plus the T-bill rate, those loans would fall into a higher cost category, but not high cost category, and would get more disclosure.

If you go 8 points over the relevant T-bill rate for a second lien, then you're in the territory of a high cost loan and there are onerous disclosures to protect these people that have been victimized.

Second mortgage loan applicants are much more likely to be abused than are first mortgage applicants.

REP. BARRY: And how often do you see the high cost loan provisionary statutes being violated?

COMM. HOWARD PITKIN: When the legislature enacted that, and I'm not sure of the year, but it was a while ago, I think it was '92, we have not seen a high cost loan.

REP. BARRY: With respect to Yield Spread Premiums, I guess my layman's definition of a Yield Spread Premium is the amount of money that a mortgage broker makes for bringing money from a

mortgage lender to a borrower. Is that relatively accurate?

COMM. HOWARD PITKIN: Well, that is relatively accurate. I think that the industry, in following that practice, has left itself open to the accusation that it has caused steering into higher cost, more risky loans.

And that, you know, if a Yield Spread Premium is being paid on, let's say, a variable rate hybrid loan, then the broker who is, you know, representing only himself, is going to steer that customer into a high cost loan.

We did see some evidence of that in our sub-prime task force with comparing FICO scores to what type of credit those customers got.

I think, I am certainly willing to talk with anyone about Yield Spread Premiums, and there is a reluctance on my part to get involved with compensation in an industry.

I tend to look at things as a purist in this, but I am, you know, if there is evidence that there is significant steering going on, I'm certainly willing to talk about it.

REP. BARRY: I read somewhere that about 85%-90% of all sub-prime loans contain a Yield Spread Premium, and that suggests to me that there is probably some mortgage brokers that are needlessly pushing prospective borrowers into more expensive products.

And it kind of shouts to this committee that we probably need to do something with respect to regulating Yield Spread Premiums.

I presume that you probably don't advocate on behalf of capping Yield Spread Premiums. Is that right?

COMM. HOWARD PITKIN: I would certainly like to talk about the issue and look at the material you have, Mr. Chairman.

I think, you know, the Department of Banking typically never gets involved in compensation unless we think it's excessive. The trouble with these Yield Spread Premiums is there is some evidence, and what we found was FICO scores of 700 or over.

And 700, you know, that's about an average credit score, you know that they were all migrating over into sub-prime credits. That should not be.

You know I'm not sure what the ideal distribution would be, as to what those customers got, but, you know, an inordinate amount of them were put into sub-prime loans, which for an average FICO score, would not appear to be the right thing.

So I would love to talk to you more about it.

REP. BARRY: Okay. And do you have an opinion as to whether or not Yield Spread Premiums should be included within the definition of a prepaid closing cost?

COMM. HOWARD PITKIN: I believe in Senate Bill 21 it is.

REP. BARRY: It's a prepaid finance charge.

COMM. HOWARD PITKIN: Right. I mean, the issue, I think, is, another issue is disclosure.

If the Yield Spread Premium is disclosed to a borrower, and I think both House Bill 5577 as well as Senate Bill 21 contains a lot of new disclosures for brokers to, you know, let customers know what they're getting into, and it's disclosed.

Then that customer has, you know, the right to go to another broker where that's not a factor. And again, I think that the markets operate on both parties understanding what they're getting into.

And I don't know that the answer right now, but I could get back to you on that.

REP. BARRY: Okay. And do you have any opinion as to whether the legislature should impose a statutory fiduciary duty on a mortgage broker with respect to a borrower?

COMM. HOWARD PITKIN: Well again, Senate Bill 21 imposes a reasonable duty on the part of mortgage brokers and lenders.

I think a fiduciary responsibility is, however, a much a stronger level of obligation, and I know that the bill submitted by Fair Housing

actually makes a broker an agent for the customer, which changes the fundamental position in the transaction of a broker.

And if he is an agent for the customer, what happens to the bank whose product that he's trying to sell, or the lender whose product that he's trying sell?

I think we have to be very careful about this, and you know, realize that there are certain parts of the mortgage industry that need restructuring and more disclosure and more supervision by the Department of Banking.

And then there are parts that are working just fine. And anyway, I'll leave the answer at that, and would be happy to look at it further with you.

REP. BARRY: And as a percentage of all mortgage loans in the state of Connecticut, what would you say percentage-wise are originated by mortgage brokers?

COMM. HOWARD PITKIN: I have anecdotal evidence that about 60% are originated by brokers, and that was an article that was written by Peter Spalthoff in the Hartford [inaudible] piece. So I would say put roughly 60%.

REP. BARRY: Okay. That's consistent with what I read in the *Boston Globe* about the national trend, I think. And, would you say that loans by mortgage brokers are particularly given to people on the low end of the credit market?

COMM. HOWARD PITKIN: I think if you look at our sub-prime task force report, it shows the distribution of FICO scores, and while a number of them are very low, probably in the region of 550 or, you know, lower, a number of them go right up through, you know, 800.

And, it tells me two things. That in certain circumstances sub-prime lending is appropriate. I mean, you know, a prime borrower is making a judgment that they're going to take a sub-prime credit, or an all day credit.

Maybe it's a corporate executive who's going to be here for two years, and the corporation is going to buy his house when he's done.

And then there are some suggestions that low income individuals have gone to, I would call it, beyond a suggestion, I think there is evidence that brokers have accepted credits based on stated income, which they themselves in their own industry call liar loans.

And then they, they don't document employment history or salary. You know, no one is being done a favor in those situations. So I think that the two reasons we're in the, in the fix that we're in nationally if not worldwide with this problem is lax underwriting, and fraud.

Fraud is the hardest thing to prove in anything I've ever tried to prove with a person that's violated the law. And therefore in our bill, Senate Bill 21, we put a fraud statute that follows the entire credit chain, and would

subject anyone who commits mortgage fraud to a class D felony.

In the other two bills on the table, fraud is allowed to be used as a defense in foreclosure, and frankly I don't think that goes far enough.

I mean, let's let that be used in the foreclosure, but let's take the individuals who've committed the fraud and make them subject to a law with more teeth than what we currently have.

REP. BARRY: So, I guess a two-part question then, you don't have a, you're not opposing fraud as a defense in a foreclosure, and secondly, I'll ask you that first.

COMM. HOWARD PITKIN: You know, when I read that, I thought a lot about it, and I'm not prepared really to say whether I support it or not.

There is a task force over in the Judiciary that is looking at foreclosure, and I know that there is bills here about foreclosure. I'm not an expert in that.

I think there's plenty of attorneys here that can weigh whether or not that, that step in the law would be a good thing, or if it would slow foreclosure.

I mean, the problem with slowing foreclosure down is that, you know whether it is the number of cases, or just going way beyond what the law date might be is that normally the properties, you know, fall out of repair.

The people living there, with exceptions, you know, they really don't have much of an interest there anymore, and you know, properties fall to disrepair, and that's why foreclosure has become really the last resort in these loan situations, which it should be. And, I think the market has acted to correct that.

REP. BARRY: With respect to fraud as a new part of our penal code, class D felony mentioned, what is the purpose of having that classified as a felony, or classified as a crime when there is already, you can already be arrested and convicted for bank fraud and other types of fraud? And it seems to me that that would already be covered by other parts of the Penal Code.

COMM. HOWARD PITKIN: A lot of the mortgage business is done outside the banking industry, and we wanted to have, there was one situation in New London where, I think, the members of the Committee saw where the Attorney General sued those people, and they had formed the perfect storm.

They had a broker, a lawyer, an appraiser, a sales agent, and they had everybody else they needed to put this fraud together with 30-some odd properties.

And, you know, the stories were absolutely ridiculous where they sold a $600,000 four-family house to a woman that had no visible income.

And, I think to approach situations like that without a law that imposes a felony as well as fine or imprisonment is not looking at our duty to the public the right way.

I think we need something there to take these people to the law.

REP. BARRY: How's your foreclosure hotline doing?

COMM. HOWARD PITKIN: Wonderful. As of yesterday, we had almost 2500 calls since August 24th. We have developed a good network of sources to refer people to, and we're trying our best to handle this, this huge inflow of calls.

We've hired a person that just does that now, and she's doing a great job, Mary Stajus? and if any person out there has a problem with their loan, the last thing they want to do is wait and be reluctant to talk about it.

And I think the more we get that word out that you've got to come forward, that a problem has got to be recognized for it to be resolved.

REP. BARRY: One last question. Could you just briefly comment on the state of the State Charter and also if there are any bad things to be coming down the pike for community banks?

COMM. HOWARD PITKIN: Well, we always have the Washington authorities leaning over our shoulder, and yet we work very well with them. The one, of course, that we don't seem to be

able to regulate well with, is the office of the Comptroller or the Currency.

While we have good relations with them, it's working together that is a problem. I think that, you know, the banking industry and the credit union industry did not cause this problem, and I do think that, and I think I testified last week that, you know, the banking industry and the credit union industry are probably the two most heavily supervised industries in the nation.

They have so many exams every year, it has become their single greatest cost of operation. I would hope that we could give some consideration to taking them out of this bill, because there is some legislation as well as regulations coming out of Washington, which they're going to be subjected to the credit union and banking industries.

We do examinations regularly on them where we have not on the mortgage bankers. Now we want to do more exams on the mortgage bankers and continue our compliance exams on the banking industry.

So I would say that what we tried to do is to not add to the regulatory burden of banks or credit unions, and that is our goal now in considering these bills.

REP. BARRY: Thank you very much, Commissioner. Thanks for all your thoughtful answers and appreciate your coming here, and I'm just going

to open it up to other members if they have questions.

COMM. HOWARD PITKIN: Thank you, Mr. Chairman.

REP. BARRY: House Ranking Member, Representative Ryan.

REP. RYAN: Morning, Commissioner. I know it's a challenge always trying to stay straight between Representative Ryan and Ryan Barry, so we'll try not to confuse things further.

And I commend you. Not only did the chairman mention your accessibility, but I can't remember a time in my career where the banking Commissioner has been such a popular person in the media for interviews.

And with that, let me ask you to go back to your first comments which also by coincidence were your first comments a week ago. We hear all these fun numbers in the media about the Connecticut's in the top ten.

Someone asked me today about we rank number eight. I know they're not asking about ESPN sort of ratings. But could you quantify for us a little better the extent of our problem?

We obviously don't have in the top ten numbers of foreclosure cases per state in the country. Are we as bad as Ohio? Are we better off than New York?

COMM. HOWARD PITKIN: Connecticut has roughly, as of 09/30/07, almost $17 billion in these loans.

That's 15% of all loans in our state, and you know, 8% of those are seriously past due or in foreclosure.

The good part of Connecticut's economy, and I'm not an economist, but I think, I'll just say this. The good part of our state is its economy right now is, is strong, and we have good employment.

If we had troubled mortgages and an employment problem like Ohio, Michigan, Las Vegas and out into California, we would be much worse off, and be dealing with a lot worse situations than what we are right now.

Having said that, that doesn't help the families caught in the situation.

REP. RYAN: So quantifiably, I guess it would be fair to say that a plus that we have is that presumably people in a state with a better economy are more likely to be able to go get another job or a second job or do something to try and get themselves out than people who are unfortunately in those other states.

That's not a good situation, but relatively speaking, we're not in a worse situation.

COMM. HOWARD PITKIN: Could I add one thing? And I first say I'm a member of the Board of Directors of the Connecticut Housing Finance Authority by statute. But the one thing that I think lessens the sub-prime problem in Connecticut is that CHFA is such an active home loan provider in the 1-4 family area.

And they take people that are not presently bankable, and they expose them to all kinds of credit counseling, and they put them in a loan they can afford, and then bring them back into the banking system.

That's the goal of the credit. Had they not been so active in doing that, we might be much worse off than what we are now.

REP. RYAN: Thank you for that answer. And now let me segue to a related issue then. And part of the problem with this committee like many is we toss these technical terms out there, and I understand that somebody listening at home wonders what the heck we're talking about.

But there was a question a few minutes ago relating to assigning liability and could we try and put your professor hat on for a second, and could you give us in a sentence or two what we're talking about when we're talking about assigning liability in the market, and why we have to worry about that?

COMM. HOWARD PITKIN: I will certainly try. Liability in any transaction is in the state laws in this case surrounding it. It assigns various levels of liability to the people that are lending money.

That liability transfers to the people that might subsequently own that loan, because the mortgage banking industry, non-bank mortgage industry typically does not hold loans for

long. They sell them into the secondary market.

REP. RYAN: And if I can interrupt for a second, I apologize, but I find that people misunderstand this all the time.

Local person comes, does closing, you get the money, etc., and the pieces of paper, the note and the mortgage deed, and the packet of all these other 40 documents ends up being sold in a big package of hundreds of millions to Ginny Mae or Freddie Mac or somebody else down the line.

So you're never dealing most of these days with the person who made the loan. Is that the situation?

COMM. HOWARD PITKIN: That is the situation. You may continue to get a bill from a lender that provided the loan to you, but the actual loan is only being serviced by them, and then they send the money along to the servicer who then pays the members of the collateralized mortgage pool investors.

When you pass liability along into the secondary market, great care has to be taken, and some people feel that it is possible if it's capped, because you can't quantify it.

You can't quantify if that servicer buys, you know, 70,000 loans from Connecticut. You try to calculate the liability on those. I mean they might meet the specs of whatever the pool

was or Ginny Mae, Fannie Mae, whatever, but you're never quite sure.

They're passed along as part of a pool they're invested in, and then, and then God knows what happens to them. But the system does work, but it's based upon calculable risk, and assigning liability can be an open hole that nobody can estimate the loss might be in.

There has been, you know, different problems that happen. One in Georgia years ago that, it pretty much stopped lending for a little bit, and they had to correct it, and then life went on.

But, it's something we just have to be very careful with.

REP. RYAN: And so if I can follow-up to that after those background questions. So, in other words, is there a concern that if we tinker with assigning liability in Connecticut we might have any deleterious effect on people being interested in purchasing loans that are made in Connecticut?

COMM. HOWARD PITKIN: Potentially.

REP. RYAN: Would that have any effect on our economy?

COMM. HOWARD PITKIN: Potentially, and if credit dries up, it could have a great effect on our economy.

REP. RYAN: Let me move to a different area, and I don't want to keep you here all morning, because I know there are a lot of people I'm sure want to testify, but there was also a reference made to in House Bill 5577 about the concept of giving the Commissioner the authority to, I guess for lack of a better term, I'll make up issue a stay on foreclosures in this state.

Now you happen to be the Commissioner I suppose, is that something that would concern you in the scope of your duties as to whether or not it creates any problems with any other parts of your job if we did that?

COMM. HOWARD PITKIN: Well I think, I think, you know, our agency is a regulatory agency. I think that those responsibilities as far as I know are in the Judiciary, and you know, I'm happy to work toward a reasonable solution with anyone.

You know, I know that those are part of three programs that are offered in House Bill 5577. I don't think if I had a chance to explain, you know, that the appropriate place is in banking. However, there may be an appropriate place for that.

REP. RYAN: So maybe a diplomatic way of putting it would be if the Commissioner is the regulator, if somebody is going to be stopping the foreclosure process cold theoretically, it might be better if it's someone different than the regulator who would have that authority. Is that a concern?

COMM. HOWARD PITKIN: It would be difficult for the banking Commissioner to take issue with the outset quality of an institution. While I've approved a moratorium on, you know, a lot of loans, a lot of mortgage loans that they may have.

It's only potential. I think that it's vague. The statute does not apply to banks in that area, but we regulate other entities, and you know, I think conflict of interest in the financial world is something that we all have to avoid direct or even the apparent.

You know, even a vague conflict of interest and I want to resolve that issue before we go any further with that if I have a chance.

REP. RYAN: And just one more on this topic, and I'm going to quit in a second, because I know other people have questions. But could you get back to us.

I'm unaware if there are other Commissioners in other states or other quasi-regulator people to use a very inexact term, that have this kind of authority, and I would be curious to find out if anyone else has done something like that, and if through your good offices if you could hunt some of that down, I'd be interested.

COMM. HOWARD PITKIN: I will find that out and get it to the Committee as soon as I can.

REP. RYAN: I could probably ask another 20 questions, but I'll pass, because I know

Representative Stripp will be bored if he doesn't have some. Thank you Commissioner.

REP. BARRY: Representative Stripp.

REP. STRIPP: Thank you, Mr. Chairman. Morning, Commissioner. Good to see you again. It was only a few days ago that we had our first meeting here in this Committee.

I've been trying to get my arms around intellectually around the sub-prime crisis, and best I can understand, and if I'm wrong, if you could correct me, but it seems to me much bigger than our little state of Connecticut.

It certainly has sent shock waves through the financial markets all over the world. In fact there was one in a cute, but tragic story about a small town, and I think it was in Norway that was north of the Arctic Circle that bought some collateralized debt obligations that had mortgages in there.

And it was creating such a major problem for them they couldn't pay their employees. So it's not just here, and that was part of reselling these collateralized debt obligations.

And I've heard other stories that the packages that were sold were only partially sub-prime loans. They had other derivatives and other things in them making it much more complicated, and that created some of the problems around the world in the financial markets.

But to take a look at what is happening here, it would seem that, and I may be incorrect in this, but it would seem to me that most of the banks, if not all the banks that you regulate are, if involved at all, involved in a very, very small percentage, with the sub-prime mortgage market because of regulations of your department and others, and to that end of making that a little more obvious to Members of the Committee, we have a page out of your website State of Connecticut Department of Banking, and it says Banks in Connecticut and it lists all the banks.

And on the left it has the names of CEOs, and on the right it says Primary Regulator. And as I go down it, I see DOB, which I assume is Connecticut Department of Banking. They are the ones that you really regulate, and the others are regulated by OCC as you mentioned before, and Federal Reserve, etc.

Do we have much control over these other banks, other than jawboning and trying to get them to cooperate, other than those that are listed under DOB as being their primary regulator?

And when I say that, I mean the State, this committee, your commission, and so forth.

COMM. HOWARD PITKIN: Well, we, we do talk to the other agencies. In fact, I'm going to be meeting with some officials from OCC very soon to work out a complaint protocol.

But I think what will go to your question is, I'm sure you're aware that there was a group of

AG's in the country that formed a group along with state regulators to try to work with the services to speed up the modification process.

And, you know, there is no more noble purpose at this point in our national economy than to clear up this problem, get people into a loan that works, and let life go on.

OCC refused flatly to take part in our group. So therefore, we had no information about some of the largest banks in the country.

Now you know that's unfortunate, because the services were at the table, and I think we could have convinced them to do some good things, because I don't think modifications are happening quickly enough.

I mean I won't be satisfied until I see, you know, vans out in our inner cities with the bank name on them rewriting mortgages on the spot.

And I think it'll take forever if it's done on a case-by-case basis representative. It has got to be done by, I believe, the Congress has to approach this, and one of the greatest ideas I think that has been put on the table right now is from the Office of Thrift Supervision.

For their banks, they're trying to enact regulation to allow the banks, or Federal Savings Banks to actively participate in the short sale of houses that occur because of sub-prime loans.

OTS is willing to issue a negative equity certificate to the bank that absorbs the loss between whatever is being paid for the house and the market price, and if that house is ever sold again, and you know, the consumer can wait out this dip in prices and the price does go up, the bank can recover their money with this certificate.

And I think, you know, a program, a pool of money instead of all of them making a single loan, you know, if we could participate in issuing these certificates, I think that they would go incrementally a much farther way.

The program is being considered right now, and I'll keep the Committee apprised of it. I think it's a great idea, and I do think it has some legs, so I hop that answered your question. We are much better off in some areas of the country.

REP. STRIPP: I agree with you in that concern, Commissioner, because if we start to regulate a group that really wasn't the major or even a significant part of the problem, we're liable to cut off all mortgage lending, which as I think you alluded to before, would create a problem in the housing market.

It would create a problem with the carpenters, the plumbers, and everybody else, and creating an unemployment situation in our state, which then might lead to additional foreclosures, because people are out of work, which is the common way they get themselves in financial trouble.

So I think your approach to try to keep the, the market going so there will be, continue to be mortgages available is very laudable, and one we have to be very sensitive to in this Committee.

Right now the financial markets as you know are very skittish, and it doesn't take much to upset the apple cart and change things. I was looking at the average mortgage, first mortgage rates recently for 30-year mortgages, and it was down below 5.5.

And then all of a sudden a couple of weeks later when the entire worldwide financial market got very nervous about the situation, it was up to 6.5, and that's very costly to the consumer.

So I think you're on the right track being very sensitive to that issue. I look forward to the additional testimony, and hopefully we can weave our way through the problems that we have understanding that Connecticut's only a little tiny piece of it, but we've got to do the best we can for the people that are in our state. That's our goal for all of us. Thank you Commissioner.

COMM. HOWARD PITKIN: Thank you, Representative Stripp.

REP. BARRY: Thank you, Representative Stripp. Representative Harkins.

REP. HARKINS: Thank you, Mr. Chairman. Thank you, Commissioner, for coming today and giving your testimony. First I'd like to thank you for establishing the mortgage fraud hotline. That was very helpful to me this past week.

I had a person call me under duress, and I referred him to the hotline for information, but he was dealing with a financial planner, and he was telling me that the planner wanted him to turn title of the house over to him, and then he was going to lease the house back to the homeowner.

I mean, it just, the more the story went on, I said stop. Let me call the Banking Department. Let me see what help I can get you. I referred him to the mortgage hotline, and that was in-state.

So I'm sure these types of incidents are becoming more common as people run into trouble, but it makes me sick when I hear that, because people are being taken advantage of.

They're not financially savvy enough to figure it out, and they're being used and abused one more time. You know it's great that the Committee has taken up the issue of sub-prime lending, but I almost feel as though it's too late.

You know, the bus has already left, the money is dried up, people made their money, and they're moving on to other things or other products, but I do feel as though it's necessary that we do address it as you said,

something else will evolve down the road or into the future.

I have a bill in the Insurance Real Estate Committee today that deals with undue influence on appraisers and appraisers working with mortgage brokers in a way that is not in the best interests of the borrower, but this was relatively recent. (HB5517)

It was a mortgage company out of Rhode Island. The appraiser actually saved the voicemail message. It's on tape, and the broker called up and said, I love hearing these things, and he's doing FHA loans.

I have a whole lot of them I want to give you, but I need maximum values. It's important I get [Gap in testimony. Changing from Tape 1A to Tape 1B.]

--recourse against the mortgage company in the State of Rhode Island that's doing business in the State of Connecticut. Do we have any?

COMM. HOWARD PITKIN: I'd have to know more about the transaction, but I think in House Bill 5577 there is some pretty specific language about just that activity, and what it does, unless the Chairmen want to explain it right now.

REP. BARRY: The Commissioner is right, I mean, with respect to that transaction. I've had that same situation occur where someone has reported to me directly. People would say to you, hey, how're you ever going to prove that this is the

case, that someone is trying to inflate an appraisal.

We have, part of House Bill 5577 is prohibiting mortgage brokers from putting undue influence on appraisers. And another provision involves real estate agents doing it, and the real estate provision may be similar to yours that you have in Insurance and Real Estate.

It may be something that doesn't need to be in this bill or needs to be in this bill, because I wanted to make, you know, the Chairs want to make sure that that was covered.

But as far as your particular scenario, you know, if the Commissioner is stumped without more facts, I think, I mean, I'm not going to answer it any better than he would.

COMM. HOWARD PITKIN: Representative Harkins, if you will call me, I'll, and give me the facts, I will certainly follow-up on it, and if we have any jurisdiction, I'll exercise it.

REP. HARKINS: Dealing with the appraiser, probably following a concern with protection of their certification, but if the broker is out of state or in Rhode Island, we don't have any recourse, though. I mean how do you--

COMM. HOWARD PITKIN: Did the transaction take place in Connecticut?

REP. HARKINS: Yes. Because, the appraisal assignments would have been in Connecticut,

Rhode Island, Massachusetts, but they would include our state.

COMM. HOWARD PITKIN: Well, we can, I can talk to Commissioner Farrell at DCP and see if he has any jurisdiction over that. I mean he does regulate appraisers and real estate agents in that part of the industry, so I'd be happy to do that for you.

REP. HARKINS: Okay.

COMM. HOWARD PITKIN: Another thing you mentioned was these schemes where, you know, I've got this sign at the bottom of my drive way, you know, will buy your home within 24 hours [inaudible] you know, give us $1200 or $1500 and we'll work this whole thing out for you.

You know, I'll only say that these companies never deliver their promises. Never. They'll buy your home. They'll have you sign it over to them with a Quit Claim, and with a promise they'll rebuild your credit and you can get back in your home a year later.

And then they'll drain the home of your equity and leave you holding the mortgage, but then you're out of a home. If somebody's got money to pay one of these companies to bring resolution to a troubled mortgage, they should put that money on their mortgage, not to a company that's peddling these services.

And you know, I would hope that all of us, if we can get this word out to the public. It's vitally important. Panicked people make very

poor decisions. We have wonderful housing advocacy agencies here in Connecticut that are certified by Housing and Urban Development.

And we have to steer troubled families and borrowers over to them so they don't make these mistakes.

REP. HARKINS: One of the other issues, Commissioner, is the whole issue of enforcement, and recently I was involved in a situation where an out-of-state bank was using real estate agents to do broker price opinions for home equity loans which is illegal in the state of Connecticut.

This one agent we found out, we ended up turning him in to Consumer Protection. They brought him in and they reprimanded him with a Cease and Desist. That's it. I mean it's almost like it's a joke. You know. It's, they're going to continue to do it.

They know they're not supposed to be doing it. They're going to continue doing it if there is no penalty in place. The one thing I'd like to see, and I know we've talked about this before, that no one likes to go fishing or go into places looking for things unless there's an actual complaint involved.

But I'm at the point now where I'm starting to think that we do need to look a little harder and be a little bit more aggressive, because the word on the street is it is a joke. There is no enforcement. And that's on the real

estate agency side, but also the mortgage brokers.

I mean, it's unbelievable the calls that I've received from some of these people. I mean it's worse than used car sales people. Most of them out of state by the way. But they're laughing.

They made the money and they're laughing at the expense of citizens here that, quite frankly, don't have the wherewithal or the financial ability to make decisions with some of these documents, and it's heartbreaking.

I know you hear the same stories I do and you deal with it, and your department has done a great job addressing this, but I would really like to see more. I mean if it's more funding the department needs to get more auditors out there or more reviewers to do investigations, let's do it.

But if we're going to do something here as a committee, and if we're going to do a bill, let's do it right, because just passing a law doesn't change anything.

And I hate to use it, but the cell phone ban is a perfect example. It's an absolute joke. You know, we talk about driver safety, but we really don't do anything about it.

Today on 91, I saw a whole bunch of troopers pulling over trucks. I was glad. As cars are still going 85 miles an hour past me, but you

know, and I do know there is a point where you can only do so much.

But if people know there is ramification and penalties in place for doing something wrong, that's when they're going to think twice about it. We can pass all the laws in the world.

If we don't go after the people, fine them, or put them in jail, it doesn't, it doesn't do anything. I mean it's nice to have a press conference and to have the TV cameras here and to say, we're doing something.

But at the end of the day we really have to be proactive and actually go out and do the investigations and actually make progress and stop people from doing this and put the word on the street that we are serious in Connecticut.

COMM. HOWARD PITKIN: I think, I couldn't agree with you more. I think Senate Bill 21 gives us the regulatory scheme we need to regulate this industry better, the non-bank mortgage industry.

And right now, there is a disparity between the two industries in that the banking industry and the depository industry, federally insured institutions, have such huge compliance costs. It's their biggest expense.

And they have exams regularly, and every mortgage folder is looked at to make sure that they have complied with laws, both by federal examiners as well as our own.

The other side of it is that the non-bank mortgage industry has little cost of compliance, because frankly, it has just never been the way that we regulated this industry.

Now, however, we are adopting examination principles, techniques. We're going to train our examiners in using the National Mortgage Licensing System, which we think is a huge step forward in consumer protection, and we're transferring some examiner resources, people with a lot of years of experience from the divisions they were in that don't have a crisis going on, down to the consumer credit area which does have a crisis going on.

And to get this examination going, and to examine a prudent number of them every year, and to make sure they're on a regular cycle and to deal with situations similar to how we deal with banks.

If somebody's lending money in an unsafe and unsound way, I can assure you they'd be stopped.

REP. HARKINS: Commissioner do you have the resources necessary to be more aggressive in implementing the laws in our state.

COMM. HOWARD PITKIN: I think I'm trying to use the resources that I've got, and I would like to get back to you on that. I'm not sure that I can say definitively if I can do all of this, because, in transferring resources, and here's another thing. A lot of these companies are from outside of Connecticut.

The states are arranging agreements just like we did with the banks, and that if somebody is out of state, our examiners can, can meet there along with other examiners and examine that company and their Connecticut lending.

And I just spoke with Marlene Mannix this morning who is a manager in our Consumer Credit Division, and she told me that the first such situation is being planned right now. So, you know, I want to use the resources I've been given, and you know, we have a high level of experience.

You know, typically in state employment, everybody complains, nobody leaves. And, I have people that have high levels of skill, and I think we can bring this industry up a level as far as the reparations go and how they approach the public and enforce the laws we have. Enforcement is the key here.

REP. HARKINS: I agree with you 100%, and the history of State government, unfortunately, is we react most of the time. And, you know, whether it's transportations issues or banking issues or any issue with State government, that's just the way it has been.

We do try to be proactive, and it always doesn't hit the mark. In this particular case, I know you're in a situation where we're working through a budget, and I know you have concerns about spending money and maximizing the staff in your department.

However, if we're going to be serious about what we're trying to propose about enforcement, I couldn't think of any other place to actually beef up some staffing and be a little bit more aggressive in enforcing our laws. Particularly given the impact it has had on people's lives here.

I mean, you know, we talk about some of the issues we deal with in State government. I mean, this is horrific when people actually lose their homes and have to go bankrupt.

I mean, it's good for the bankruptcy lawyers, I guess, and maybe real estate agents that get to sell these properties, but it really is a travesty.

And the one thing State government should be doing is protecting people, and looking out for their best interests particularly when it comes to predators such as mortgage brokers going out trying to use these people and drain them of resources.

I thank you for coming today and giving your testimony again, and I'd also like to thank the Chairs for taking this issue very seriously and coming forward with a proposal also.

Hopefully, we can get a combination of both, and it sounds like we're going to get a bill out of here that's going to address this very important issue, so thank you.

COMM. HOWARD PITKIN: Thank you, Representative Harkins.

REP. BARRY: Thanks very much, Representative. Senator Duff.

SEN. DUFF: Good afternoon, Commissioner. How are you?

COMM. HOWARD PITKIN: Good afternoon, Senator.

SEN. DUFF: Thank you for being here again, and for taking the time to testify on a few of the bills. I had a question for you in light of, well, let me just, let me back up a little bit.

With regard to the summertime with some of the sub-prime loans. How many sub-prime loans do you expect to reset this summer and maybe even next year?

COMM. HOWARD PITKIN: Not to evade your question, I'll give you answer and then bring it back to Connecticut. It depends who you listen to.

This group that was formed by the AG's and the State regulators that OCC would not participate in said that seven out of ten borrowers, this was as of October of 2007, seven out of ten borrowers were not involved in lost mitigation of any kind.

That payment resets were not yet a factor in foreclosures, because they were behind on their payments anyway. Homeowners are helping themselves more often than not and somehow paying their loans, those that can bring them up to date, and refi's may no longer be the

solutions unless the lenders can, you know, style new products that will help life go on.

I have a report in front of me that factors impacting foreclosure starts and 61% here in Connecticut are tied up and borrower defaulted despite previous, borrower would not respond.

That's 19%, so one out of five is out there not even responding, and 13% are no longer occupied by the owner.

I mean, I'll submit these two reports to the committee today. I think, my opinion is that having looked at the figures as of 9/30/07 as compared to when we did our task force report, there is not enough modifications going on.

Everybody is trying to work with the servicers, and they're dealing with one case at a time where it has got to be done more rapidly than that in order to save as many homeowners as we can.

SEN. DUFF: Okay. Thank you for that information. What I'm trying to get at is, and I know that it may not be an exact number, but are we talking 10,000, 20,000 mortgages that could be reset, 50,000?

COMM. HOWARD PITKIN: We have roughly 70,000 of these loans, and not all of them are past due. You know, roughly 80% are paying as agreed somehow. The other 20% need some attention, and of those 20, which I believe is 21,000, you know, something fast has to be done, I believe.

To deal with them one by one is just not the way to do it.

SEN. DUFF: Right. Okay. So what you're saying is that there is 21,000 potentially that are resetting this summer. There's another 50,000 more people may be okay, but we may just not have that information. That's according to what you said last week as well, correct?

COMM. HOWARD PITKIN: Correct.

SEN. DUFF: Would it be fair to say that there is 30,000 or 40,000 maybe of the loans, forget about being foreclosed on or if they are current, but that are going to reset by June or July of this year, which is when we're looking at when the bubble is going to hit.

COMM. HOWARD PITKIN: The resets?

SEN. DUFF: Yes.

COMM. HOWARD PITKIN: The resets. There is going to be 21,000 loans that are going to reset before the end of this year.

SEN. DUFF: And what about for next year? Do you know?

COMM. HOWARD PITKIN: It will be an equal number, because these reset generally on an annual basis.

SEN. DUFF: Okay. In light of then your opposition to House Bill 5577, what then, and your being for Senate Bill 21, what then are we doing as a

State, because in House Bill 5577 we have some procedures in place to try and deal with the now.

I think what we've talked about is the now and then the future, and I think Senate Bill 21 takes a look at now going forward so that we don't get into these kinds of complications in the future.

What are your proposals to help deal with the now, the 21,000 people, and how that affects our economy, how that affects our neighborhoods, how that affects individual homeowners, and the entire state as a whole? How do your propose to deal with those 21,000 people?

COMM. HOWARD PITKIN: I believe that the Connecticut Families Program, which was begun by the governor, given some time to work will take care of, I believe, up to 400 families and will grow over time as those families begin to repay those loans.

The Federal Government has come out with three or four programs which, in my opinion, haven't gone far enough, and we need some sweeping legislation that is going to bring the Federal Government to bear on the national problem.

I don't know of any state that has the financial girth to address this entire problem. And the thing that we tried to do in the task force that we were in was to try to use non-taxpayer money, and we tried that and I think

that the pre-element money that CHFA came to the table with is just that.

And it's a noble purpose to use money for, I believe, and can help a great many families. Does the program need to be tweaked or changed? Yeah.

But you have to bear in mind that underwriting standards change hourly in the marketplace, and it's very difficult to just have one set of specs and make them apply to a whole market that's troubled.

So I think that's a beginning, Senator. The three opposing, not opposing bills. I don't feel that they're opposing each other. I don't think in the case of legislation of this type that there is good or evil or good or bad.

I do think that I want to sit down with the parties and talk about these bills and that we can put together the right consumer protections and the right lending principles and rules to protect not only the industry and regulate the industry the right way, but to protect our public.

SEN. DUFF: Okay, thank you Commissioner. I think we can also ask those questions of Michael Ward when he comes up for CHFA, but are you testifying today that you think when there is 21,000 potential resets out there that helping 400 families, is that adequate?

COMM. HOWARD PITKIN: No.

SEN. DUFF: Okay. Thank you.

REP. BARRY: Are there any other questions by Committee members? Okay. Thank you very much. You're relieved of duty.

COMM. HOWARD PITKIN: Thank you very much.

REP. BARRY: Thanks for coming. Okay, at this time more than an hour has gone past, and we're going to be switching over to the public sign-up sheet, and we're also going to be instituting a three-minute rule.

We have, someone has a bell in this room, an oven timer or something. We're going to start off with Erin Kemple from the Connecticut Fair Housing Center.

HB5577
SB21

ERIN KEMPLE: Thank you very much for allowing me to speak today in support of Senate Bill 423, AN ACT CONCERNING FORECLOSURE PREVENTION AND RESPONSIBLE LENDING.

I have brought my colleague, John McGrath, with me today, not to speak except for to whisper in my ear and help me answer questions, because for the most part, I'm just a pretty face.

I'm the executive director of the Connecticut Fair Housing Center, a statewide organization that has been receiving an overwhelming number of complaints from consumers and borrowers who are either in foreclosure or in danger of going into foreclosure.

As a result of this, the Connecticut Fair Housing Center has been working with advocates nationwide as well as throughout the State to craft a bill that would attempt to stop the foreclosure crisis from happening again.

We are very appreciative of the co-chairs' bill, House Bill 5577, and the information in there and the proposals in there to regulate the lending industry as well as Senate Bill 21, which you just heard a lot about from the Department of Banking.

There is much that we agree with in both of those bill, but I would like to use my time today to highlight a few of the differences and really talk about the need for regulation of the sub-prime industry here in Connecticut.

Senate Bill 423 primarily regulates mortgage products that increase the risk of foreclosure. This includes not just sub-prime mortgages, but also nontraditional mortgages.

Nontraditional mortgages are things that are, mortgage products that are sometimes at a prime rate, but that include terms such as an option arm or other types of risk enhancing features that, and both of these are not regulated by Senate Bill 21 or House Bill 5577.

According to the Interagency Guidance on Nontraditional Mortgage Product Risks, more than traditional arms mortgage products such as payment option arms and interest-only mortgages carry a significant risk of payment shock and

negative amortization that may not be fully understood by consumers.

In other words, nontraditional mortgages carry the same types of problems that we are now encountering in the sub-prime market.

Secondly, we would like to ask that all discount points be included in the annual percentage rate. Currently what is proposed in House Bill 5577 is to exclude bona fide discount points from the calculation of the APR.

Exempting such points will provide originators with an incentive shift costs into points making interest rates deceptively low and the cost of credit opaque and avoiding important consumer protections for costly loans.

In addition, the definition of Annual Percentage Rate has long been established by Federal Law and includes any discount points. By changing the definition, Connecticut will create an unnecessary compliance burden.

I can tell that my time is up, but let me just say that we welcome any comments from the Committee, and would like to work, as Commissioner Pitkin just said, to ensure that there is a strong bill that protects all borrowers, and finally that there is also a private Right of Action.

Many of the questions that were asked here today are about how the Commission on Banking could enforce the laws, and one of the things

that we have seen in our practice is that the only thing that consumers can use in order to protect themselves is a Private Right of Action, an action which they can bring or use as a defense to foreclosure violation of the bill. Thank you.

REP. BARRY: Thank you very much, Erin Kemple. A few questions. I was just looking over your written testimony, which is very helpful, because we have a three-minute timer. It's helpful to the Committee members.

I personally asked you, when you're here, I know you were in the audience when the Commissioner was testifying about, and then I think it was, it was Representative Ryan or Harkins who was asking about, it was Ryan actually, Representative John Ryan, asking about his, if there is any precedent in other states for banking commissioners to have the ability to impose any type of a moratorium on foreclosures.

I thought I read where there are states that have given that authority to a banking Commissioner, but I just was wondering in your area of expertise if you have anything to lend to that.

ERIN KEMPLE: The only one that I know for certain is the State of Massachusetts, and I believe in that case it is the Attorney General, and not the Department of Banking that has imposed the moratorium.

All the other moratoriums that I am aware of are voluntary moratoriums. But there are people who are more aware of what's going on on a statewide, on a nationwide level that may be able to answer that, particularly Uriah King.

REP. BARRY: Is this the, I read an article recently about Massachusetts. Is the Attorney General there Coakley?

ERIN KEMPLE: Yes.

REP. BARRY: And is this a more recent law? Something that's come down in the last year or two, or has it been around for, you know, since their State Constitution?

ERIN KEMPLE: My understanding is that the Massachusetts law allows the Attorney General to regulate, to a large extent, a lot of the consumer issues having to do with sub-prime borrowing, and that the Attorney General has used that to impose the moratorium ban and to promulgate regulations.

So Massachusetts is not having a bill go through the legislature the way we are here in Connecticut, because the Attorney General has been able to do much of what we are proposing by regulation.

REP. BARRY: Okay. So it's outside of the courts. It's with a Constitutional officer, but it's not with the Department of Banking Commissioner in Massachusetts. Is that correct?

ERIN KEMPLE: That's my understanding. Yes.

REP. BARRY: Okay. And then with respect to the, you refer to the Interagency Guidance on Nontraditional Mortgage Product. I think I read that. Is that the Federal Register?

ERIN KEMPLE: It's the Federal Reserve, the OCC, the Office of the Comptroller, the Currency, and the FDIC.

REP. BARRY: It's all their interagency, its opinion based on interagency discussions [inaudible].

ERIN KEMPLE: Yes. That is.

REP. BARRY: All right. There are several years of them, and I can't remember which one I saw this exact quote in.

ERIN KEMPLE: I can get you the year and the exact wording--

REP. BARRY: I have it. I know I have I t.

ERIN KEMPLE: Okay.

REP. BARRY: What types of, where it says, more than traditional arms, mortgage products such as payment option arms, interest only mortgages can carry significant risk of payment shock, negative amortization that may not be fully understood by consumers.

I understand that, and I guess my question to you is, there is a lot of these nontraditional mortgages are very helpful to different types of people whether, obviously some sophisticated

borrowers would like to, maybe make some more money, and they take all the equity out of their house, and they get a no-interest loan.

And as an attorney I would not advise that person to not do it, if I know that person knows what they're doing, and they're going to make a lot more money by paying, you know, 4% interest on that and getting 12% in the marketplace somewhere else.

What type of regulation then would you impose on nontraditional mortgages as a result of your reference to that Interagency Guideline?

ERIN KEMPLE: Those are the same regulations that we include on some of the sub-prime mortgages such as prohibition on churning, meaning refinancing without a net benefit to the borrower, disclosures, mandatory escrow, some of the other things.

It would definitely not ban those nontraditional mortgages. It would simply provide greater protections to ensure that non-sophisticated borrowers are not being sold those kinds of products at a prime rate.

So it really would not, I think really, it would also ban pre-payment penalties on them, and so I think that it would, it would simply regulate. It wouldn't ban them.

REP. BARRY: What's your understanding of the effect of banning a pre-payment penalty on a nontraditional mortgage?

ERIN KEMPLE: My understanding is that if someone gets into a nontraditional mortgage, even a sophisticated borrower expecting for instance to be able to move within a two-year period, that they would be in a difficult position of paying the mortgage off if there was a prepayment penalty, because they would have to not just pay the mortgage off, but also any prepayment penalty.

So it would protect borrowers, even sophisticated ones, from a change in circumstances that they couldn't foresee at the time that they took out the loan to allow them to prepay the mortgage.

REP. BARRY: Okay. I'm going to ask the question in a different way. What's your understanding of the purpose of a prepayment penalty in a nontraditional mortgage from a banker's point of view, or a lender's point of view?

ERIN KEMPLE: My understanding is that a prepayment penalty is supposed to give the borrower something as well as the lender. So the borrower should be getting a better interest rate or some other type of advantageous terms of the mortgage, and yet we're not necessarily seeing that. Yes. They may qualify for a prime mortgage, but they may have qualified for a prime mortgage anyway, based upon their FICO score.

REP. BARRY: I always thought it was a little more sophisticated than that, but what you're pretty much saying to sum it up in a nutshell is, it's a quid pro quo situation.

ERIN KEMPLE: Yes.

REP. BARRY: Okay. With respect to banning certain loans that greatly increase the incidence of default. You didn't mention that. You ran out of time there. Can you explain that a little?

ERIN KEMPLE: It's certain loan terms, not certain loans. The loan terms would be prepayment penalty, balloon payment, negative amortization, and default interest rates, and that would only be for sub-prime and nontraditional mortgages.

REP. BARRY: Okay. Not for prime. What about for nonprime as defined in House Bill 5577?

ERIN KEMPLE: We generally agree with the definition of sub-prime as it appears in House Bill 5577 with two caveats. One is that it doesn't include the nontraditional mortgages, and second that it does not include the discount points in the definition of APR.

REP. BARRY: Okay, and with respect to the exclusion of the discount points in APR, how does that work with TLA right now, or the Truth in Lending Act? How are discount points, what is the relationship between a discount point in TLA right now?

ERIN KEMPLE: I'm looking at my colleague here. My understanding is that discount, and the definition of APR under TLA, the APR includes discount points, but you're going to have to

ask somebody who comes after me who's a little bit more knowledgeable about TLA than I am.

REP. BARRY: That's fine. And then with respect to Private Right of Action, do you have any objection to the Fiduciary Duty Language?

ERIN KEMPLE: We do not have any objection to the fiduciary language in House Bill 5577, and we do like the fact that House Bill 5577 includes a Private Right of Action and also assigning liability.

One of the misunderstandings is that assigning liability as it is currently proposed in House Bill 5577 or Senate Bill 423 would be unlimited, which is what I believe they had down in Georgia. We're not proposing assigning liability that is unlimited.

It is assigning liability limited to the amount of the mortgage itself if that is what needs to happen in order to allow for rescission or other type defense to foreclosure.

REP. BARRY: Okay. And the last question. You mention as one of your bullets here, prohibit lending without verification of the borrower's reasonable ability to repay the loan. Why do you think that's so important?

ERIN KEMPLE: One of the things that we have seen is that a lot of borrowers are approved at a teaser rate or an introductory rate for a mortgage so that when the loan resets in six months or one year or two years that they are not able to pay the reset.

And one of the things you heard from Commissioner Pitkin is that 21,000 loans will reset within the next year to 18 months, and we are concerned that we don't want that kind of reset happening without an ability to repay based upon the fully amortized, the fully indexed rate meaning the cost of the loan itself after resets.

REP. BARRY: So than based upon what you just said, I assume you're just talking about sub-prime loans, because that's what the 21,000 is.

ERIN KEMPLE: That is what we are talking about. We do agree with the ability to repay language that is contained in House Bill 5577, and we think that that's very similar to what we've proposed.

REP. BARRY: Okay. Thanks very much. Anyone else on the Committee? A little comic relief from Representative Ryan. Thank you very much. It's pretty dull stuff here. Senator Kane?

SEN. KANE: Thank you, Mr. Chairman. I do have just a couple of quick questions. Senate Bill 21 and House Bill 5577 are addressing the sub-prime crisis as it's referred to, and you mentioned in your testimony that you would like to see it go further into nontraditional mortgages.

My question to you is haven't we had nontraditional mortgages for years and years and years, and have never had a crisis like we're talking about in sub-prime, so what is

the need to go after nontraditional mortgages when the issue here is being addressed that's currently underway?

ERIN KEMPLE: I think because the nontraditional mortgages are being used in a different way than they have been in the past in that they are being sold to non-sophisticated borrowers.

Sometimes they're called exotic loan products, and--

SEN. KANE: Not to interrupt you, but I'd like you to define that. What's a non-sophisticated borrower?

ERIN KEMPLE: A borrower who is entering into the market for the first time. Maybe they're the first time in their family history who have owned a home.

They do not have the ability to actually compare the mortgages that are out there and that are being offered. They don't know to ask questions about what does this TLA Disclosure mean when it says that my payment after 15 years is going to be $75,000. They don't know how to look at those documents, and yet they're being sold loans that have information that they don't understand.

SEN. KANE: Isn't that what your organization, or CHFA does for these people though?

ERIN KEMPLE: One is that my experience is that the majority of borrowers don't come to my organization or to CHFA or any housing

REP. MCCRORY: Well, now you lead, that's a whole other conversation in regard to redlining and everything else. But first we've got to get through the fact that individuals qualified for loans are not getting what they're supposed to do, and then we'll have another discussion about redlining the neighborhoods and all the other stuff. But thank you for your answers.

ERIN KEMPLE: Thank you very much.

REP. BARRY: Deputy Speaker. Representative Kirkley-Bey.

REP. KIRKLEY-BEY: Thank you. Thank you, Mr. Chairman. I want to ask you a question, and you may have answered this, and I apologize, but I had to testify in another Committee, and they went on forever.

But in the case that you just cited where you said that if you found out that a mortgage dealer was steering people toward sub-prime while they may have qualified for regular mortgage, what do you do?

ERIN KEMPLE: One of the options that we will consider is litigation.

REP. KIRKLEY-BEY: Litigation against that person.

ERIN KEMPLE: Yes.

REP. KIRKLEY-BEY: My question is, I was hoping you'd say that. My question is do you go back and look at their portfolio to see if there are

people who have been taken advantage of that that wrong is righted?

ERIN KEMPLE: Absolutely. That is one of the reasons why we take litigation of these kinds of cases very seriously.

We usually look at them not just on behalf of one particular individual or one particular instance of discrimination, but changing the way that particular lender or other housing provider does business to make sure it does not happen in the future, and to compensate anybody who has been victimized in the past.

REP. KIRKLEY-BEY: Thank you.

REP. BARRY: Any other questions for Erin Kemple? Representative Moukawsher.

REP. MOUKAWSHER: Thank you, Mr. Chairman. I may have missed your emphasis on this earlier in your remarks, but reading your written submission, you identified one problem in persons getting higher interest loans than they should as the Yield Spread Premium, which is a compensation to brokers.

ERIN KEMPLE: Yes.

REP. MOUKAWSHER: How much do you think that single incentive for brokers has contributed toward, you know, this sub-prime problem?

ERIN KEMPLE: One of my colleagues who is going to testify in just a few minutes, Andrew Pizor, can give you the specific statistics.

But certainly in the loans, the sub-prime loans that I've looked at, the majority of them had Yield Spread Premiums in them, and they contribute to the higher cost of the loan itself, because they're usually not included in the definition of, in, in the costs and fees that are charged.

So the cost of the Yield Spread Premium tends to be high.

I've also seen cases in which the Yield Spread Premium has been financed as part of the mortgage as opposed to having the borrower pay it directly, and so they're really being charged almost twice for that, because they're paying interest on the Yield Spread Premium that they're paying to the borrower.

REP. MOUKAWSHER: All right. And the higher the interest rate, apparently the greater commission that a broker earns apparently if there's that feature.

ERIN KEMPLE: Yes.

REP. MOUKAWSHER: I wondered when Representative McCrory was speaking before about someone who would have qualified apparently for an ordinary mortgage, whether that incentive was a reason that this person was steered to something that was not in a sub-prime type mortgage as opposed to an ordinary mortgage.

ERIN KEMPLE: Well, I do think that the higher interest rate the more compensation is for the

broker [Gap in testimony. Changing from Tape 1B to Tape 2A.]

--the agreement that they had with the lender. But there's also, I think a larger question as to why do you only want to make money off of African Americans or Latinos and not Whites.

You know, in other words, why steer an African American or a Latino person, which is part of what we're seeing in our, in our testing, to a higher cost mortgage, and not everyone.

And certainly, it's true that lots of people have been steered to higher cost loans. I heard Freddie Mac speak and what they estimated is that a third of the people in sub-prime loans should have been in prime loans, had credit scores or FICO scores which would have gotten them qualified for a prime mortgage.

REP. MOUKAWSHER: Well, thank you for that statistic. I was going to ask you, because I think the color that's important is green in this, and it seemed like, you know, there would be just as much incentive to steer anybody if a broker can make a higher commission.

And people do, you know, have the impression that the broker is working for them, getting them the best available mortgage, and apparently that hasn't happened.

ERIN KEMPLE: Yes. That's true, and I think that part of what House Bill 5577 as well as Senate Bill 423 do is try to really alter the relationship between the broker and the

borrower to make it clear who the broker owes a fiduciary duty to.

REP. MOUKAWSHER: Okay. Thank you very much.

ERIN KEMPLE: Thank you.

REP. BARRY: Are there any questions, any other questions from Committee members? Okay, thank you very much. Thanks for the work you do. Thanks for coming here today.

ERIN KEMPLE: Thank you.

REP. BARRY: Okay. At this time, I know that Representative Minnie Gonzalez is in here, and I just want to hold off on you. You'll be next. But I'm going to call the Commissioner, Commissioner Pitkin back up. He has requested to clarify something that he had said earlier in his testimony. Thank you.

COMM. HOWARD PITKIN: The last question dealt with the 21,000 resets that are likely to occur in the sub-prime area over the next 12 months, and in view of those 21,000 resets was the Connecticut Families Program adequate enough.

I didn't answer that correctly. I guess maybe my mind just wasn't dealing with it, but if you extrapolate the 8% 90-day past due in foreclosure rate right now, on that figure you would wind up with about 1600 borrowers who, facing the reset might not get through it and default.

I think the Connecticut Families Program is very adequate in terms of that number of borrowers.

REP. BARRY: Did anyone have any questions?

COMM. HOWARD PITKIN: Thank you, Mr. Chairman.

REP. BARRY: Thank you.

REP. GONZALEZ: Good afternoon. I want to clarify that I have here with me Mr. Nick Carbone. He is not a lobbyist. He has just been working with me on this bill, and any questions that, you know, I want him to help me with the answers.

I think that he can, he has been very involved in this for a year.

REP. BARRY: Very well. We understand.

REP. GONZALEZ: Okay.

REP. BARRY: Thank you very much.

REP. GONZALEZ: Chairman Duff, Chairman Barry, and Honorable members of the Banks Committee, I wish to express my strong support for House Bill 5577, and I would like to thank the chairmen and Committee Members for bringing this proposal forward for a public hearing.

However, I would like for you to consider the following concepts to be included in this bill: Predatory sub-prime lenders have issued

mortgages without such escrow accounts which forced the purchasers into tax foreclosures.

Purchases were unaware that the escrow accounts were never opened. I believe all mortgages which do not have an insurance and property tax escrow account should be outlawed.

Predatory lenders have also been found to have used unscrupulous practices amounting to deception and even fraud. We should require stricter license and regulation of all mortgage brokers and their agents.

This includes: And I would say that one of the questions that was before was, how can we enforce this? And I would say, 1) all must be bonded, 2) all must maintain an office within the State of Connecticut, 3) brokers must have a net worth of at least $10 million or must have posted a surety bond for that amount.

That's how I think that we can enforce this, how we can enforce the predatory lenders. 4) Agents must post a surety bond equal to the mean single-family house price in Connecticut as posted by the State Banking Department each year.

5) Agents must have at least four weeks of training including ethics classes. 6) All brokers and agents must have additional background checks.

Predatory lenders have also issued mortgages to borrowers with no documentation of their income or ability to pay the mortgages.

Proper underwriting standards must be required to ensure that potential borrowers can meet the 30% standard at the highest interest level that the mortgage can attain.

It must be required that no mortgage may be underwritten with payments which exceed 30% of the borrower's household income. Such payments must include all principle and interest, property taxes, insurance, and all utilities.

In distressed cities and communities, FHA underwriting standards must be followed. Additionally, predatory lenders offered mortgages to unqualified purchasers at low teaser rates.

Those rates would quickly escalate to unaffordable levels, and the prepayment penalties would make it impossible for the purchasers to pay off the original mortgage.

The prepayment penalties that predatory lenders require, which have been outlawed in other states need to be outlawed here in Connecticut.

The governor's task force reported that it is estimated that there are about 71,000 active sub-prime mortgages in Connecticut with outstanding balances totaling more than $15 billion. Over 8% of these are mortgages are now seriously delinquent.

The task force also reported that there is a concentration of sub-prime mortgages in communities with a higher than average number

of low and moderate income households, minority households, and affordable single-family housing.

I also, in my package you will find a flier like this. This flier says: Big money maker! Live Rent Free! Owner Financing! No Money Down! Good Credit/Bad Credit/No Credit. 100% Financing, No money down, owner pays all closing! Free moving expenses! And then on the side, We Speak Spanish. Se Habla Espanol!

And then on the side you can see that they are passing these fliers, Hartford, Waterbury, New Britain, Meriden, New Haven, Bridgeport, Hamden, Bloomfield.

And I was a little bit surprised when I saw West Hartford. But this is the poor area of West Hartford. So they are targeting Latinos and African Americans.

And one of the questions before was why they are targeting Latinos and African Americans and why not Anglos. I will say that it's because the experience, the language, the money, and our programs.

Representative McCrory says, well, the question was what is the advantage to refer this, when a person qualified for a regular mortgage, why then refer them to a traditional mortgage, and it's the commission.

They know that with a traditional mortgage they will get more commission maybe with a regular

mortgage, and that's why they are doing, they are, they referred those cases.

The Commissioner, he said that he supported Senate Bill 21, and I will say that Senate Bill 21 may have, I'm not saying that it's a bad bill, but we want to resolve the problem for now and the future.

And I really believe that House Bill 5577, it will do both, that we can work together and improve House Bill 5577 or maybe Senate Bill 21. Yes, it's possible. I think that we can work together.

We want to solve the problem now, it is no problem working through and we can work together. I think that we all want to be part of the solution, not part of the problem.

And Senator Harkins, he was saying how can we enforce this. How can we resolve this problem, and that's where House Bill 5577 says broker must have a net worth of at least $10 million or must have posted a surety bond for that amount.

I think that that is one of the ways that we can enforce this, and also having an office in the State of Connecticut. I think that this is a couple of things that we can do to enforce this.

And, any questions, I have my buddy here to answer any questions.

REP. BARRY: Thank you very much, Representative Gonzalez, and I certainly appreciate your zealous advocacy for especially people you represent in Hartford, a lot of low income and minority population that is, you know, have been very much on the bad end of the sub-prime loans.

And those are the people that have been taken advantage of, and I think those are the people that for the most part and in many respects, they probably should been more represented on the governor's task force.

Then maybe we'd have a better refinancing program today with CHFA if the people, a lot of the people you represent were represented on that task force. So with that, if anyone has any questions. Representative Kirkley-Bey.

REP. KIRKLEY-BEY: I'd like to ask a question, and it can be answered by either Representative Gonzalez or Mr. Carbone or anybody on this panel.

25 years ago when I bought my house, I had my own realtor, I had my own attorney. The person who was selling their house had an attorney. There was somebody there that handled the closing and the costs and all that for the two of us.

In this sub-prime mortgage, are those entities or some of those entities missing?

REP. BARRY: I'm sorry. Can you repeat the question?

REP. KIRKLEY-BEY: I think--

REP. BARRY: Oh, yeah. Sure. I'm sorry.

NICK CARBONE: The answer is, if you look at the flier, when they say the owner pays all the closing costs, and we found out, and I've gotten phone calls on it, they discourage you from having your own attorney.

The attorney at the closing produces the paper. You're ready to move in the house, and then you find out you didn't get a fixed rate mortgage that you had thought you applied for, and you got a teaser.

So the answer is the attorney is missing. And one of the weaknesses I would have is I would have an outside attorney have to be represented in this non-banking industry, and it should be a Connecticut attorney.

Because they have had also title companies coming in from out of state with an attorney handling the closing and the legal representation of people before the borrowing Connecticut who have a license at stake are missing from the table.

REP. KIRKLEY-BEY: You brought something to mind, Mr. Carbone. I did have someone who was a title person. I had someone who came from, I don't know if it was L&I or something to check out all these different things in the house.

counselor before they get a mortgage. They find the house. They fall in love with the house.

They really want to buy it, and they are getting a hard sell from a lender saying, yes, it can be yours, without understanding all of the different pieces.

The lending market has gotten so much more complicated since the sub-prime market grew up, and as part of that, the nontraditional mortgages have gotten much more complicated also.

SEN. KANE: Don't these nontraditional mortgages give people an opportunity to buy a home where they otherwise couldn't?

ERIN KEMPLE: That may be true, but one of the things that we have found is as a result of the current foreclosure crisis that we've actually had a drop in the number of homeowners.

African-Americans and Latinos in particular have had a drop in percentage of home ownership among those groups, because of being taken advantage of by some of these both exotic loan products as well as the sub-prime loan products.

SEN. KANE: So now, now we're using the term exotic home product?

ERIN KEMPLE: That, that, I'm sorry. Sometimes lenders use exotic loan products as well as nontraditional to denote a mortgage product

that is something other than a 30-year fixed rate or a typical arm.

SEN. KANE: But is it not true that we have not had issues with the nontraditional mortgages historically?

ERIN KEMPLE: I don't think we've ever seen the number of nontraditional mortgages that we have, but I think when there was just a very few people getting nontraditional mortgages, you're right.

Because it was mostly given to people who were in construction, or were, my parents have an interest-only loan. My father is a retired attorney, he, you know, did closings for his entire career.

He completely understood what he was getting into when he got an interest-only mortgage, and yet I was yapping at him, don't do it, don't do it, don't do it.

He understood much better than I did exactly what he was getting into. And those are the people who have traditionally been given the option arms, or the interest-only mortgages.

SEN. KANE: Okay. Thank you, Mr. Chairman.

REP. BARRY: Thank you very much. Representative McCrory.

REP. MCCRORY: Thank you, Mr. Chairman. Question, or maybe it's a comment in regard to some of the literature and the high percentage of

individuals, African-American, Latinos, and white, well dis, it's not disproportionate, but it's spread across the board. However, it affects some communities more so than others.

I guess this is one of the concerns I had, and I did some research on it, and it has been written about also. I got two phone calls within the past three weeks in regard to the sub-prime, what's going on in the sub-prime market, and this is what happened.

I had an individual go in to apply for a mortgage. They did everything they were supposed to do. They were told they didn't qualify, but the reality was after all the work was done, they took the information to another attorney.

They were coerced into purchasing a sub-prime mortgage when they actually qualified for a traditional mortgage, and of course, now we are where we are.

But the reality was they did qualify for a traditional mortgage. What can we do to prevent such collaboration with mortgages, realtors, and mortgage, you know, purchasers when situations like that happen? Because, you know, it, good, I'll let you comment.

ERIN KEMPLE: That's how my agency got into this whole sub-prime work in the first place is that our experience was that African Americans and Latinos were getting a disproportionate number of sub-prime loans, and while that may not be true, one of the things that we have done is

testing of the mortgage lending market in order to determine if people of color are being steered to high cost loans.

We will have a report coming out by the end of the year that details the results of that testing. What we've done is we've asked African American and Latinos to go in. They have good credit, never had a 30-day late. They ask for information about a 30-year fixed rate mortgage.

What we're finding is that they are being quoted higher interest rates than similarly situated whites.

Similar income, same credit score, and so we will be putting out a report on that, and we are currently looking in my agency about what we can do to try to address this issue on a statewide basis, because we do believe it is a problem.

REP. MCCRORY: Because you're doing a study, do you foresee there is going to be some discrepancies when that report comes out, I mean,

ERIN KEMPLE: We've already found discrepancies.

REP. MCCRORY: Okay. And what do you plan, or what can we do to eliminate those discrepancies going forth? Do you have any ideas?

ERIN KEMPLE: One of the things that my agency is doing is looking at all of our options, including meeting with people, the lenders who we have found do have some discrepancies. One

of the things that we are trying to determine is, is that a policy of the lender, or is it a failure of training for the loan officer, and if we think it's a failure of training of loan officers in general as opposed to a,

REP. MCCRORY: I don't think it's a failure of training a loan officer, because they know when someone has good credit score and good history, that person qualifies for a traditional loan.

Now when you put that individual or suggest to that individual to go down another route, is there any advantages for that lender, or you know, why would someone do something like that and risk jeopardizing a foreclosure down the road?

I mean is there an advantage for the lender to place someone in a sub-prime market as opposed to a traditional market?

ERIN KEMPLE: The answer to that is very, very complicated depending upon the type of loan, but with regard to what I think is the bigger issue, which is what is that doing to somebody's ability, to an African American or Latino's ability to buy a home in the neighborhood that they want to live, that maybe has the best schools for their children, or the best job opportunities.

That, I think, is really hindering people's ability to live in the neighborhood of their choice, and I would be happy to meet with you about that, because it is something my agency is very, very concerned about.

So if I understand your response to me correctly, they bypass all of the things that are done under a traditional mortgage, dupe you into thinking that you have a fixed rate, and maybe you do for two years, and then it balloons up to something else.

NICK CARBONE: Yes. The people that I've talked to so many and we've met with were duped, were, and the agent misrepresented the whole transaction to the person when they were knocking door to door.

And they waived inspections in some cases, they waived their attorney because it was free closing cost. We'll pay for the closing.

REP. GONZALEZ: And one of the problems that we have also is a family from Waterbury that, because there was not, they didn't have a lawyer present with them, they ended up signing papers, and then they find out that they signed papers for three properties.

And then at the end of six months, they were losing the three properties. So that's one of the problems, the biggest problems that we have.

REP. KIRKLEY-BEY: Thank you, Mr. Chair.

REP. BARRY: Thank you. Any other questions. Thank you very much, Representative Gonzalez and Mr. Carbone.

REP. GONZALEZ: And I would like to add that in the House Bill 5577 I think there are a couple of

other things that we would like to see if we can sit down and discuss. We have a couple of other concerns with that bill.

But I think that with the Commissioner we can sit down and maybe we can discuss that bill. And, you know, between all of us, we can come up with the best solution for the residents of Connecticut.

REP. BARRY: More than a couple other things that you've just mentioned here in your testimony, so thank you. And then Senator Duff has something to say.

SEN. DUFF: Thank you, Representative. Thank you for your passion on this issue as well, and I echo the words of my Co-Chair, Representative Barry.

I would ask you, though, were the trains leaving soon on this? Our JF deadline is, we're JF'ing on the 4th. So we're asking people to deal with their suggestions on any of the bills, especially House Bill 5577 is to get us a list of suggestions.

We're going to be working on that over the weekend and trying to put a bill forward for Tuesday. So please give us your suggestions. We'll be happy to consider them.

REP. GONZALEZ: We will. And thank you.

REP. BARRY: Thank you very much. Next we move over to public comment, Pat McCoy, representing himself, or herself.

JOINT
STANDING
COMMITTEE
HEARINGS

BANKS

PART2
290-617

2008

PAT MCCOY: Good afternoon. I'm a professor, a law professor at the University of Connecticut, and I'm speaking only on behalf of myself, not on the behalf of UConn.

I'm here today to testify in support of three important bills to regulate sub-prime loans, House Bill 5577, Senate Bill 21, and Senate Bill 423. I've been writing about abuse of sub-prime loans since 2002 when I proposed a Duty of Suitability in the sub-prime market.

By the way, my student, John McGrath, has done a substantial amount of work alongside me in the sub-prime market.

Earlier this month, Fitch Ratings estimated that fully 48% of sub-prime loans securitized in 2006 will go into default. Most of the reasons why these loans will go into default are either they were made in disregard of the borrower's ability to pay, or they were infected by fraud.

What are the repercussions? We know about the rising tide of foreclosures, but that's not all. Bad sub-prime loans have had a domino effect, paralyzing one market after another.

Some of these ailing markets are only indirectly linked to the sub-prime market, such as the market for interbank credit, but worst of all now, contagion has infected other markets that had nothing to do with sub-prime loans.

Jumbo mortgages, student loans, municipal bond offerings, and today in the Wall Street Journal, yet another market has crashed, variable rate demand notes.

We no longer have a sub-prime crisis; we have general investor panic. Investors do not know who is tainted sub-prime or how many more multibillion dollar wipe-downs are in store.

As a result, investors have stopped trusting almost everyone except Uncle Sam and gold. So our job here, at least for the people of Connecticut is to restore public trust.

People need assurance that in the future home mortgages can be trusted, that they are sensibly underwritten and free from fraud. If anybody is going to restore that trust, it is the senators and representatives in this room. It is the government.

All three of these mortgage lending bills go a long way toward restoring that trust. Furthermore, these bills are designed so they will not reduce access to sub-prime credit.

I have a new study with three economists from Wharton, USC, and Marquette, that have studied the effect of anti-predatory lending laws in 42 states, in every state that has anti-predatory lending laws.

We found that when you lower the annual percentage rate triggers, the likelihood of a sub-prime loan being made goes up, not down.

It expands access to credit. My time is up. I'd be happy to take questions.

REP. BARRY: Okay. Thank you very much, Professor McCoy. [inaudible] I'm a proud graduate of UConn Law School, and I appreciate you coming here today. And I didn't recognize your name without the professor before it, so sorry for that. There's a lot of footnotes. It's like a Law Review article you gave us.

PAT MCCOY: Thank you. You know we're longwinded.

REP. BARRY: That's quite all right. I just want to ask you a couple questions. What is your, I see here the George J. and Helen M. England Professor of Law, what do you teach at UConn?

PAT MCCOY: I teach banking regulation, securities regulation, business organizations, and consumer law.

REP. BARRY: Okay. So you have an ear, you're really an expert in this area. There's no doubt about that. I guess I'd take judicial notice of that if I were a judge. But, I guess, one question I'd have for you is, how do you think House Bill 5577 would affect the availability of credit, would affect Wall Street?

PAT MCCOY: Right. Right. Our studies also look at the effect of the assignee liability provisions, the state anti-predatory lending laws, and what we found, we looked at the states that adopted assignee liability after the fiasco in Georgia.

What we found were two things. First of all, the later states that adopted assignee liability learned from Georgia, and the crafted their provisions to have caps on assignee liability. Wall Street can deal with that, and House Bill 5577 follows that same approach.

Secondly, when we looked at the effect of these assignee liability provisions in these other states, more often than not, the assignee liability provisions led to an increase in the likelihood that a sub-prime mortgage would be made. In other words, they were compatible with expanded access to sub-prime credit.

REP. BARRY: Are you familiar with the Connecticut Families Program, Refinancing Program?

PAT MCCOY: Only a little bit.

REP. BARRY: A little bit. Okay. I guess someone like yourself would be, I think, seems to greatly benefit from the experience of someone such as yourself, and we all would here, so I'm going to be looking through this 10-12 page document and trying to glean as much as I can from this, because we only have four more days before we have to get a bill out of here.

But there's three competing bills that are not necessarily competing, but they're on different tracks, and we're, we're going to try to work to make something that, put something together that's going to have legs and move and help protect consumers and also make sure that credit is available for people moving forward.

And I just want to thank you for coming here taking the time out of your busy day to testify.

PAT MCCOY: Representative Barry, thank you very much. I have confidence looking at the design of these three bills, that they in fact will increase the flow of sub-prime credit, and they certainly will not impede it.

REP. BARRY: Thanks very much. Representative Moukawsher.

REP. MOUKAWSHER: Thank you, Mr. Chairman. I missed your testimony. I did take a really quick look at what you provided us in writing. It's very extensive, and the history of the whole lending, sub-prime lending field, I thought was very interesting.

And even, even one of the things I was quite startled at was that there has been problems in the past overseas. I mean, many times the demise of sub-prime lending has been predicted, and it has reinvigorated itself.

I think you're even predicting that that market will remain. If we do have a sub-prime market, and you may have testified about this, is that a healthy thing to have?

In other words, there are people who can't qualify for, you know, ordinary regular mortgages, but I know that's not a proper way to describe them.

But is there something healthy about at least having the opportunity for people to have, get credit for purchasing of homes at a higher rate of interest? I mean is that something we should not be afraid of?

PAT MCCOY: There is a need for good sub-prime loans. The problem that we're all struggling with is that the sub-prime market was unfortunately operated in a way that led to overpriced loans, loans that were underwritten in a way where people could not afford to repay them, and outright loan fraud.

These three bills are very serious approaches to dealing with all three of these problems, and I'm confident that if we can outlaw those types of abuses, get the interest rates down to the appropriate interest rates for people rather than charging them too much, we will both expand access to credit and do so in a way that makes home ownership sustainable.

It doesn't do any good to put somebody in a home if they're go into foreclosure. In fact, that's tragic.

REP. MOUKAWSHER: Yes. We've seen it. Again, I don't know if you remarked on this. On the federal level, are there similar, is there legislation similar to what, you know, we are proposing, or--

PAT MCCOY: There is indeed. The House has passed the Barney Frank Bill. On the Senate, Senator Dodd has sponsored a major federal anti-predatory lending bill, but in conversations

with both federal banking regulators, Washington, D.C., and advocates, it is unlikely that the bill will be reported out of committee, because there may not be adequate support in the Senate.

I am not sanguine about the likelihood of federal legislation, particularly in an election year.

REP. MOUKAWSHER: So there's some urgency for us to ace on this at the State level.

PAT MCCOY: Very much so. And in fact, our history in the past 10 years is that the states have been the one who have taken the leadership role.

It's because the states have taken the lead that finally federal banking regulators are slowly groping toward being somewhat responsible about the banks and their jurisdiction.

And, I'd like to also add that if you look at sub-prime loans, fully one-fourth of them were made by depository institutions, and another fourth were made by their mortgage lending subsidiaries, so banks very well may be part of the problem.

REP. MOUKAWSHER: I want to thank you for your work on this. I mean, it's very instructive and informative. Thank you very much.

PAT MCCOY: Thank you so much. Thank you.

REP. BARRY: Thank you Representative Moukawsher. Anyone else? Representative Stripp.

REP. STRIPP: Thank you, Mr. Chairman. Professor I have to compliment you on writing this article. I've read hundreds of articles, and it took me hours and hours to get to the point that you got to in a few short pages, so you did a, did a great summary job.

Some of the questions I have is that as this thing started to build, it would seem to me, and correct me if I'm wrong, but the, the marketing channel that was bringing these mortgages in were more and more mortgage brokers and less and less traditional lending banks as we know them, and I'm excluding investment banks as being a separate industry. Is that basically correct?

PAT MCCOY: Yes, particularly in two markets, the market for sub-prime loans and the market for the nontraditional mortgages which I defined to be the option arms and the interest-only arms.

A majority of those loans were originated by brokers.

REP. STRIPP: Thank you. In page five at the top, you talk about that it was alleged that some investment banks ordered it to cut, and we're talking about the rating agencies here, to cut its random sampling of sub-prime loan pools.

Why would they go along with that? And I guess we're talking about Standard and Poor's and Moody's primarily.

PAT MCCOY: No. Actually what I'm referring there are investment banks ordering Due Diligence firms, so not the rating agencies, but independent contractors who would go in to lenders and do random samples of, of loan pools to check for compliance.

One of those firms, in fact, is here in Connecticut, Clayton Holdings. And Clayton Holdings has apparently testified to Attorney General Cuomo in New York that several investment banks ordered it to shrink its random samples to make it less likely that it would find fraudulent loans.

REP. STRIPP: Now who used these random samples of the pool? Was it Standard, Poor's, and Moody's when they put triple-A ratings or whatever rating they would give to a group or a pool of securitized loans? Is that who used it?

PAT MCCOY: The first user was the investment bank itself who would draft the prospectus for the offering. The rating agency should have been provided with those random samples and the reports.

They say they were not, so they may not have even seen these reports.

REP. STRIPP: Why would they put their indicia and their reputation on the line to say this is a triple-A or a double-A pool without asking for that information? How did that happen?

PAT MCCOY: We don't know, and I think as the investigations of both Attorney General Cuomo and Attorney General Blumenthal go forward, we may get some answers.

We don't know if the rating agencies were also defrauded, or if they too were hiding their heads in the sand, and I, I certainly can't answer that question today.

REP. STRIPP: Perhaps because of very lucrative commissions they were getting. If you look at the profitability of Moody's and Standard and Poor's in this area at that time, they just skyrocketed, so.

PAT MCCOY: That's exactly correct, and furthermore, because the volume of sub-prime securities grew so quickly over the period of 2005 to 2007, that also boosted their, their revenue.

REP. STRIPP: Now in your opinion is there anybody in this chain of events, the mortgage brokers, the securitization of Wall Street investment bankers, Moody's, the companies that put, that did the sampling and so forth, is there any culpability where people can go back or the government can go back after them for what they have done, or is that just, their hands are clean, they got their fees, and they move on to the next program, whatever that might be?

PAT MCCOY: Right. There are two forms of culpability. One is clearly criminal if a crime can be proven. That is often easier to do for either the originator or the broker than

it is for the investment bank or the rating agency.

The second is possible civil liability to try to get some remuneration for the victims of either for investors, municipalities, or borrowers. But in many cases, the well is dry, especially for brokers.

We've also seen many sub-prime lenders go out of business. There is a web page called Mortgage Implodometer that lists all of these bankrupt lenders.

So that's very difficult. On the borrower end where the rubber meets the road is, if you've been the victim of a predatory loan and you're now in foreclosure, your ability to raise that as a defense is very limited.

And I think we need to give serious consideration to leveling the playing field, because the number one forum where a borrower needs to be able to litigate that they've been a victim of a predatory loan is in foreclosure.

REP. STRIPP: I wonder if, well, it would seem to me it would be very difficult for one borrower to really start an action, because the dollar amount is relatively small to the cost of proceeding with prosecution.

Is this a fruitful area for class action lawsuits perhaps?

PAT MCCOY: First of all, if the legislation will award reasonable attorney's fees to the injured

borrower, then the lawsuit does become cost effective.

Class actions in this area, although some have been filed, they're very difficult to certify in most cases, because it's difficult to prove the commonality requirement for certification, so we really need to figure out how to make individual actions cost effective. And, the way to do it is a fee shifting provision.

REP. STRIPP: Well, thank you very much, professor. It has been very enlightening.

PAT MCCOY: Thank you very much, Representative.

REP. BARRY: Thank you for those very good questions, Representative Stripp. Does anyone else have any questions of Professor McCoy? Okay, thank you very much. Thanks a lot.

PAT MCCOY: Thank you very much.

REP. BARRY: Okay. We're going to go back to the department heads and elected municipal officials, and the next person is Mike Ward from CHFA to testify on House Bill 5577. Good morning, Mr. Ward. Good afternoon, I'm sorry. Sorry about that.

MICHAEL WARD: Good morning. Oh, good afternoon. It is 1:24. Good morning, Chairman Barry, Chairman Duff, and members of the Committee. I'm Michael J. Ward.

I am the administrator for Planning and Budget at the Connecticut Housing Finance authority,

and I am here this afternoon with Valencia Taft-Jackson who is a program manager in our single family area that has responsibility for implementing the Connecticut Families Program.

Valencia could help us out in the question and answer period, as we would [inaudible] address some of the Connecticut Families Program issues.

I'm here to testify this morning on behalf of CHFA regarding Raised Bill 5577 AN ACT CONCERNING RESPONSIBLE LENDING AND ECONOMIC SECURITY.

Before making specific comments on Raised Bill 5577, I want to thank the Committee for the opportunity to be here this afternoon to discuss this important legislation with you.

Though we must oppose some aspects of Raised Bill 5577, we would like to acknowledge the Committee's efforts in proposing legislation to address the important challenges in this state by sub-prime lending.

CHFA understands the nature of the problem our State and the Committee is facing. We would like to work with the Committee to address these challenges.

It is in that spirit that CHFA offers these comments to the committee this afternoon. I have provided a detailed statement to the Committee on behalf of the Authority regarding this bill, and I would like to summarize a couple of the main points.

First, transferring of $40 million dollars in CHFA bond proceeds for the purposes of Raised Bill 5577 has broad and far-reaching implications for CHFA's and the States bond rating.

CHFA's bond proceeds are private capital invested by individuals, private companies, and investment firms that expects CHFA to invest their funds consistent with CHFA program requirements as ascribed in CHFA bond documents.

These are documents of trust. Removing these funds from the Authority investing them otherwise would violate that trust and reflect negatively on the Authority and the State.

CHFA's bond rating is currently AAA, which is providing us strength in the marketplace right now as we seek to continue to fund all of our home mortgage and multi-family funding programs, and this AAA rating is particularly advantaged in the common marketplace whereas you heard Professor McCoy testify earlier there has been a significant amount of turmoil and disruption.

Any deterioration of the Authority's bond rating will result in higher interest rates charged on all CHFA's programs, and negatively impact the State's own bond rating.

Transferring these funds would have serious ramifications for Connecticut's Families Program itself, CHFA's First Time Home Buyer's

Program, our multifamily lending bond finance programs, and any new programs the authority would be developing to address sub-prime borrowers.

So for these reasons, the Authority must strongly oppose taking the Authority funds as authorized in Raised Bill 5577.

Second, the Connecticut Families Program we believe is a good approach to refinancing sub-prime borrowers, and the program will utilize the funds we've made available.

The Connecticut Families Program was developed and implemented based on the careful work of the governor's sub-prime mortgage task force. It is a fundamentally sound and flexible approach that will utilize the available funds to address as stressed Connecticut homeowners.

We have reviewed Raised Bill 5577, and believe the real program and the Connecticut Families Programs are very similar, but the Connecticut Families Program is a more flexible approach with regard to credit scores, payment histories, and debt-to-income ratios.

They can offer assistance to a wider range of borrowers with some adjustments to the program, and with some adjustments to the program, we have very confidently utilized all the funds available.

In fact, at this morning's monthly board meeting, the CHFA board did vote, approve

changes to the program which would expand eligibility.

These include making, essentially making any person with an adjustable rate sub-prime mortgage eligible for the program. There was relief that it takes away the requirement that applicants be first-time home buyers.

And we have looked into the, the Pennsylvania real program, oops, into the real program--

REP. BARRY: You can complete. I can see you're summarizing this testimony, and you're not reading it, so you can just go along and summarize.

MICHAEL WARD: So I should continue? Okay. Thank you. And, we looked into the Pennsylvania Real Program, and our experience implementing Family, the Connecticut Families Program and the Pennsylvania Real Program is, in fact, quite similar, and I think ours is actually implementing a bit faster.

The Pennsylvania Program has been open since last, last July, and has only closed, has closed 14 loans and has 33 reservations pending.

Our program has been open since early December, and it has extended 30 reservations, and has foreclosings currently scheduled.

It is important not to underestimate some of the challenges faced by the borrowers that we are seeing applied to this program, which need

plenty of individual attention to work out their situations, especially along the lines of some of the flexibilities I mentioned earlier about debt-to-income ratios and in credit scores, etc.

A third point we would like to, we believe that the HERO Program approach authorized in Raised Bill 5577 is a good way to help additional Connecticut homeowners, and the Authority would like to work with the Committee in developing this approach.

This is a creative approach. It was discussed in the Governor's sub-prime task force, and the Authority has initiated steps to develop such an approach to supplement the Connecticut Families Program, and it is looking for way we might be able to raise additional mortgage capital for that purpose.

However, it is important not to underestimate the challenges of developing a loan purchase approach. Given the complex realities of the sub-prime origination and servicing environment, a loan purchase program does have its own specific challenges.

And also in the Committee, we offer a suggestion to the Committee you may wish to incorporate some investor concession requirements for the sake of equity in this effort, and also to stretch the funding that could be made available.

In our initial look at this type of approach, we believe that getting the mortgages,

purchasing the mortgages out of people's portfolio at some discount is really critical to making the program work for many of these borrowers given their income situation and the debt overhang that they're facing.

Lastly, but, oh, and I must add at this point, you know, the cost of the Authority of running such a program also would be directly impacted if the Authorities bond rating was in any way damaged.

It would just raise the cost of funds for us that we would have to go to the marketplace to raise to implement such a mortgage purchase program.

Lastly, but not least, the Emergency Mortgage Assistance Programming such as that authorized by Raised Bill 5577 can play an important role in the State's overall approach.

At last week's hearing on Raised Bill 5165, the Authority suggested that if funding becomes available for these purposes, the Committee may wish to consider funding its overall effort through nonprofit organizations statewide such as Neighborhood Housing Services.

Through our work with the Governor's sub-prime mortgage task force and the assistance these organizations have provided to the Authority in implementing the Connecticut Families Program, we have become much more aware of the range of good work undertaken by these organizations.

These folks are on the front lines. They are very close to borrowers, their communities, and the sub-prime problem.

They work in areas of lost mitigation and delinquency and foreclosure counseling, and this puts them in a good position in the marketplace and in the communities to be of assistance.

The approach that we would suggest for the Committee's consideration would be using these organizations to originate emergency mortgage assistance loans in much the same way that the Authority uses its wide network of participating lenders to originate all its housing, home ownership program loans.

This approach could save the state money and time that would be required for a State agency or entity to ramp up to develop such a program since they're already in the marketplace, and it is a matter of adding capacity to a system that's already there rather than developing it whole cloth.

And finally, you may want to also consider whether or not it is part of an emergency mortgage assistance approach.

You wish to add some requirements for some lender concessions as well in light of consideration for the public money authorized for these purposes.

For example, you could, if mortgage assistance was extended to a sub-prime adjustable rate

borrower who was then through the Mortgage Assistance Program, kind of had their credit rehabilitated and put on an even keel, and were able to refinance their mortgage with the State's help and benefit to do so, you may ask for a concession such as a waiver or prepayment penalty in order to get out of the mortgage that the State had been subsidizing previously.

CHFA is available to work with the Committee and nonprofit housing organizations to develop such an approach further. Thanks very much for the opportunity to share these remarks with you, with the Committee this afternoon, and I will do my best to respond to your questions.

REP. BARRY: Thank you very much, Mr. Ward. I'm sorry I didn't get the name of the other person that is with you.

MICHAEL WARD: Oh, Valencia Taft-Jackson.

REP. BARRY: Valencia Taft-Jackson. And your title, Valencia?

VALENCIA TAFT-JACKSON: I'm the manager of the Residential Lending Department, supervise underwriting.

REP. BARRY: Okay. And then, Mr. Ward, your title is, is--

MICHAEL WARD: I'm an administrator for planning and budget and a couple of other things as well.

REP. BARRY: Okay. In the last couple of years before this committee, I know we've had Carol

DeRosa come, and before that it was Tim Coppage, so now I just want to make sure I know who's coming before us.

But with respect to the Connecticut Families Refinancing Program, what are the present eligibility requirements?

VALENCIA TAFT-JACKSON: Well, currently they are, thank you. Sorry about that. Currently, you would have to be a first-time home buyer that used an adjustable rate mortgage to purchase your first home, but as of today, and the board's vote, that restriction has been eliminated.

REP. BARRY: First of all, I'm just wondering, I don't even know anything about a vote and the board taking a vote today.

There are other eligibility requirements, so just, if you could just list them for me, the ones that were, were put forth in November, I guess, and you started taking applications December 10. Could we just go back and just start from the beginning.

VALENCIA TAFT-JACKSON: Okay. The first one would be the one that I just described, that they would have to be a first-time home buyer. The second one would have to be that they would have to be in a non-FHA arm.

We were also requiring that all of our Connecticut Families mortgage [Gap in testimony. Changing from Tape 2A to 2B.]

Other debt, but they could be delinquent on their mortgage. So if they were delinquent on their mortgage as a result of their mortgage loan resetting to the higher interest rate, they would still be eligible.

Then the general underwriting requirements would kick in that have to do with the amount of the appraisal. The property would have to appraise out for the amount of the mortgage.

If it didn't, the Connecticut Families Program had a separate second mortgage that we would make available up to a maximum of $10,000 to help bridge that gap with some of the equity financing. We would also help to cover closing costs and some of the other fees that might be associated with refinancing with us through that program.

REP. BARRY: Okay, and was there any expectation or any eligibility requirements? Was there an eligibility requirement requiring you to look at credit history and make sure that they had a reasonable expectation of repayment?

VALENCIA TAFT-JACKSON: Yes. And we also required that all taxes and insurance would be escrowed into the mortgage loan.

REP. BARRY: Okay. And when were those eligibility requirements promulgated?

VALENCIA TAFT-JACKSON: When we made the decision to do the program in conjunction with the FHA secured product that it was, we made that decision then.

The underwriting criteria that we're using is the same as what the Federal Housing Administration is doing. The only difference was our program was a little bit more restricted, because we did try to narrow it to people who used an adjustable rate mortgage to purchase a first home.

In keeping with the CHFA mission to work with first-time home buyers, the first thought was that if we could work with that population who may have been able to qualify for a CHFA loan in the beginning, but didn't get that as an option, and helps them to keep them homes that we would be providing a great service.

REP. BARRY: And do you remember the, do you recall the time period? Was that in September, October, November when those eligibility requirements were set forth?

MICHAEL WARD: It was at the, either in October or November the board meeting when they did adopt the program, they authorized the program. We can get you the exact date.

VALENCIA TAFT-JACKSON: It was in November--

REP. BARRY: Okay. I'm just looking for ball parks. And then you started taking applications--

VALENCIA TAFT-JACKSON: On December 10th.

MICHAEL WARD: On December 10th.

REP. BARRY: Okay. And then since then, how many applications have you received?

VALENCIA TAFT-JACKSON: We have over 30 reservations for funds.

REP. BARRY: I'm sorry. How many applications have you received?

VALENCIA TAFT-JACKSON: Over 30, 30.

REP. BARRY: You've received 30 applications?

VALENCIA TAFT-JACKSON: Yes.

MICHAEL WARD: No, we've, we've authorized--

REP. BARRY: I'm confused.

MICHAEL WARD: We've extended 30 reservations and have four commitments.

VALENCIA TAFT-JACKSON: Right. If I understand the question, the number of loans that we've received from the lenders who are authorized to originate on our behalf is 30, and out of that 30, we have set aside monies, I don't have the total--

MICHAEL WARD: Just a second, I'll get it.

VALENCIA TAFT-JACKSON: --to refinance those numbers of people. What happens when you make a reservation for a mortgage loan at CHFA, you reserve the funds, and then when the package is received, we review it for approval.

So we have 30 that are, we've already approved for, and we have 30 that are still going to come in to us.

MICHAEL WARD: For about $6 million dollars altogether.

REP. BARRY: Okay. And going back to my question, how many people have applied for the Connecticut Families Refinance Program since December 10?

VALENCIA TAFT-JACKSON: Right now we have 30 applications of people who have applied. Although we have received over 3,000 calls through our Call Center for help through the program.

There is a difference, the calls that are coming in, we're taking information with regard to their particular situations and making referrals in the Call Center, which is also part of the Connecticut Families Program.

Out of the 3,000 people who have called, we have referred them to various places, including their loan services, other lenders, or to the loan lender institutions that are originating on our behalf.

Out of those people who contacted the lenders, right now 30 of them have been deemed eligible for participating in Connecticut Families, and they have made reservations for funds.

REP. BARRY: Okay. Thank you. And so, so when someone wants, if someone wants to get into the

Connecticut Families refinancing program, the first thing they do is they contact CHFA? Is that correct?

VALENCIA TAFT-JACKSON: Either they can contact CHFA, or they can go directly to one of the lenders that are approved to originate the program.

We have the information available on our website, but we also provide it through our Call Center or any contact made in our department, so they could get to it either way.

REP. BARRY: And your lenders are McCue Mortgage, New Alliance, and what else?

VALENCIA TAFT-JACKSON: Webster Bank.

REP. BARRY: The Webster Bank. And how did you come to the determination to pick those three?

VALENCIA TAFT-JACKSON: We looked at the ability of the lending institution to service the loans in the State of Connecticut, and those were able to fit that.

REP. BARRY: Are those three lending institutions the top three CHFA lending institutions?

VALENCIA TAFT-JACKSON: They're in our top ten. They're not our top three. We are in the process of looking at expanding the program to include other lenders.

MICHAEL WARD: And the resolution adopted by the board this morning did also call for that, to add additional lenders.

REP. BARRY: Okay. I'm going to get to that, I guess later. I'd like to talk about the resolution [inaudible]. I wasn't aware of any of that. But that will be very helpful, obviously.

Okay. So when they've gone through New Alliance, Webster, or McCue, then they, so I understand this correctly, then they go, that lending institution goes to you, and then you make a reservation, approve of some funding to go to that institution to then fund a loan to this individual borrower mortgagor.

VALENCIA TAFT-JACKSON: Correct. They reserve the funds with us, and when we receive the full file and approve it, then we agree to purchase.

REP. BARRY: Okay. And how many people does CHFA employ today?

MICHAEL WARD: 110. 115.

REP. BARRY: Did you, since CHFA or the board made that decision back in the fall early winter of '07, did you have to hire more employees to undertake this Connecticut Families Program?

MICHAEL WARD: We hired two temporary employees to man the Call Center to field the 2,000 telephone calls coming in.

And otherwise, we're able to run this program with existing staff, because it's, in many respects the product is a mortgage product that the Authority purchases mortgages all the time.

In recent years, we've done 4,000 home mortgage loans a year. This year we expect to do a little under three.

The Connecticut Families Program, you know, mechanically, operationally, operates the same way as the mainline program. It doesn't add any additional burden except for the Call Center, which was Customer Service.

REP. BARRY: So your testimony today would be, if last year, how many CHFA loans did you do last year?

MICHAEL WARD: 4,001. There really was a one.

REP. BARRY: And that was a good one, I'm sure.

MICHAEL WARD: And it was on December 31st I'm sure.

REP. BARRY: So you did 4,001 CHFA loans. This is to first-time home buyers.

MICHAEL WARD: Correct.

REP. BARRY: And you expect that number to not go up this year?

MICHAEL WARD: No. The reason why it's not is that we have been operating for several years under a lot of constraints and Federal tax rules regarding the recycling of bond proceeds that

the Authority is able to reutilize over and over again with the repayment of first mortgages.

There are certain time limits in which the Authority can recycle those proceeds. We had a lot of business back a decade or more ago that we were able to recycle going forward, but the sand has kind of run out of the Regulatory hourglass on some of those proceeds in a kind of a big way.

So whereas last year we had enough funds to purchase about 4,000 loans, this year we anticipate having enough to purchase only about 2,700, because of the requirements to turn back proceeds and also because we have less prepayment in the marketplace because of the experience that we're all having right now with sub-prime.

So we've been affected by a couple of things. A combination of Federal rules and market conditions.

REP. BARRY: Okay. Thanks. The task force report that came out, I think it was in September of '07. I'm not positive.

MICHAEL WARD: I think I have the date on the front cover. November 9, 2007.

REP. BARRY: In any event, okay. So some final draft was probably distributed to me, and I'm basing on that. Indicated that there would be 21,000 sub-prime mortgages with adjustable

rates that would be resetting between October of '07 and the end of '09--

MICHAEL WARD: Correct.

REP. BARRY: --and of those 21,000 loans, I'm just curious to know how many of those are first-time home buyers?

MICHAEL WARD: We looked at, we focused, I don't know about outside of, I would imagine about 10% maybe. I think we, we went through an exercise in the, we kind of, in devising the Connecticut Families Program, we kept our kind of eyes on the pie.

I mean if you've looked at the task force report, there are several important pie charts in it that break down the outstanding sub-prime loans in the state at the time to about 71,000, of which there was about a third of those, you know, about half of those 71,000 were for cash-out refi's, about 40% of them were for purchases.

And then we focused on, and about 22,000 of those loans were two-year hybrids, which are these kind of, some people refer to them as exploding arms or adjustable arms, you know.

There are the 228s. They had the short fuses. And we focused in on the 228s and figuring that about 10%-12% of the 228s were probably first-time home buyers. We kind of broke that down in the report that way.

So I think that about 10% of the 71,000 were those, some of the more exotic products that are outside of the 228s may have less first-time home buyers in them, because as it was referred to earlier, many rather sophisticated borrowers take Fault-A loans or no document loans for certain reasons.

And I think more of the 228s and the adjustables were the ones that focused on providing the most kind of initial affordability, which would have been a little bit more tempting to a first-time home buyer.

REP. BARRY: All right. So based on the 10% figure, upon reflection, do you believe that that particular eligibility requirement regarding first-time home buyers was too narrowly drawn?

MICHAEL WARD: Well, we gave that a lot thought actually, when we were kind of looking at this, and realizing that the Authority's resources, bond finance resources that are available to refinance people are limited.

I mean that's not a permissible use generally under new bond proceeds. We had these Pre-Ullman proceeds that you see referred to in the bill, and in our literature, are actually very aged, obviously mature bond proceeds that have been coursing through the Authority's balance sheets for a couple of generations now.

They actually, the Ullman refers to the Chairman of the Ways and Means Committee in 1980 who passed a bill that put restrictions on the use of mortgage bonds.

These bonds pre-date that. We have a small amount of proceeds that we had accumulated relatively speaking that were not so restricted in terms of refinancing eligibility.

So we looked at what was the best use we could put that limited amount of proceeds to in trying to assist, you know, people.

And we went back to the folks as Valencia mentioned earlier, who had been the focus of the Authority's and the State's home ownership efforts in the past, which is predominantly, you know, low and moderate income first-time home buyers.

So we went back to our initial constituency and said, tried to take some of those people. One of the persons around the Authority said we kind of went back to the beach and tried to pull people off before the tide came in with the program to help avoid them getting into foreclosure difficulty.

Feeling that maybe they had been steered away from a CHFA loan or didn't get one for some reason. We would maybe reach back and try to extend them that opportunity here to get out of their sub-prime loan.

And we thought that the numbers kind of roughly matched up with the scale, roughly matched up with the amount of resources we had available.

REP. BARRY: Okay. And when you referred to the pre-owned taxes and bonds, are there more than $50 million dollars on the books?

MICHAEL WARD: There's a bit. We had actually reserved that money in the past, and we do get some trickles in from time to time. It all depends on, a little bit it's kind of like a lottery. Who had it before, whether they paid off, how the money is coursing through the, the mill so to speak.

And we had previously reserved that money for use with the Department of Economic Development to provide, because there was no income restrictions and first-time buyer restrictions either.

We were working with the department to provide mortgages to support economic development and recruitment efforts, and we reprogrammed that money into the sub-prime program based on the Connecticut Families Program based on a higher priority at the time.

REP. BARRY: Okay. With respect to the eligibility requirement about the appraised value of the home having to support the mortgage, upon reflection today, and this is, the task force indicates information about the fact that house values are going down.

Mortgages, for example, someone goes in and applies for a $300,000 mortgage, and gets an appraisal for $300,000 and has 100% financing in 2006, and now we're in 2008, and that

person's property is worth $260,000. The loan balance is now $298,000.

Did you contemplate that scenario when you decided that the eligibility requirement be, you'd have to meet an eligibility requirement that the appraised value of the home must support a mortgage?

MICHAEL WARD: First of all, I think there's two levels at which to answer that question. I think that, you know, the Authority would never underestimate the scale of the problem with some of these individual cases are, are pretty outstanding, and I myself had one back in the last real estate downturn, where I was underwater, sort of upside down, or whatever you want to call it for a number of years.

And, the Authority, when it borrows money in the marketplace, as I mentioned earlier in my comments on the Pre-Ullman proceeds, the Authority is pledged to return that money to its investors.

And we have in the past, we've always tried to find a way to balance, you know, the risk and the return of the public benefit of the program.

And the Authority is not in position to borrow money and lend it in an underwater situation. There is nobody in the marketplace, that I understand, that is doing that right now, and as I understand the bill, neither does either of the two options in the bill, because they

are both based on 100% of current value as I read the legislation.

This is a problem that the marketplace is going to need to work out over time. It is, in fact, you know, the time is what is the objective of the repayment plans, and the pressure for loan modifications that is currently coming from Federal regulators, the Congress.

The Federal regulators or these institutions themselves are advising folks to, you know, modify loans to buy time so that the value will be covered, because, lending institutions especially in the coming credit marketplace are not in position to be lending funds for more than the appraised value.

It's, it's a repeat of what happened earlier, and credit standards are tightening across the board, and the authority and all other secondary market kind of financial institutions are impacted in the same way by investors.

It just, lending it for much more than the appraised value. Other than the smaller amounts of money [inaudible] available to slightly more than appraised value with a reasonable down payment, which has proven to be a reasonable risk historically is what we've continued to extend to these, you know, these sub-prime refi folks.

REP. BARRY: And then, you know, Valencia Taft-Jackson had mentioned that one of the eligibility requirements was that you had to

be, you had to be making your mortgage payments in the past.

Another thing that seems to be just evident to me in reviewing the task force report and hearing testimony from different people is that there are people who have a mortgage that they cannot afford, and they may not be able to pay that mortgage, or they pay the mortgage on time.

So if they pay the mortgage on time, but they don't pay other bills, would they be qualified under the standards we're talking about right now, or the eligibility requirements that were established back in the fall or winter if their credit score was affected adversely, but they still paid the mortgage?

VALENCIA TAFT-JACKSON: Yes. Yes they would if we could demonstrate that they could afford to pay their new mortgage with the refinance. The product that we have, Connecticut Families, is not a credit score-driven product.

So we are not limited to being able to offer the opportunity to refinance, because the credit score has been impacted, because they were unable to pay their other debt.

What we do want to determine is that they will be able to afford to not only pay their mortgage debt going forward, but also their other outstanding debt, so we look at the total picture.

REP. BARRY: So they would have to agree to financial and other concessions. Is that correct?

VALENCIA TAFT-JACKSON: We would work with them to come up with the best approach that makes sense to help them.

We are working very closely with the Housing and Counseling agencies. So as a result, we would probably work with them to do some budgeting and restructuring.

We would look at their outstandings are. We would look at what their current income is, and then we would apply that to the underwriting standards for the product.

MICHAEL WARD: So there is an approach here, I mean many of these loans are difficult circumstances that come in, and they need, they require, you know, some careful attention, and some work with the borrowers, and in many respects they are a little bit more difficult than many of the regular first-time buyers who we see who are clear of situations.

VALENCIA TAFT-JACKSON: I just would like to say that because it is not a credit score-driven product, we do have some flexibility, and we can make loans to borrowers at higher debt-to-income ratios.

I don't know how much you know about what that means, but and looking at how much of their income actually goes to pay all of their total debt including their mortgage.

If it makes sense, if they were able to manage their debt before, even though their ratios are high, we would take a look at that, and we would see what we could do to structure something that would even be better for them.

So if they were making a $1500 a month payment, and their debt ratios were high, we could restructure them so that their payments go down to $900. They still have their other debt.

We would probably do it even if their credit history was impacted by making that higher payment previously.

MICHAEL WARD: Yes. The spirit of it is to try to look back through, kind of the noise in the credit that may have been caused by the sub-prime pop even if that has reverberated in other areas, so just try to look through the underlying strength that remains.

REP. BARRY: Well for the past, you know, past few years, I've pushed the Emergency Mortgage Assistance Program, and I think that's a very valuable tool that we have in our statues that.

It may require some tweaks, but I've always, in my three years bringing it to the Committee, I've met great resistance from CHFA to that.

I have only asked for $4 million dollars to run that pro, to get that program going in the past, and now I see a program that has $50 million dollars in it that you're able to run

with an additional resource of two temporary workers fielding calls.

In the past in testimony before this Committee, I've been told that EMAP could not be run within existing resources.

This $4 million dollar program that would help that people that seems like some of the people you were just talking about, where they may be unemployed, because they worked at GE and they were making $120,000 bucks a year, and next thing you know, they're out of a job, and their wife and their four kids are at home, and no one else is making money, but they need to get by for another six months or so.

And they would pay just a portion of their mortgage to CHFA and CHFA would pay the rest, and they'd have a lien on their home. It's not a give-away. You'd have a lien, a secondary lien, whether it's a second mortgage or a third mortgage.

And it seemed to me, based on when I looked at Pennsylvania, the way they run their HEMAP program, when the put, in 1985 they put $25 million dollars into that program, and they did it in three successive years, and after '87 through '94, they put less and less money into that program.

And their repayments were being recycled into the program at 9% interest. In the statute right now, we have a provision where it's 99% interest, and it's, it's the cost of loans

negotiated between the Treasurer of the State of Connecticut and CHFA.

And from '94, in Pennsylvania from '94 to '97, no monies went into, no state appropriations or bonding went into run that program, were spent by the State of Pennsylvania or the commonwealth of Pennsylvania to run that program.

And then less and less money has been spent up and through today. It's a very successful program. They also have programs that have the same plans that Senator Duff and I and others have proposed to have where you have a plan for buying loans from lenders.

I think that's a significant thing to do, because when you've got home values going down and mortgages hanging out above the home values, people can't get out. Forget about a prepayment penalty. They just can't get out of that. They can't refinance.

They're going to get a foreclosure sign on their lawn in two or three months. So I think that, just seems to me it just like sticks out as some program that is critical to have, and I see in your testimony that you, your written testimony and what you said before that, the HERO Program is something that you would be, that CHFA would be willing to work with us on and incorporate into some kind of a program that would assist consumers.

And what baffles me is that we had a task force that worked on this and studied these issues

that had people from industries that, very well known people, a lot of experience, lot of integrity, and then we had a lack of what I think, the composition, I think, was not adequate to bring the right voices to that task force to be able to relay what's going on in certain segments of the industry.

And I know EMAP was brought up by a couple of different people, but it was never ever entertained at any other level. I read through every page of the report and the testimony and through emails going back and forth between people.

But, you know, there was one consumer advocate on there. There weren't people, I know the African American Commission had sent a letter to the Governor and Secretary Genuario, and also CHFA at the end of last year's session, and said we need this EMAP Program, and along with them was the Fair Housing Coalition, Fair Housing Center, Raphael Podolsky, Legal Assistant Resources, the Puerto Rican and Latino Affairs Commission.

These are all stakeholders, people who represent those downtrodden, the people who seem to fall through the cracks in government in many regards, not just in home lending.

So it just seems to me that to be able to tell the committee three successive years that you can't go do a $4 million dollar program to provide this small benefit to people, and then all of a sudden be able to have $50 million

dollars infused into your organization and do it effortlessly.

Then come up with 30 loans possibly out of 3,000 triggers maybe, or in Pennsylvania now as last year they did 10,000 applications and they did 2,500 loans out of those 10,000 applications.

That's the kind of result that I would want to see as someone who is in a position of public trust. So that's just where my concern lies. I'm not using any rhetoric. It's just based on facts and looking at what other states are doing.

So I guess I'd be interested in hearing what your thoughts are and just those comments.

MICHAEL WARD: I'm going to address the EMAP and the HERO situations directly. In the past, it's my understanding the Authority opposed this, first of all, we did implement a round of EMAP a decade or so ago where the general perception was that it helped, and we still have some people paying back actually. They're still on the books.

It did help a relatively small number of borrowers for the level of money assisted, and the overhead to run the program was relatively high.

There was a number of temporary employees that needed to be brought on board to get this program up and to then let them go once the

homes, the money was exhausted and the loans originated.

It's important to distinguish between an effort like the EMAP Program and what it takes to run something like that successfully, and what we're talking about in the Connecticut Families Program.

There's two very different pictures administratively. In the Connecticut Families Program, the loans that we're buying are first-time home mortgage loans that are variations on a theme that we, business that do a lot of.

The time is spent with the originating institutions. They're not CHFA staff that is doing the work with the borrowers. It's the participating lender and the counseling agencies.

So that their job is to work with this borrower to determine whether or not we can work everything into this picture and then get the picture in the shape so that the Authority can purchase the loan.

So in that respect, that was why the Call Center and the Customer Service fund end of that was what we needed to add to that program to implement it, because we're working within, giving more work to existing, similar work to existing staff.

The EMAP Program is a completely different set of parameters. It's a second mortgage program. We did that directly so it required the

handholding to place at the Authority rather than in the lending institutions, because quite frankly with the level and the size of the loans to get a traditional lending institution to pay attention to it at that time would be very difficult.

They have to be able to clear their costs and expenses and things like that. The reason why we suggested the nonprofits and like NHS is because they operate in a kind of, with a funny mixture of all those environments every day.

They're in the communities working with trouble borrowers trying to get people into homes, trying to keep people in homes when they get in trouble, and they've hit more of that in the sub-prime area.

So they're gaining experience in that realm, and they're used to working with those types of people. Many of them do have secondary finance programs that they do operate for down payment assistance and other types of purposes.

So administratively they may be in a position to gear up to help support the whole network in that way.

It's kind of like finding people who do kind of what you need done that are already kind of doing it, and asking them to do a variation of it by providing them probably some compensation for it on a per case basis, to both provide counseling and originate the mortgages.

That's why we suggested the model we did in the testimony to kind of avoid having to spend program resources on gearing something up whole cloth at the State or another Government entity.

With regard to the Pennsylvania HERO Program, my understanding is that the money for the is, in fact, a bond issue by the State in the State of Pennsylvania considering another one, which is a general obligation of the Commonwealth of Pennsylvania.

The reason why that's an important distinction from the Pennsylvania Housing Finance Authority is the Pennsylvania Finance Authority, they are kind of revenue bonds. Meaning they're lending the money out to a first-time home buyer or a refi program like ours.

They're expecting to get paid back, and then that money is going back to pay off bond holders. So there is a direct nexus between the payment on the appointments and payment and the credit on the mortgage and the appointments and payment and credit to the bond holders.

There is a pass through. If a State goes on, or a general government entity, there isn't necessarily a direct connection between the use of the funds and the return of the money.

So that for example you could purchase loans, the Pennsylvania program may be able to purchase loans greater than 100% of value, because they're, you know, it's not a direct mortgage credit per se that's behind that.

It is my understanding how the Pennsylvania program is set up. That's the reason why I mentioned in my testimony that we think the key to a purchase program that the Authority again involved in is getting the loans at some discount, which represents an investor concession for the amount of the overhang.

I mean, we have loan to value restrictions that we need to pay attention to, because that's what the people who gave us the money expect. That's their risk tolerance, and it's different if it's a general obligation of a government entity.

That's my understanding of how the Pennsylvania program is structured.

REP. BARRY: Were you at CHFA in '94 when EMAP was first--

MICHAEL WARD: Yes I was, but I didn't work in the EMAP Program.

REP. BARRY: Okay. Did you, Valencia?

VALENCIA TAFT-JACKSON: No. I'm sorry. I was not.

REP. BARRY: Okay. Because I think back in '94 another $50 million dollars was on the books there at that time, or monies, Pre-Ullman monies were on the books then.

MICHAEL WARD: The EMAP Program is kind of an assistance program and a second loan program. The Pre-Ullman proceeds that you're talking

about are required to be used for first mortgage lending. It's not a secondary, maybe-they-can-pay type of resource.

It's a structured first mortgage resource that's under the rules that the money was raised under the Federal Tax Law and by the bond covenants of the agency. It's just a little looser on who's actually eligible.

REP. BARRY: AND The fact that that program lasted one year and you still have some loans that haven't been repaid to CHFA--

MICHAEL WARD: About half of them not, actually.

REP. BARRY: --I think that's less reflective of how good the program is, but more reflective of the fact that you didn't do it in successive years like has happened in other states, including Pennsylvania where you've got to make an investment in something like that's what we're trying to do here, going forward with a long-term plan.

We're not just trying to throw something out there and have it look good for a year, and I think with EMAP throwing $4 million dollars at it in '94, and maybe it got some traction for a year, but over time, I think that program would have been very successful, because we have other Authorities from other states telling us that it has. It has worked in other states.

MICHAEL WARD: Their experience administratively was similar to the experience that we had in the earlier version. They have set up a staff to

run, and they do it as a direct lending program. Our approach was more to originate these loans and suggesting just using a network of existing institutions to do it.

REP. BARRY: Okay. Carol DeRosa testified last year that the majority of sub-prime loans deal with the minority population. Is that true? The majority?

MICHAEL WARD: Well, there is a heavy concentration of sub-prime lending in communities that are, you know, heavily minority and low income, that is true.

In fact, you may find it instructive, in my testimony, we attached two maps to the back, one of which shows active CHFA loans, and where our single family lending, our first-time home buyer programs are concentrated.

And a second map that shows the concentration of the active sub-prime lend loans that were in the research that we undertook for the Governor's sub-prime task force.

It shows the distribution in the states. You can see there's quite an overlap. I think that an important consideration of that overlap is that we have done lending in those communities for years.

It was part of the reason why when we went back to where to spend our scarce resources under the Connecticut Families Program we went back to that group and said, here's the low or moderate income first-time home buyers in this

state, let's see if we can focus on those folks, and kind of help get them out of the storm, because we have always worked with that constituency.

REP. BARRY: I know Carol DeRosa mentioned last year that also a majority of the sub-prime loans were made to low and moderate income families as well.

So those are the two groups that we are concerned about, I was concerned about, and then recognizing that they were not, I don't think they're fairly represented in the task force.

I'm just trying to go back to the beginning of this and how the Connecticut Families Program came about. I think that might be one of the reasons why we're kind of deficient today and why there are perhaps some modifications to the program that you may be presenting to us.

I would like to know what those modifications are, and what brought about those modifications. There was a Board of Directors meeting today?

MICHAEL WARD: We have a monthly board meeting, so there was a Board of Directors of the Authority that kind of monitors and watches these, you know, the Authority's operations and programs on a month-to-month basis.

They are the governing body for the Authority so to speak. They provide the ultimate authorization for the use of funds in the

parameters of the programs. The initial, when you look at the work, we were very mindful of the work that the sub-prime task force did, and trying to most effectively target the amount of funds that we did have available at a low cost to do refinancings.

So that's why we did focus back on that narrower slice of the pie, that hopefully there was a couple of thousand folks as we could figure out who might need some assistance.

So the philosophy was to, when we initially went into the marketplace with the program to kind of keep it focused on those folks and kind of see how it goes.

And if our experience with the program, you know, we need to kind of get this out faster, we can look at successfully kind of opening up this door wider so to speak based on what's allowed under the Federal Tax laws with the underlying bonds.

That is why we limited it to the first-time home buyers in the initial roll-out, and subsequently we looked at the experience and the need, and the desire to get the money utilized and out on the street to help folks.

We decided to open it up to people who weren't necessarily first-time home buyers. They had bought a home with an adjustable rate mortgage, and they were living in it now. They were eligible.

MARY WALLACE: Yes. And a certain amount of diligence.

REP. BARRY: So I believe you'd be happier with that. That's in House Bill 5577. Maybe that's not in 423.

MARY WALLACE: Oh, it is. No, it is. There is a standard of reasonable care to try and get the borrower into the best possible loan.

REP. BARRY: Now I'm not sure. Is the bona fide error defense you talked about--

MARY WALLACE: Good faith error.

REP. BARRY: For some reason I thought that was just a defense you can always assert in Civil Court in a Civil matter, just saying you followed standard procedures, and those standard procedures resulted in a bona fide error.

I don't know whether it has to be in the bill or not.

MARY WALLACE: In the 423 there is a good faith error provision which allows the lender to fix the loan.

REP. BARRY: I understand. Do you think it has to be in the bill, or do you think it's already covered under existing law? I'm not putting you on the spot, I'm just wondering because I, I need the help. That's all.

MARY WALLACE: I don't know.

REP. BARRY: So in other words, these are pretty, it's not like these are, the bills we present every year are just about like changing some technical thing and he sends a lawyer over.

But when, if we wanted to say, revamp CHFA or taking bond money from CHFA and moving it to DECD, those are pretty major measures, and then the leadership, like the titular head of that agency, you see Commissioner Pitkin here every meeting, and obviously we have a great deal of respect for him, and then the CHFA Executive Director, Gary King, who is in charge of, he has a great deal of power, there's no doubt about it, running a program for 30-some odd years, I think. At least 25 years or so, 30 years. And just hasn't ever shown up in this public hearing since I've been on the Committee.

It says something to me about some lack of leadership at CHFA. I'll leave it at that. Senator. Okay. Anyone else have any questions? Okay. Thanks a lot. Appreciate your comments.

REP. BARRY: Okay. We're going to move back to the public. Uriah King. Good afternoon.

URIAH KING: Good afternoon, Chairman Duff, Chairman Barry, members of the Committee. Thank you for the opportunity to appear here on such an important topic. My name is Uriah King.

HB 5577
SB 423

I'm with the Center For Responsible Lending, a National Nonprofit, Nonpartisan Research and

Policy Organization. I'm affiliated with the self-help credit union.

One of the largest and oldest community development credit unions in the country. We're both a direct lender and a secondary market player, including right here in Connecticut where we financed tens of millions of dollars of first-time home buyer loans.

I know that the hour is late and I only have three minutes, probably two minutes now, so I'll be very brief. But I want to express my general support of House Bill 5577 and particularly Senate Bill 423 which we've endorsed.

My three major points is that the market correction has been insufficient, and will likely only be temporary. Two, fair and reasonable standards are necessary, and they do not restrict access to credit, in fact, they preserve it.

I want to echo Professor McCoy's statements in that regard, and the three bills that you have before you are in line with policies adopted by other states as well as recent actions taken by Congress and the Federal Regulators.

And it's that third point that I'll spend the balance of my time on.

In just the last 18 months, Ohio, Minnesota, North Carolina, Colorado, Illinois, Maine, and Massachusetts have all moved to address these root problems that have gotten us into this

sub-prime foreclosure crisis and then resulting credit crunch and housing market recession. Much of which is included in these three bills.

These steps include inability to pay at the fully indexed, fully amortizing rate with income verification.

They tend to limit the serial refinancings that you see which are essentially designed to generate fee income for the broker or particularly non-bank lender without any real benefit to the borrower, establishing clear ethical standards whether it be fiduciary duty or agency or good faith fair dealing or some type of ethical standard in the marketplace.

Banning sub-prime prepayment penalties, in some cases they're banning them all, but in particular the sub-prime prepayment penalties which is, again, now a common action being taken by the State level.

I do want to say that of those seven-eight bills I mentioned, all of them have a Private Right of Action. Of course, when you're defending your home against an illegal loan, you can't really go file a complaint with the Regulator.

You have to be able to defend the home in a legal action, because somebody's suing you trying to collect on a loan that may be illegal or certainly predatory.

Obviously it makes sense to be able to defend your home against foreclosure, otherwise really you know, what's the point.

There are a couple, I do want to highlight some distinctions since the time is short, although I generally would, if I had more time, I'd say all kinds of great things about all three bills, particularly two of the three, but there are some things I wanted to point out.

One is the Yield Spread Premium. We heard a lot about that, but and I'll wrap up. The Yield Spread Premium in particular, I would support the Coalition's Bill, AARP, and the Fair Housing Center's approach to that which includes it into your existing points and fees cap.

That's the approach that about a dozen other states have taken. They've actually seen an empirical reduction in steering, because of that. Because Yield Spreads are the financial incentive to steer, by actually curbing that, not banning it, but curbing it, they actually see an empirical reduction in steering.

But to put it in perspective, Massachusetts just banned them outright. So I think it's a reasonable approach what one other bill does. The other thing is a--

REP. BARRY: Which bill are you talking about?

URIAH KING: The Coalition bill. The one that's centered on the AARP. Let me put the numbers in front of me, I'm sorry. Senate Bill 423.

They're supposed to basically monitor and regulate nontraditional banks. I think there needs to be more emphasis there in looking at the sub-prime lending and looking at people's credit scores to see whether indeed they do have, because there are borrowers who certainly qualify for conventional loans who are not getting it.

Because for some reason maybe they're not just looking at their credit scores well enough to know that, you know. So there's something going on behind the scenes that needs to be looked at. So that's all I would like to say. Thank you.

REP. BARRY: I think that's what they told us Connecticut Families does. They don't look at the credit score. So anyone else have any questions? Okay. Thank you very much for your testimony. Appreciate it.

FRANK SYKES: Thank you for your time.

REP. BARRY: Yes, thanks for hanging around. Okay, then Attorney Dan Blinn.

DAN BLINN: Good afternoon.

REP. BARRY: Hi, how are you? Nice to see you.

DAN BLINN: I'm doing very well, thank you. Okay. Chairman Barry, Committee, thank you very much for the opportunity to speak today. I'm here to speak in favor and in support of Senate Bill 423. I also want to speak very briefly on

HB 5332
HB 5577
SB 21

House Bill 5332 and express some comments in opposition to that bill.

First, I want to thank the Committee for the hard work it's doing on this subject. It's extraordinarily important. I think that 5577 is also a wonderful bill. I like 423, however. It has a few things in it that I think are important that are not in 5577.

Erin Kemple addressed a number of these. I think Andrew Pizor is speaking shortly after me. He's going to address them too, so I'm not going to duplicate them, but there's one thing in particular I'd like to emphasize.

That is the expansion of the conditions upon which a claim can be brought under the broker bond.

REP. BARRY: Hold on a minute. What does your testimony look like? You're representing, are you with a consumer law group today, or who are you--

DAN BLINN: I'm here on my own behalf for the Consumer Law Group.

REP. BARRY: I was looking for your testimony.

DAN BLINN: It was submitted.

REP. BARRY: It's submitted. Okay. You can keep going.

DAN BLINN: Okay. Thank you. As a private attorney, I have been contacted by, without exaggeration,

hundreds of individuals who have been victimized by fraudulent mortgage practices, and in many of these cases, there has been truly outrageous conduct my mortgage brokers.

I don't mean to besmear the entire industry. I think that many, if not most, of the mortgage brokers are honest and ethical people, but there are some very, very bad actors there.

And although we've obtained many default judgments against mortgage brokers, the most likely result when we bring a suit against a mortgage broker is that they're going to close up their LLC, they're going to come back again under a new name, and there's no ability to collect against them.

It's a good thing to increase the amount of the bond, which Senate Bill 21, and House Bill 5577 both propose, but it's not enough.

It's also necessary to include the scope of coverage to include any violation of the law or any unsatisfied judgment, and that's a provision that's uniquely in Senate Bill 423.

The point I want to make on House Bill 5532, which would exempt State banks and some other institutions from the cap on late charges. As I understand the primary argument that has been raised in support of that provision is that Federal banks aren't subject to it, because of Federal pre-emption.

But what I'd like to point out to the Committee is that the vast majority of retail installment

sales contracts were originated by car dealerships and assigned to these finance companies.

And that these finance companies, in fact are honoring the late fee cap under the Retail Installment Sales Finance Act.

This discrepancy that is being put forward as the basis for this really is not an issue, because they are complying, because they are not the originators of these loans, they're assignees.

If there are any questions that the Committee has, particularly on Senate Bill 423, I would be very happy to address them.

REP. BARRY: Thanks very much, Attorney Blinn. First of all are there any members in the Committee that would like to ask a question of Attorney Blinn. Okay.

You were on the mortgage task force. Correct.

DAN BLINN: I was. Yes.

REP. BARRY: Okay. And how did you think that went?

DAN BLINN: Well, I think that the people that were involved were well-intentioned. As you noted in response to earlier testimony there was only one consumer advocate that was on that committee.

REP. BARRY: That was you, right?

DAN BLINN: That was me. And, there were things that obviously I would have liked to have seen that were not there. There were a couple of things that were there that I would have preferred not to see.

But the Task Force did operate by consensus, and my two single departures were, number one, I was advocating for a much stronger language in terms of what we were going to be recommending in terms of legislation to combat abusive and unfair mortgage practices.

Much like what we see with Senate Bill 423 and House Bill 5577. The other point of departure that I had that I, well, there was some language in the Task Force, that reflected this. It was my disagreement with the recommendation that criminal sanctions for mortgage fraud extend to consumers.

I disagreed with that very much, and the reason why is because, although consumers frequently do wind up signing credit applications that contain false information in my experience the vast majority of the time, that's information that's put in front of them, and it's signed with very little scrutiny.

And even when they do notice it, with very little understanding of the implications, and it's done at the prodding of somebody else as a requirement for the extension of credit.

It can be terribly, one of the most pernicious collection tactics you see is when a debt

collector or a creditor threatens criminal prosecution for payment of a debt.

My concern is that if criminal liability were extended to consumers in this context, then that would be used as a tool in collection when people are late with their payments.

REP. BARRY: My understanding is that that's against the law though, right?

DAN BLINN: It is against the law. It violates the Creditor Collection Practices Act if it's done by a creditor. It violates the Faraday Collection Practices Act if it's done by a debt collector.

But if, in fact, there is a basis for criminal prosecution, and if a creditor does intend to pursue criminal charges, that's something that could happen, and it happens all the time.

My concern is that actually having a criminal statute out there is going to increase the likelihood of that type of collection tactic happening.

REP. BARRY: I'm of the same opinion. That's what I told the Commissioner earlier, but I see back in one of the Appendices and read an email from you back when you were having these give and takes, and it didn't look like your recommendation got adopted, but I agree on that.

In any event, anyone else have anything to add? Yes, Attorney Moukawsher. You are an attorney, but Representative Moukawsher.

REP. MOUKAWSHER: Thank you. You know my experience with credit applications is that that information is taken by a credit officer either over the phone or otherwise, and handwritten, and then at the closing, there is a typed up copy, and oftentimes, you know, it's pretty detailed.

And most times people sign them because it says, do not make any alterations, and they may not be aware of anything that maybe amiss in it.

So that whole process of the way they are generated and the way they're provided and the circumstances at a closing with a huge pile of paper, I agree that I think it would be very unfair to be having criminal charges against consumers in those situations.

Unless there's something truly egregious that could be demonstrated outside of that document that there was some kind of fraud, so.

DAN BLINN: If there is actual fraud that's engaged in by a consumer, and if the prosecuting authorities desire to prosecute, there are existing criminal statutes that would apply to that.

The reason that the Task Force was endorsing additional criminal provisions is that we felt that by including that language that, number

one it would encourage prosecution of this type of crime.

And number two, it would provide a deterrent to those in the mortgage industry if they were aware of a special mortgage fraud criminal sanction, that they'd be less likely to engage in that type of conduct.

And my thought was that neither of those two reasons to have essentially [inaudible] criminal sanction would apply to the consumer, because number one, the consumer is not going to be aware of it so it's not going to have that deterrent effect, and number two, I don't really think that it's going to increase the likelihood of criminal prosecution of consumers.

REP. BARRY: Anyone else have any questions of Attorney Blinn? Representative O'Neill.

REP. O'NEILL: You raised the issue that there are already various kinds of statutes to deal with fraud committed by people at the present time. I'm just wondering how much of what has happened do you think is subject to prosecution?

And the other thing, I was going to give you a hypo, not a hypothetical, but an actual experience that I had and ask for your opinion.

Let me throw that out when you can think of the other things. In terms of what would constitute, when talking about a mortgage application, and it's the typed up version

sitting at the closing table at 6 o'clock night as you're about to do a refinance or something.

And you say now have there been any major changes in your financial situation, and if the person then says, well I lost my job. I've always taken that to be the kind of thing that if the bank knew about it, they probably wouldn't want to extend the credit, so at that point, I just sort of would stop the presses.

This has to wait at least, I'm assuming that that, even though it's on the application, it's not that they lied at the time of the application, but they're reapplying for the loan in effect at that moment when they sign it, that's a pretty big change in their circumstances. Am I correct in that assumption?

DAN BLINN: Well, I'm not sure. I mean clearly it's a change in their personal circumstances whether or not they're doing more than verifying that the information was true at the time it was given them, I'm not sure.

But, yes, I would agree that it's a change in their circumstances.

REP. O'NEILL: Okay. And it's the kind of thing that if they didn't disclose it that you're not clear that it necessarily would constitute fraud?

DAN BLINN: I'm really not. No. I just don't know one way or the other whether or not that would

be fraud. I don't practice in the area of criminal law really.

REP. O'NEILL: But even though from the standpoint of the bank being misled into the person's financial condition, you don't think that that constitutes misleading the bank?

DAN BLINN: If somebody misrepresents the current status of their employment, yes, that would be a false statement that was made. I would have to agree with that. Certainly.

REP. O'NEILL: Do you think that the stuff that was going on under existing laws, that there are enough criminal laws to prosecute the people from a criminal standpoint for things that have been going on in this whole arena?

And you may not be the best person to ask this, but since you kind of raised the subject, the question is if somebody is looking for a way to try to game the system, which is what it seems like was going on here for the last few years before everything came crashing down, do any of these people look at the criminal laws that would affect white collar crime, which is the kind we're talking about now.

And say to themselves, well, I'm not going to do things, because I might get caught. I mean are they any different from the guy that goes out and decides to steal using a gun or something like that?

In other words it seems like people who commit crimes, there's some people who will stop,

because it's the wrong thing to do, but we kid ourselves to some extent in thinking if we just pass more laws that's going to stop people from committing crimes? Especially this kind of crime.

DAN BLINN: Well, number one, I think that there are criminal laws that are already on the books, and I think there have been prosecutions under those statutes.

I think there should be more, and I think that many of the types of transactions I've looked at have involved very clearly criminal behavior on the part of a number of people in the mortgage approval chain.

Whether or not it's adequate or not, I agree with the Task Force's recommendation that there be a mortgage fraud statute that imposes specific criminal sanctions for this type of thing, because I do think that that would provide an additional deterrent from the type of things that we've seen and that I'm sure you've already heard much about.

REP. O'NEILL: Okay. Thank you.

DAN BLINN: Sure.

REP. BARRY: Any other questions? Representative Betty Boukus.

REP. BOUKUS: Thank you, Mr. Chairman. Good afternoon everyone. It's a long one. Just for clarification for me, and I've been sitting here listening and reading testimony for people

that have not come here before us today, and their situations are dire.

If I have, or if a person has a mortgage on their home right now, and someone comes to them, and we all know, too good to be true offering, and they get ready to sign.

And when they come to your house, I never even heard of that before. They come to your house to get all these papers and all that stuff, and they start to present you with the materials.

One person said that the person with the materials didn't stop talking from the minute they came in, to distract, you know.

But they start to say to you that 6% mortgage we were going to give you is now 7.2, dadat dadat dada. If the person just says, that's it. I'm not signing it. Isn't their original mortgage still in place?

Don't those mortgages disappear once you start to file the papers and they pay off the other person? So the reality is that the people do have the right to be able to say, no, and still have a mortgage.

Unless they're having other problems and that mortgage is too high for them to be paying. There's other issues beside just the idea that they're trying to get a deal.

DAN BLINN: In the mortgage context, yes, they do have the right to say no. They do have the right not to sign the papers. And in fact, in

a refinance context, they also have a three-day period in which they can cancel the transaction.

However, there are a number of reasons why that typically doesn't happen, and I can give you several examples of that.

Number one is that frequently they're told that we're going to be able to refinance you under the other terms, but it's going to take a couple of weeks to do that.

They'll engage in additional affirmative fraud in order to prevent them from engaging in the things that they could do to protect themselves.

Second is, one of the specific acts that I know is prohibited under Senate Bill 423, I'm not sure if it's in House Bill 5577 or not, is a prohibition against telling people not to be making payments on their existing mortgage.

Frequently, what they'll do is they'll put people in a trap where they really don't have a choice, and then they get to the closing and they find out.

I have one client, for example, where they did pull exactly this type of switch on her, and she was dragged along, and the closing kept getting postponed and getting postponed and getting postponed until the point where she was on the verge of foreclosure.

Sometimes people actually are looking at a foreclosure, and they're doing it on the eve of the law date, where they really don't have a choice except to go through with the transaction at that point in order to save the house.

So there are various techniques of use. And then, of course, you have the very, very large percentage of people who don't even understand what it is they're signing.

The disclosures, there was a question earlier about the disclosures and whether or not those are adequate, and the problem is that the papers are, for many people, just simply impenetrable.

And there are so many disclosures that are mandated by Federal law, and additional disclosures that it's too much for most people to process.

And ultimately that's going to have to be addressed on the Federal level, because the Truth in Lending Act and Real Estate Settlement Procedures Act require much of that, and I'm hoping that at some point there is going to be something simple, easy to understand, where somebody can see on one page the relevant terms.

But oftentimes, the people really don't know that things have been switched on them. And I hear that story time and time again.

REP. BOUKUS: Well you've mentioned three or four issues that just stick out there, you know. And then earlier I heard something about 1% mortgages or whatever they are, and they're still out there, you know.

Why or have any of the states, including Connecticut, done any PSAs that go out there and say beware?

DAN BLINN: I don't know if other states have done it. I do know that one of the things that we discussed very early on in the Task Force was the desire to do that type of public education, and that was part of the final report.

I was not on the subcommittee that was involved in that, but I also note that there are significant private initiatives, one of which my firm cosponsored to try to tell people to look before you leap when you're putting your home on the line.

I think that that's something that the State could do much more of. It's probably, well no, it's not probably, it's too late to do anything for the present crisis, but it's going to come around again.

And unless serious measures are enacted, we'll be here again. It will happen again unless some of these practices are outlawed.

REP. BOUKUS: The last question I have is understanding these foreclosures for people who I can't imagine. Of course it speaks of our national dilemma right now, and the morality of

people to be able to change someone's income or what have you.

But the other point is there are other people that are going into foreclosure, because they've lost their jobs or they found themselves, they were doing very well, found themselves in a catastrophic illness or something. Are we doing something for them too at the same time?

DAN BLINN: Are we doing something for them? It's really, I mean you're raising a phenomenally important issue, which is the fact that right now we're in an economy where so many people have such a fragile existence, where if somebody gets sick or if somebody loses their job that they don't have the support system that they need to.

There's a book called the two-income trap that addresses this in tremendous detail, and very eloquently.

And the truth of the matter is we're doing very little for them. You know, I think, and I know that bankruptcy is a Federal issue, but that's one of the places where I think we have done the least with the recent Bankruptcy Act.

It's an area where we really could do much, much more to help people in that type of situation to enable them. Things like being able to restructure mortgages in bankruptcy, which is part of what's proposed in legislation before the center right now.

Again, I recognize that's nothing that we can touch here--

REP. BOUKUS: But we do hear from constituents, and we hear over and over again. You know we, we make our payments. We abide by what we know is the right thing to do. We took out mortgages based on incomes we had.

We did all the right things, and we're still struggling to make these payments and now we've got a whole foreclosure issue from lack of study or resolve to make sure what we're signing is adequate.

And I know that it's difficult for people as they grow older not having experienced it myself, but I know that as they grow older, they start to question their own ability.

So consequently they may be forced into signing things that they really don't want to. But we still have to do a job out there to educate them in the fact that they have two days or three days or whatever the likelihood.

Or if you see this, know it's just too good to be true. I mean it was always buyer beware when you bought the house, and it's just very difficult to explain to other constituents the work we're trying to do to help these people.

And at the same token those that are also foreclosed upon because of catastrophic situations. So while I read all this, and I marvel at some of the things that people have

been asked to do, and they don't have the ability to stop it.

And I think many of your points are clear that if they tell you don't, I have a constituent I have in mind that one of the financial people are telling them don't pay your mortgage, just pay my bill.

To me that's such a red flag, but I guess it's not. But I think we have a job, we have a huge job to do. And I'm not sure, and in agreement with you, I'm not sure that all these laws that we've put into effect really, other than having penalties for those who do these things, these awful things to people.

The general public, the ones that get themselves caught in here, I think will get themselves caught again. And we've got to have the penalties that try to go after these people that are doing it. It's just unconscionable.

DAN BLINN: There are two issues. One, of course, is the fraud issue, but the other one is the substantive terms of the mortgage. Now 30 years or so ago, it was very difficult, if not impossible for somebody to take a loan that they couldn't afford.

REP. BOUKUS: I have to interrupt you having lived through this, you know. No matter how much I was making, you know, it didn't matter. It was what my husband was making, so you know, there's whole areas that we all come from that we recognize.

So absolutely now combined incomes, they'll take anybody, the cat, the dog, whatever it is.

DAN BLINN: Well, it's more than the fact that there's combined incomes. It's the fact that what has happened and the whole reason that we got into this mess is there was a separation between the underwriting and the risk, and Professor McCoy submitted materials that explains how this works with the secondary market and the Acid Backed Securities and the like.

The profit incentive was so huge that the incentive for fraud was there, and the incentive to create products that people cannot afford was there, and it's perverse.

Where you make money by loaning to people who can't afford to pay it back, but where I would disagree with you though, is that I do think that there's something that we can do, because Senate Bill 423 regulates a lot of the worst types of instruments, and House Bill 5577 does as well. But I think that Senate Bill 423 goes further in the right direction.

And it will essentially prohibit certain types of transactions from taking place or dramatically limit them and limit the types of people that those of products can be sold to.

I think that that would be a tremendous step in the right direction to prevent this from happening again.

SEN. DUFF: Thank you.

DAN BLINN: Thank you very much.

SEN. DUFF: Is Frank here? Sykes: Did already. Okay. Paul Peduto? Good afternoon.

PAUL PEDUTO: Good afternoon.

SEN. DUFF: Thank you for being here.

PAUL PEDUTO: Chairman Duff, members of the Committee. My name is Paul Peduto. I'm with the Federal Home Loan Bank of Boston, and I thank you for this opportunity to testify before the Banks Committee on behalf of the Federal Home Loan Bank of Boston in Support of House Bill 5331.

The Federal Home Loan Bank of Boston is one of 12 regional wholesale banks organized by Congress in 1932. It is a privately capitalized cooperative.

Its mission is to support the residential mortgage and community development lending activities of banks and other financial institutions located in the New England region.

Seventy-seven financial institutions located in the State of Connecticut are currently members of the Federal Home Loan Bank of Boston. Federal Home Loan Banks are regulated by the Federal Housing Finance Board which is an independent federal agency.

One way in which the Federal Home Loan Bank of Boston assists its member banks is by providing

REP. MOUKAWSHER: Sorry, I didn't get the number of that second bill. What was it?

KELLY FUHLBRIGGE: It's Raised House Bill 5332.

REP. MOUKAWSHER: Oh, 5332. Okay, thanks.

KELLY FUHLBRIGGE: You're welcome. Thank you.

SEN. DUFF: Thank you, Kelly. Okay. Just real quick, is Warner or Frank Sikes here by any chance? No? Okay. Last call, Joe Carbone.

JOE CARBONE: I am Joe Carbone and I'm president of the Work Place, Inc. We're a private not-for-profit in Fairfield County and we act as the workforce investment board for the region. HB5577

Let me start off by first of all commending all of you. I've been here for several hours and I've listened to each of you kind of reaching to find solutions to help people, and it wasn't just about banks and lending institutions. You were really searching for ways to help and I commend you for it. And I have another way in which I think you can help.

Let me begin by saying that the workforce system in Connecticut might be familiar. We've got five work-force investment boards that cover all 169 towns.

We've got he Connecticut work centers, and there are 15, eight of which are comprehensive, full-service centers and the others which are basically satellite centers.

I'm suggesting today, and I've passed out my written testimony of which I'll give just a three minute summary, actually creating a program called the Mortgage Crisis Job Training Program.

If you look at the report from the Governor's task force, and you look at the top 30 communities with respect to the number of sub-prime loans, we've done some research and noticed that there's a striking correspondence between the highest rates of unemployment and those actual 30 communities.

If we were to serve people who are either in foreclosure or into delinquency in a serious way, it would be very difficult under the current kinds of limits and funding that work-force investment boards have.

Most of our money comes from the federal government, onto the State Department of Labor, and then onto us. Under the Work Force Investment Act, the income restriction for a family of four would be $46,000. We could not serve anyone in any capacity who earns anything beyond that.

We all know this will not be a short-term problem. As the reset dates occur there will be more and more coming into a state of need each and every year.

So we have a program here that we've outlined that I think will provide the kind of services that people need. My idea is to work with the banks and the lenders to ensure that they give

notice to folks who are either in foreclosure or are moving at least 90 days delinquent on their mortgage.

And make them aware of the existence of work-force investment boards and to send them there to give us a chance to work with them. And I'm talking about people who are both unemployed and under-employed.

I think you'll find the vast majority here are probably under-employed. Give us a chance to work with them and to create placement centers for them and develop programs of training that might help them.

Now, why is this important? Because when you upgrade people's skills in Connecticut, they can earn more. Sometimes families have to understand what their capacity is to learn and the whole family has to work at these things.

We can provide the family's support programs that can ensure that they're taking advantage of federal and state programs that can be of help to them.

So I've given you two options in my report. One is to attempt to do this as a pilot in the two communities that have the greatest need, one being southwestern Connecticut, which would be the greater Bridgeport region from the Naugatuck Valley right to Greenwich, and the other being the greater Hartford area. That's measured by both the sub-prime loans and by the unemployment numbers.

A pilot would cost about a million dollars, half a million for each region. And with that each region could serve anywhere from 112 to 150 families. To do it statewide would cost between $2 and $2.5 million.

Since it's going to be a long-term problem, I suggest that we do a pilot. But I'm suggesting that we replace the kind of despair that's there with some hope and restore some sense of dignity through the dignity of the job.

So, I add that for your consideration and I certainly thank you all for having me here today and I will take whatever questions you might have.

REP. BARRY: Representative Moukawsher?

REP. MOUKAWSHER: Thank you, I appreciate the hope. I'm not sure how this would work. You generally work to find employment or re-train people and it seems like the biggest component of our problem right now is that people have taken mortgages they can't afford. How would you help those people in a little more concrete fashion?

JOE CARBONE: We can help them in two ways. There are many folks that are earning under their capacity. That is to say they have the potential for greater skill levels than what they currently have, and in a market like Connecticut, where the unemployment rate for the state has been low for a good number of years, the great your skill level, the greater your earnings.

So if we can bring them into the one-stop system, and we have resources to actually serve them, and we ensure that they're taking advantage of all the family-support programs that they're entitled to, then we can help them through a testing process, and an assessment process.

With the proper resources we can provide them training opportunities that can put them in positions where their earning capacity can grow.

Now, to the extent that the cost of their monthly mortgages have increased, that will help. To the extent that families need help with respect to looking at the whole family, and not just the person who's the apparent bread winner, and trying to work with the system to empower all of them with skills and make them earners. I guess that's the way to react to this thing.

I know there are a number of cities around the nation that are looking at the possibility of employing this job training element as part of the sub-prime loan problem.

We're prepared to do it as part of our state's work-force system. It's a case of dollars to do it and to do it well and to do it right. The federal dollars are just not sufficient, but most of all they're just too restrictive to allow us to serve very many people on this.

REP. MOUKAWSHER: I noted in your remarks that you said, each work force board can build upon relationships with local lending institutions to enable good-faith community reinvestment.

I'm not sure if that means that you would, in the case of somebody who was in trouble with the local bank, say, look, let us work with this person. We can get them back.

But if that's in fact what you mean, a lot of our persons in trouble now with their mortgages don't have local state banks as their lender. How would you stop the worst case of foreclosure to retrain somebody? How would you accomplish that?

JOE CARBONE: Well, we're not into the business of banking or lending, so I can't answer the question as to how it might stop foreclosure. I can address the need for a person or for families to increase their earnings, and using their skill capacities to make it happen.

But I can also tell you that we work with the banks. Each of the work forces boards does training and we do a lot of referral for the folks who come through our doors.

Just to give you an example, in southwest Connecticut we've got three One-Stops, one in Bridgeport, one in Stamford, and on in Derby. 22,000 people per year come through our doors, so we're a resource center for all the banks.

In the case of the workplace, we get contributions, mostly philanthropic types of

contributions, from the banks, and we use that money to provide retraining opportunities that people need. But there's never enough federal money to make that happen.

So, I would commit that we work with the banks and the lending institutions. I don't know how much of this might cover the banks that are covered by the Federal Reserve, but we work with banks now to help them meet their obligations under the Community Reinvestment Act. I don't know how many of those banks might be involved in having folks who are subject to foreclosure or serious delinquency.

I think there are ways out there to get these lending institutions and banks to be partners in this to the extent that we can strengthen their customers and place them in a better position, too.

REP. MOUKAWSHER: So I think that maybe what you're role would be is that with the number of people that would have sub-prime mortgages, as you've outlined here, you would be helping them meet their obligations.

And as their interest rates are reset, you're going to help them have the ability to afford and pay for that instead of going into a delinquent situation.

JOE CARBONE: Exactly, and right now they are all facing it. I can tell you one very quick story.

I met a gentleman who is in foreclosure, in fact, there's apparently a sign in front of his home stating he's in foreclosure. He had lost his job. So it's both a case of being unemployed and an interest rate that spiked up. We are working with him right now, and it's a very tough case. I don't think we'll be able to avoid foreclosure.

But, we are doing other things for him. We have helped him with programs with respect to cost for energy, with food stamps, and lots of other things that are helping him and his family get through this.

He's go two children who are embarrassed at the notion of seeing the foreclosure sign up. We've obtained work for his spouse, and we've got him thinking about a new career. He is one that had more potential than he was currently earning at.

So we do a lot of that, but I think in this case we'd have to market it. We would have to work with the banks and make sure that the referrals are made. Obviously, we can't get the names unless the lending group or bank made that referral.

Once we brought them in, as I spell out in my statement, we would use the case-management tool, do the assessment, consult and test to help people reach their full potential in their careers. That will make them greater earners in Connecticut which would mitigate, not all of this, but certainly some of this. Thank you.

REP. MOUKAWSHER: Does anyone else have any questions? Representative Ryan.

REP. RYAN: Sir, thank you for waiting all this time. Quick question: as long as this is a multi-part problem, and as long we're looking at all these bills, are you unselfishly volunteering to be grafted into whatever solution we come up with on Tuesday? Did I summarize that pretty well?

JOE CARBONE: Yes. I want to be a part of it. I think we can turn this whole thing. This has been an extremely sad experience for an awful lot of people. I think we can put some hope in this and take advantage of that great dignity that comes with work.

We can do that. We can put a lot of kindness into it and we can really, really help people.

SEN. DUFF: Thanks Joe, for coming and testifying in front of us today. I just want to thank you for bringing this concept to the committee's attention. I know it's something you've just heard about recently and brought it to our attention.

I think it's a way of us thinking outside the box a little bit, and thinking of creative ways to not just look at this from a one-dimensional standpoint but to really being to wonder how we're affecting the entire economy of the state and how are we helping people get back on their feet again. Rather than just throwing out the life preserver, we should really be trying to fix the boat, I guess.

JOE CARBONE: It's probably more important with respect to the next 12 or 24 months of reset dates. As new folks come on or people are approaching a point where they're 90 days delinquent. Those are the ones that I think we probably have the greatest degree of chance of saving.

SEN. DUFF: Great, thank you very much, Joe.

JOE CARBONE: Okay. Thank you very much for having me.

SEN. DUFF: Turn to Dave Weiss. Good afternoon, Mr. Weiss.

DAVE WEISS: Good afternoon. Chairman Duff, Chairman Barry, Members of the Committee, I appreciate you all hanging in there. It's been a long day. I appreciate you giving us the opportunity to speak a little bit.

You have over 20 bills on your agenda to day, and we have a number of comments on quite a few of them, but I don't think time will permit me to go through them all, so I think what we'd like, with your permission, to do is really focus on Raised House Bill 5577 and submit some written testimony after the fact on some of the other bills so that our position—

SEN. DUFF: Do you have any written testimony now?

DAVE WEISS: Not at this moment.

SEN. DUFF: Okay. That's fine.

DAVE WEISS: With Raised House Bill 5577, AN ACT CONCERNING RESPONSIBLE LENDING AND ECONOMIC SECURITY, we really are trying to address a very serious problem. There are a lot of victims out there and there have been a lot of abuses that need to be addressed and we applaud the committee and its efforts to do that.

As we go through each of the provisions of the various bills that are out there, you read through them and realize there's a lot of common themes and a lot of predatory practices that need to be addressed.

Different bills have different approaches to this. Some, well all, are well intentioned. And I think as we go through each provision we ought to keep a couple of themes in mind. I'd like to respectfully offer some of those themes.

One: We've got to always remember that the prime markets really didn't contribute to this crisis and we need to preserve access to the prime market and make sure that it's a robust market, particularly in our economy right now where things are a little bit tenuous and the housing market seems to be in a decline.

The prime market will be the fuel that hopefully at least partially sustains the housing market and part of Connecticut's economy.

With respect to the non-prime market, there is a serious credit crunch going on there and we

don't need, with any legislation here, to exacerbate the credit crunch.

In fact, we hope that what we come through with is carefully targeted legislation that deals with the problems of the sub-prime market, but leaves behind the opportunities for responsible lending, because as we've heard before, in order to bring people out of this crisis there needs to be credit available to help them into the next day.

So, we really have to look at some of the unintended consequences of individual provisions. And we also have to recognize that federal preemption's going to play a significant role in policy making here.

The commissioner has testified before that the community state charter banks didn't cause this problem. And it would be a shame if we would up with some provision with unintended consequences that only applied to the state charter banks and made them less capable competing going forward and maybe a flight to the federal charter which means fewer banks under your jurisdiction and that report to the commissioner who's done a really good job of making sure that the banks have not been irresponsible.

The proof is that the Connecticut state charter banking industry has been very responsible in this.

Let me conclude by saying we support House Bill 5577. It's got some really good concepts in

it, it's a great starting point for a lot of very important discussions. There are a few areas, respectfully, that we think are well intended, but may have some unintended consequences.

We'd like to work with the committee leadership, the banking department, and with all the participants in the market place to try to come up with something that is carefully targeted, makes sense, and that help to lead us out of this crisis.

REP. BARRY: Thank you very much, Mr. Weiss. I think it's pretty clear to us that we want to preserve the prime market. There's no doubt about that. We appreciate your willingness to work with us on perhaps improving the House Bill 5577 if there are things in there that you've noticed as deficiencies in our bill.

One thing I just wanted to ask you was if you could explain to the committee the significance of regulating pre-payment penalties. That is a very complicated topic, and I have difficulty getting my hands around that.

We all kind of know from previous speakers what a pre-payment penalty is, but the significance of regulating it, whether it's non-traditional mortgages or non-prime.

In the House Bill 5577 we want non-prime regulations, but there are other interest groups that would like to see regulations of non-traditional mortgages and pre-payment penalties in those.

DAVE WEISS: Like many loan features, pre-payment penalties have a viable and legitimate purpose in loan products, whether it's a prime-loan product or non-prime-loan product. The unfortunate part is that like many legitimate feature there are some people who abuse those features.

But let me just talk about some of the legitimate uses of pre-payment penalties so we can understand that we don't want to throw the baby out with the bath water. We want to have carefully targeted legislation that allows certain types of pre-payment penalties to survive.

One example of a legitimate use is in home equity loans. I don't know how many of you have home equity loans, but these days the industry is giving those things away.

There are no closing costs to obtain a home equity loan today. Right now the bank or the lender eats all the up-front closing costs. They pay for your recording costs, the credit report, the appraisal, and the flood certification fee. There's a whole host of things that the bank eats.

The reason they're doing that is because they will often time build in a pre-payment penalty as an option. They will have other products that don't have that penalty. In these products you may pay up-front fees because over time they expect to earn the money back.

But if you take that loan out with no cost to the lender and repay it too early before they've had a chance to earn the cost back that they've eaten plus some profit on the loan, then the product doesn't make sense anymore.

If you were to ban pre-payment penalties in that context, whether it's a prime product or a responsible non-prime product, you take that product off the market and you have lessened choices. That's a legitimate product for some people.

Another example: It's typical in loans that are being sold into the secondary market that lenders often times will retain servicing and they'll get paid to service the loan.

When pricing the loan, they are taking into account somewhat of a "guesstimate" about how long they'll be able to receive those servicing fees.

One way that you can be relatively certain that you'll be able to receive those servicing fees for a reasonable period of time and thus be able to reduce the interest rate on the loan because you know you're going to get some servicing fees out of it, is to put a pre-payment penalty on there. And this is a legitimate purpose for it.

Again, there are products without pre-payment penalties as well, so borrowers can pick and choose. If they want the lower rate loan with a pre-payment penalty, and if it's adequately disclosed, and truth in lending does disclose

pre-payment penalties, then that consumer can make a legitimate choice to obtain a lower-cost loan with a pre-payment penalty.

So, again, I'm just trying to give you some examples of legitimate uses. I think where some of the abuses came in of pre-payment penalties, and believe me there are some very bad actors that have entered the market place, is where the pre-payment penalties have been tied to these absolutely, horrendously priced arm products where they're deeply discounted for the first period and then tied to a very high interest rate when it resets. These products often have no opportunity to get out of the loan because of the pre-payment penalty.

Usually, within these types of fraudulent transactions, we're not talking about responsible lending activities, the broker and the irresponsible lender have not really made sure that the person can afford the loan at the reset rate.

So there's the abuse that we're talking about, and everybody wants to ban pre-payment penalties but let's not throw the baby out with the bathwater.

REP. BARRY: Thanks. That's a very helpful explanation of that. Obviously there are people who have differences of opinions on that and I appreciate your opinion.

Most loans that I see have, say, on a 30-year fixed loan it will say, if there's a pre-payment penalty it will be disclosed, but it

will say that it may or may not have a prepayment penalty in this loan.

Is there any reason why most of these loans say six months interest as opposed to two or four months interest?

If you've got a 30-year fixed loan and you have a three year arm and you want to refinance it after two years, you have to pay six months interest to refinance, which amounts to $6,000. If you paid three months interest it would obviously be cheaper to get out of the deal.

DAVE WEISS: I think it depends on the economics of the transaction itself. In the types of scenarios I've described to you before, the higher the closing costs the lender eats, the longer he needs the borrower to be in the product. Did I answer the question? Did I understand the question correctly?

REP. BARRY: Yeah, you did. With respect to yield spread premiums, are there instances where yield spread premiums, in your eyes, is a yield spread premium a lender kickback? Is it a bribe? Are there legitimate reasons for yield spread premiums?

DAVE WEISS: Again, this is another example of a concept that arose as a way to differentiate different products for legitimate competitive reasons that has been abused by some of the bad actors in this marketplace.

I think there's been a little confusion surrounding what exactly a yield spread premium

is. It is a form of broker compensation that is tied to the yield on the loan. But brokers get compensated in a bunch of different ways.

There are legitimate honest brokers out there who do a lot of work and they deserve to be paid. The question becomes, in a responsible loan, there are some buyers who want to reduce their up-front closing costs, and there are others that may be willing to pay some larger up-front closing costs.

For those who don't want to pay the larger up-front closing costs, the lender will say, all right, you don't have to pay your broker. I will. I'll pay all or part of the broker's compensation, but I'm going to increase the interest rate. And the consumer says, you know what, that's a fair trade off.

If they're informed of it, which RSPA requires disclosure yields for premiums (whether or not it effectively does that is open for debate). In theory, an informed consumer will be able to say, you know what, that's a legitimate choice for me. Do I want to pay--

REP. BARRY: I'm sorry, did you say RSPA?

DAVE WEISS: RSPA, yes. Actually on the HUD-1

REP. BARRY: On the HUD-1 there's always the Y-L-S for yield spread premium or it could be hidden as points, I suppose.

DAVE WEISS: This is part of the confusion on the part of consumers, because this does get

complicated. When the lender is paying a yield spread premium to the broker, that's not something the consumer pays up front, so it doesn't belong in the right-hand column on a HUD-1 because it's not part of the cash that's changing hands from the consumer to the lender. It's the lender that's paying it behind the scenes.

That's why you see the yield spread premium in the left-hand side of the HUD-1 saying POC, paid outside of closing.

Therefore, it's not a direct cost to the consumer and it shouldn't be part of the APR because it's not a cost at closing, because the lender's paying the broker for the consumer.

Having said that, the APR reflects the indirect cost of that because, as I mentioned before, what happens is that the lender gives the consumer the choice. Do you want to pay lower fees and a higher interest rate so we'll pay your broker, or do you want to pay the broker up front and have a lower interest rate?

What happens with the APR is that it goes up because the interest rate goes up, not because the lender pays the broker the yield spread premium behind the transaction.

In that context I hope you see that it can have a responsible product usage, or can be a responsible product feature.

Unfortunately, there have been abuses of it because yield spread premiums do provide the

incentive or opportunity for irresponsible and unscrupulous parties to try to steer people into higher price products so that they get larger yield spread premiums. Again, the amount of the compensation is based on the yield of the loan.

RSPA tries to deal with that [Gap in testimony. Changing from Tape 4A to Tape 4B.]

--with yield spread premium compensation and with what is legal and what is an illegal kickback, if you will, under RSPA.

Unfortunately, I would submit to you that it's not working very well as evidenced by the crises we are in right now. There are laws out there that try to address the difference between a legitimate use of yield spread premium and an illegitimate use.

REP. BARRY: Thanks again. This is become kind of like a battle of the experts, because I've heard you explaining this and it sounds like it makes total sense to me.

Then I've also heard people testifying prior to you that have a much different characterization of what a yield spread premium is. I appreciate your comments.

With the yield spread premium, if we were to regulate them for non-prime loans like we are in Raised House Bill 5577, is there any kind of [inaudible] effect on the market at all?

Will it affect the market ff we're regulating to the extent that we say you have to disclose them to the borrower in a different way than we're doing now because the feds aren't really helping us do it because whatever rig it is in under, RSPA isn't really helping the consumer out enough.

If we're making sure it's clearly and conspicuously explained to the borrower, and we're also doing further explanation, in laymen's terms, of the cost of that yield spread premium over the term of the loan, even though that may conflict with what your definition of a yield spread premium is anyway, will it affect the market?

What would you suggest in light of the fact that people have been abusing the yield spread premium in this market, as being some kind of remedy to try to address that going forward?

DAVE WEISS: That's a very hard question. I don't think there are any perfect solutions to this. If you ban yield spread premiums, I think you have [inaudible] issue. I think you have an un-level playing field.

The federally chartered institutions may very well come in and say that it's a legitimate form of compensation that they state laws preempted and there may be competitive battles that go on to get loans from certain sources. The state chartered institutions may lose out to the federally chartered institutions that are still using yield spread premium compensation.

Can you cure it with disclosure? I think the disclosure scheme that's in place right now is inadequate. I think that there can be better disclosures. I've seen better disclosures of yield spread premium.

But like everybody, I think, that's been up here, and I'm sure you've had the same experiences, adding another piece of paper to an already complicated closing tends not to change the dynamics of thing tremendously, particularly for this segment of the market place, where often times English may be a second language or they may not have the education levels that some of the prime borrowers have.

Again, I don't know that it would hurt, but I'm not sure it's going to have the complete effect that we'd all hope it might have.

REP. BARRY: Alright, and just one final question in general. You'd be a good person to ask this to. The cost of the loan concept, I was just trying to get my hands around this the other day. This is all about making sure we're not going to do anything here in the legislature that's going to create more of a credit crunch if there's one already.

When a bank has an interest rate going out on their deposits and CDs to holders of those products, and they're doing loans at a certain rate so they're bringing money back into that bank, we want to be able to make sure that

banks are profitable enough, I assume, to continue giving loans out to people.

One of the concerns I have is to make sure that the non-prime definition in this bill is going to ensure that the banks don't, at some point eventually, if the stock market's going a little crazy and the T-bill rate goes down, all of the sudden find themselves with loans that are coming into the bank at a lower rate than what they're giving out.

It seems to me that this is the potential problem of a definition that is misdirected. Can you comment on that?

Dave Weiss: I think that the trigger definitions are really critical to any piece of legislation that comes out. There can be a lot of different debates about what the right indexes are to use here.

What's in your bill is in part what is known as the [inaudible] index triggers, which is a set of indexes and triggers that were put into place by the federal government for a completely different reason; not to address the sub-prime crisis. So there is debate about whether or not that is the appropriate trigger.

Part of your bill also includes some additional concepts adopted in North Carolina where there's a backup index there that may be helpful in different rate environments.

This is a hard one, because right now the market is very dynamic. It is changing very

rapidly. Just recently, Freddie and Fannie, who a lot of lenders sell to, changed the pricing matrices for loans that banks sell to them.

So there are some new points being added to a variety of different types of loans with different types of credit profiles depending on loan to value ratio, credit scores, whether the property is single family or multi-family.

Those additional add on points are now challenging for us in determining whether or not we consider conventional financing. The APRs on that is now getting up very close, if not in some cases we fear in excess of the triggers we're talking about n this bill.

We don't know whether there are other shoes to drop, whether the mortgage insurance companies are going to come in with additional charges. And all of those types of charges tend to be pre-paid finance charges, which increase the APR.

So, one of the fears that we have with the definitional triggers is that the conventional market place is going to slip over the trigger, pushing us into the next highest tier—the non-prime tier—which is subject to additional regulation and restraints and reductions of flexibility that are going to not only restrict our ability to be competitive, but it will also restrict our ability to serve that segment of the community which we really want to serve.

It is a critical issue, and I would very much encourage you to give consideration on the data of modeling on the different indexes and what they do different rate environments and things like that. And also, perhaps push some cushions on there just so we're not in the type of situation that I just described. I hope that was responsive.

REP. BARRY: Yeah, thank you very much. That was very helpful to me. Anyone else have any questions for Dave Weiss? Thanks very much. Oh, wait, I'm sorry, Representative O'Neill.

REP O'NEILL: You reminded of yield spread premiums. I'm not sure I understand. Is there something we can do as a legislature to provide a disincentive to the abuse?

You seem to distinguish between legitimate uses and illegitimate uses of the yield spread premiums and I'm wondering what, in your mind at least, is the distinguishing characteristic.

DAVE WEISS: Again, no perfect answers, but I do think some better disclosures, while not a cure, might be helpful.

I also have asked myself what has caused the state charter banking industry, and the banking industry in general, not to be the ones we're talking about right now, what has caused them to be more responsible?

I think the answer is that there is more rigid enforcement and examination of the banking industry. It is just the daily part of a

bank's life to have its regulators looking over their shoulder.

That, unfortunately, just hasn't been the case in the non-bank market place. There are a lot of very responsible mortgage lenders out there who are very competitive, very honest, and the like.

But I think experience has shown us just recently that there's also been a lot of bad actors who don't have any skin in the game. They fold their tents and they're gone.

I think some additional measures in that regard, plus the examination can help them be more responsible when their house is on the line.

When their money is in the capital that's exposed, they'll perhaps be a little more responsible to the consumer in complying with laws that already exist in many cases.

So, again, no perfect solutions, but just some observations.

REP. O'NEILL: I'm trying to understand what is a legitimate purpose for a yield spread premium and what would be an illegitimate purpose or application of the yield spread premium in your eyes?

DAVE WEISS: A legitimate use of the yield spread premium is when an individual may not have the cash at closing to pay additional closing costs that he or she would otherwise have to pay to

the broker. What happens is the lender says, the broker needs to be compensated because they did work here. We'll pay the broker for you, but you're going to pay a higher interest rate.

If that's adequately disclosed to the consumer they can make that choice not to pay the broker's fees themselves up front but rather to have the lender pay it and increase the interest rate.

It's not financing the broker's fees; it's increasing the interest rate. That is a legitimate choice by the consumer for a legitimate use of a yield spread premium.

Where the yield spread premium abuses have come into play is when the compensation itself is tied to the interest rate. The higher the interest rate, the more the broker can be compensated.

And because of bad standards, that I would submit to you are not necessarily in the banking industry, but elsewhere, the brokers have been able to push, if you will, higher cost loans to lenders who are willing to buy those higher-yielding loans when the consumer is being abused.

That consumer may very well be able to get a lower-priced loan from another source if the market place were to work well. Does that make sense?

REP. O'NEILL: Is there something in the contract between the broker and the lender? I always

get a little confused as to who people are especially when I'm trying to do a closing. I think I'm talking to the broker and it's the lender; I think I'm talking to the lender and it's the broker. After awhile I don't know who I'm talking to.

The people that are the ones who are bringing the borrower to the source of money, the people who are going to send me a wire transfer, those people have, I assume, some kind of contractual relationship with the entity that is going to issue that wire transfer where in the olden days would have given me a check.

DAVE WEISS: Typically, yes.

REP. O'NEILL: Okay, so, can we regulate that contractual relationship saying that you cannot condition your yield spread premium on higher rates of interest or limit the maximum amount of interest or yield spread premium that can be given over?

The things you recited as things that are going to be paid for like a flood certification fee, usually on the RSPA when they are paid for by somebody it's $20.

Most of the things you recited are comparatively modest costs and not tens of thousands of dollars in there. I would think that 4% of a $200,000 loan is $8,000. That's a lot more than any of those costs amount to.

DAVE WEISS: You asked, can you regulate the compensation relationship between the lender

and the broker? The answer is you can. You guys are the legislature, so you can certainly pass laws that attempt to get to that relationship.

I would go back though, and urge you to give some consideration to preemption issues as you do that, because there may very well be federally chartered institutions that may say that the law interferes with their ability to conduct operations under their federal charters. Therefore, the state laws preempted leaving behind the state chartered banks to have to contend with that.

REP. O'NEILL: I think you just indicated that those are the ones that seem to have the least problems right now.

In other words, the abuse seems to have been those guys from out-of-state. I was on the phone with somebody in New Jersey and then their other division is in Mississippi, and another piece elsewhere, so I talked to five different states in one mortgage transaction.

None of them are here, so it all seems like some sort of Internet/Ethernet that is kind of floating out in outer space someplace.

DAVE WEISS: If you're brokering a loan in Connecticut, or if you're making a loan in Connecticut and you're not a bank, you have to be licensed, and that puts you subject to the jurisdiction of the Connecticut Department of Banking. For a variety of reasons, those entities have not been examined as often or as

rigorously as the banking industry is, and that my be part of the problem.

There are laws on the books that, including RSPA, that do restrict the amount of yield spread compensation that can be paid by the lender and received by the broker. If it's excessive it can be deemed to be a violation of section 8 of RSPA which deals with kickbacks and illegal referral fees.

REP. O'NEILL: How much is excessive?

DAVE WEISS: You have to know it when you see it, unfortunately, because it's a changing market place out there. It's reasonable compensation. The broker, or any settlement service provider, whether it's a lawyer, or a title insurance company, or a broker, can only receive reasonable compensation for the services that they actually render.

So that to the extent that the broker is rendering lots of legitimate services, the amount of compensation they can receive goes up, and its judged by the local market place under Section 8. So the market place sets the compensation for the services that are being provided.

Candidly, to the extent that the market place is paying high fees for services and part of that may be deemed to be illegal, in excess of what is reasonable, it may very well help to goose up the argument that it's reasonable because other people are paying it.

REP. O'NEILL: Well, in the olden days, you walked into a local bank and filled out a mortgage application. There was a person who sat there, and I don't how much they were getting paid, but given the car they drove and the clothes they wore I didn't get the impression that they were getting paid $1,000 for each application.

They were getting paid a salary and it was probably comparable to what legislators get paid, maybe a little bit more today, but it wasn't a huge amount of money. And it wasn't 4% of the value of a $200,000 dollar loan. It wasn't $8,000.

So, in other words, if I use those people (and there are still some banks that operate that way) and look at their salary and what they get paid per hour and then look at how may hours it takes to process one of these loans that's being brokered through six different states to find an entity that's going to issue a check or send a wire transfer, if I use that a measure of compensation then it doesn't take long at all to figure that a lot of these fees are excessive.

DAVE WEISS: Yeah, if you look at the compensation litigation out there it's all over the place, frankly. There's no one answer to your question, candidly. Again, there are laws on the books that deal with this that have just not been effective.

REP. O'NEILL: But if the law says reasonable or fair, I mean those are great words, but inevitable they require you to litigate and

probably bring in expert witnesses and it's going to cost a lot of money.

A lot of times when you have a lot of litigation going on is when the legislature steps in and says, okay, here's the number. Or perhaps they can authorize the banking commissioner to issue some regulations on the numbers because we're not there's not one number that can be used. It's where you step in and try to draw some black-letter lines.

DAVE WEISS: As a general rule, we are not in favor of rate or fee regulation. We think the free market normally works. We do know that there are places where it sometimes doesn't work and we recognize that this is a tough issue, but we would try to come up with solutions that do not involve saying you can't pay more than a certain amount of money on that transaction.

Enforcement is a big vehicle. In part, the banking industries avoided this because they had the examiners in looking at that compensation.

REP. O'NEILL: I guess it's not a question, just a comment. Whenever I did one of these transactions, I always felt sort of bad because the bank down the street that pays local taxes, hires people, donates to the United Way, and does all those other things that most of these mortgage broker outfits don't do, and kind of come and go with the changing of the seasons almost, I always felt a little unpatriotic from the standpoint of being a citizen of Connecticut.

But this is what my client brought me as who their lender was going to be. I always charged them a little bit more for dealing with these out-of-state outfits because they were always twice as difficult to deal with in terms of communication, paperwork, and understand what they wanted.

It would be better for most people, if they could do it, to deal with a local bank based here in Connecticut than what they were dealing with elsewhere, getting a ¼% on the interest rate or something like that. But everything else that went with this was much worse.

It would be better for the industry in Connecticut if there was not this, what I always saw as, potentially unfair competition because they weren't bearing a lot of the expenses and costs and the long-term consequences of what was going on at the time.

I'm just saying I think the bankers in Connecticut would be better off if they didn't have to deal with these outfits that come breezing in from out-of-state when the market is good to cream off some of the business for those folks that will get ten truth-in-lending statements and go with the one that shows the lowest rate on the APR because that's all they're thinking about.

DAVE WEISS: If I could respond to that, we enjoy honest competition. We really do. We want competition to be there, but it's the unfair

actors out there that nobody enjoys. And the consumers are victims.

SEN. DUFF: Thank you, David. Okay. Frank Haran?

FRANK HARAN: Good afternoon.

SEN. DUFF: Good afternoon.

FRANK HARAN: Chairman Duff, Chairman Barry, Members of the Committee, my name is Frank Haran and I'm here representing the Connecticut Mortgage Bankers Association. The Mortgage Bankers are made up of banks, mortgage companies, and brokers. I am a mortgage banker.

My comments today will be on Raised House Bill 5577 and Raised Senate Bill 423.

I was especially interested in the Emergency Mortgage Assistance Programs Committee and their responsibility to develop emergency mortgage assistance programs. I Googled HERO and REAL and read about Pennsylvania.

I think it's a very good program, and I like HERO the best, although there are a couple of problems with HERO.

I think we have to accept the fact that if you're going to refinance or modify a sub-prime loan, owing to the initial poor credit quality, owing to the fact that income was not verified and could have been drastically overstated, the prevalence of 80/20 in low equity and high loan-to-value loans, it is really difficult to

make this loan work in such a way that the borrower can pay back the debt.

I realize that you people are very frustrated. You've shown it with CHFA and with others. There will be problems with this loan, too, because of the nature of the loan that you're trying to repair.

I have a lot of other comments on that, but I'd like to skip those unless I'm asked to go back, to talk about the bills themselves.

My problem with all these bills is there's an entire mortgage industry that doesn't do sub-prime. There are brokers, mortgage bankers, and banks that do fixed-rate loans. I get the impression as I listen listening today that we feel we have to change the entire industry, and we do not.

Section 5 of the bill requires the mortgagee to notify the borrower of the existence of lost mitigation programs. FHA has a rule that you have to do that on 45 days.

CHFA has a rule that you have to do that on 60 days. Does this mean that we would, having failed to get the borrower to go into lost mitigation, again have to ask them to do the very same thing?

You have private mortgage insurance companies who also have programs. A private mortgage insurance company is a typical insurance company. They want to collect the premiums and they don't want to pay. If they can get the

borrower to stay in the house and modify the loan they'll attempt to do that.

My concern is that the law does not take into account that there are professional, existing, competent companies that do this.

The other problem I had is the ability for the judge, after the state program has rejected the borrower, to call for a six-month delay. I quite frankly think there is not a better program out there for the borrower than the state programs, and if the state can't do it, I don't think it serves any purpose.

I especially liked Section 9 and the attempt to define non-prime or sub-prime loans by pricing. I think that's an excellent idea. I don't have any problem with the [inaudible], they seem to be appropriate.

Traditionally the ten-year T-Bill has dictated the rate of a conventional loan, and I like the fact that we are using the Freddie Mac 60-day rate which is what they call the conventional rate.

However, today jumbo loans, PMI conventional loans, and FHA loans all could fall into sub-prime by the definition here. The credit crisis has increased the price of jumbo loans greatly.

That's because jumbo loans are not guaranteed by the federal government like FHA and they're not guaranteed by Fannie Mae or Freddie Mac.

Therefore, the price of jumbo loans has risen significantly.

This really started, I guess, in July, and then it got worse and worse. Perhaps it will recover, but right now pricing is changing, sometimes on conventional loans two and three times a day.

Concerning high-rate PMI loans, it's been discussed before, that on any loan that's between 65% to 95% based on credit scores, Freddie Mac and Fannie Mae are lowering the price they they'll pay.

A borrower with a 740 credit score, which is well above average, that has a 95% loan, will pay a half a point from Freddie Mac right now.

So this is new, and it's included in the APR. All the charges that we give, the borrower ultimately pays for.

Every FHA loan, which is guaranteed by the government, pays 1.5% mortgage premium up front, even though that is added to the debt in 99% of the cases. That is considered a finance charge.

Therefore, and FHA loan of 6.5% has no points when you're talking a cap in the low 7's. Because of the 1.5 point MIP, you can find FHA who quite honestly has the best lost mitigation program available and does not surprise the borrower. FHA could be classified, as high-cost or non-prime, and the Senate Bill 421 calls it sub-prime.

I like the law and the concept if you can possibly allow for flexibility in an annual check or a bi-annual check or something so that it can reflect the market place. I am told that these collars or margins were picked three years ago. I have no idea if that's true. It might have worked three years ago.

My point is that I think the margins ought to be reviewed. I think upon passing, or if we put this in, I think conceivably the regulation laws should allow the banking commissioner, or whomever, to change the margins based on actually running a lot of loans through statistically.

Section 19 calls for the current holder of the note or the assignee to have liability to the borrower. Although it's been said that the federal government will not pass the current law that's through the House, that is highly contested.

Most of your big aggregators are commercial banks today. And commercial banks operate retail as well as wholesale operations. Anyway, I would like to not lead that. I would like us not to be the state that forces the banks to consider whether or not to withdraw.

As for Raised Senate Bill 423, I like most of the things they are doing. I like the restrictions, the real problem I have with Raised Senate Bill 423 is the yield spread premium as a prepaid finance charge. You've

already received an excellent explanation of it.

We can go further, but the bank makes money on that loan or they wouldn't do it, and they don't have to tell anyone what their spread is.

The mortgage banker who funds the loan doesn't tell you what he's making, mainly because they sell the loans after the closing. It's not considered part of the closing.

And quite honestly, the mortgage banker does not know what he's going to make. He's taken steps to ensure or protect what he's going to make, but he will find out in a month or two how much money he'll make on the loan. That does not help the borrower.

All these things were drafted because of the broker who gave people loans they could pay. What I'm looking for is in your remedial action to not ignore the existing laws. And there are a lot of responsibilities when you're dealing with prime loans.

Freddie Mac and Fannie Mae, I've said before, have a four trillion dollar portfolio. If they think I've committed fraud they ask me to buy the loan back or they will not allow me to sell anymore.

FHA is the same way. If they don't like the underwriting, and they audit every delinquent loan, about 10% of the loans, they ask me to buy it back.

I run wholesale where I work, and I will then go back to the broker and determine whether or not there was fraud committed, and we'll stop doing business with the broker if that's an issue.

So the broker is responsible to me and I am responsible to the investor. There's too much money involved. People don't just say, "That's nice, don't worry about it, we'll continue to buy loans from you" if they feel you've committed fraud or if your loans are paid off too quickly.

If you have a loan that's paid off in four months you have to return all the money to the investor. That has something to do with your prepayment; it's the same theory.

They are evaluating the price of the loan based on the present value of the servicing rights, and also what the loan is worth today in the market place. No points means a higher rate.

I'm fine. I'm done.

REP. BARRY: Thanks very much, Frank. And I would say that your company has a sterling reputation out there in Connecticut and I think, with the people on this committee, I imagine that I speak for everyone.

I just wanted to ask you about your comment about he mortgage lender not knowing how much they're going to make off the yields spread premium at the time the transaction is consummated--

FRANK HARAN: We are selling the loan forward. We hedge the loan. We sell a mortgage-backed security forward and try to fill it with the product if we can. If the market changes we may pair off the security and sell it directly. We may fill the security. We may only sell forward 70% of our pipeline. If rates go down we probably won't close 70%. If rates go up we'll probably close 100%. There are certain risks involved in it.

REP. BARRY: Does anyone else have any question for Mr. Haran?

FRANK HARAN: There's one thing I'd like to say about appraisal value. There's a lot of talk about appraisal value when you're rewriting a loan.

I don't think appraisal value is your biggest problem; I think your biggest problem is what the borrower can afford to pay. You want to give them a loan that they'll be able to keep, and if you have brought the loan under the HERO program from a sub-prime operation, the mortgage your bought is probably greater than the appraised value.

The mortgage that the borrower can afford is probably less still. So what are you going to do with that?

Also on the HERO program, the people who could not make the real program are given to the REAL. That means they have a lesser credit score.

And when you start talking credit scores in the 500's, these are messy credit lives. You may not be able to get a first mortgage position on the new loan that you're writing because they are already delinquent. There's a lien on there taxes, there could be a lien from the condo; there could be any number of liens.

So you've got the borrower not being able to pay the entire amount that you've brought, and now you can't get a first mortgage unless you pay the taxes, the condo fees, and all other liens. So it's very hard to get everything that works in.

FHA has a program called Secure. I have been told, I can't guarantee it, it's been out for six months, 400 in the entire country have been written. This program was designed for sub-prime. It's very frustrating, I think, but they're also very hard to do.

If you have a $300,000 loan, you might have the borrower paying only on $200,000, and the remaining $100,000 in a second position that wakes up when he sells the house. And if you want a first position you may have to increase that $100,000 to pay off encumbrances. When the loan didn't make sense to begin with, it's very hard to have it make sense at all.

REP. BARRY: Yeah, thanks very much. You're very helpful. Andrew?

ANDREW PIZOR: Thank you. My name is Andrew Pizor. I'm a staff attorney with the Connecticut Fair

SB423
HB5577
SB21

Housing Center. I'm generally going to speak in support of Raise Raised Senate Bill 423. There are also a lot of great things in Raise House Bill 5577, so I'm primarily going to concentrate on differences between the two.

You have my written testimony, but I'm going to cover a few other things that have come up today, so I might not get to all the testimony they have written.

First I'd like to speak about Raise House Bill 5577. I think also in Senate Bill 21 there are triggers for coverage exempt to bonafide discount points. I discourage an acting law that does that.

It would really encourage people to try and avoid the law by adding discount points that wouldn't have been on the loan otherwise.

People don't always get the benefit of discount points because people tend to refinance after just a few years. People don't keep the loan for 15 to 20 years, where they would have gotten the benefit of paying down the interest rate by the discount points.

Actually, there are a lot of states that use the same kind of trigger system for their sub-prime lending regulations, but none of them exempt discount points. Connecticut would be the first state to do that, that I am aware of.

Regarding the need to regulate non-traditional mortgages, I believe one of the representatives here, who I don't believe is in the room right

now, earlier questioned whether it was necessary to cover them because they're not as common and not as big of a problem.

According to a government accounting accountability office report only about 10% of mortgage originations in 2004 were what people have been generally calling non-traditional mortgages. That number went up to 30% by 2005, and I suspect it has continued to increase.

So there is a need to regulate them. One of the reason they are a concern is because a lot of people who've gotten into mortgages they shouldn't have been into tried to help themselves by refinancing into another loan that was more affordable. And when people say affordable they usually mean their monthly payment.

Non-traditional loans can look more affordable because if the payment's interest only, or it doesn't fully amortize the loan, the monthly payment will be smaller than a traditional loan, which pays principal, interest, and amortizes over the life on the loan.

So there are people who have, or might be tempted to, finance into these types of mortgages, so there needs to be some regulation to make sure they aren't offered to people who are not qualified for them and they're not abused.

I want to correct what I think may have been a misperception about coverage of prime mortgages. We agree that prime lenders are not

really the problem, but Raised Senate Bill 423 and Raised House Bill 5577, I'm sure you know that better than I do, Mr. Chairman, just sort of floor in general for certain provisions like ability to pay.

I don't think you can find any bank that will admit to making loans without regard to ability to pay. The main banks that do prime lending, they don't do it.

This will just set a floor if anyone changes their policy in the future. This would prevent that problem.

I know I'm out of time. The other issue I was going to cover in my written testimony was yield spread premiums.

There's a very good study from a Harvard law professor published in a Stanford University Law Review, that has a lot of statistics and discussion of the yield spread premiums. I said it in here, and I talk about it a little in my testimony, but I'll be happy to answer question if there are any.

REP. BARRY: Thank you very much. Any questions? Thank you, we appreciate your time. Raphael?

RAPHAEL PODOLSKY: Thank you, Mr. Chairman. My name is Raphael Podolsky. I'm a lawyer with the Legal Assistance Resource Center. We represent low-income consumers. I want to s eak briefl to Raised House Bill 5332 before I say something about the sub-prime lending bills.

SB21
SB 423
HB5577

We oppose Raise House Bill 5332. This is the bill that would exempt Connecticut banks from the retail installment sales financing acts putting restrictions on late fees. There is simply no reason to do such an exemption.

The institutions we're talking about are not preempted federally. They talk about having a level playing field which to me is sort of a strange concept because it's an anti-consumer level playing field.

They are saying that federally chartered institutions, by using preemptions, can charge anything they want as a late fee. They would like to also be able to charge anything they want as a late fee, there it's only fair that they should have a level playing field.

My feeling is the playing field works the other way around. The Connecticut consumers are entitled to the benefit of the statute entities that are not preempted or are not covered by it, and indeed it may be an incentive even to uncovered entities to federal institutions to go ahead an follow it.

I'm told by Attorney Blind who testified earlier that his experience is that most federal entities in fact are following the Connecticut statute, even though arguably they might not have to.

There's no particular reason for a change now, and I don't know what's happened that would make a difference, and I would urge you just to leave the statute alone.

The main testimony I want to make is in regard to Raised Senate Bill 423 and Raised House Bill 5577. We support both of those bills as we also supported Senate Bill 21.

I think it's a real task for the committee to figure out how to meld these together and pull together the best pieces of each of them.

They are clearly inter-related. Raised House Bill 5577 has the first 8 sections that deal with financing sections that are different from the other two bills.

I think there may be some adjustments needed to make sure that these are going to work properly, but the concepts are certainly excellent because those are critical needs to making financing available and to make an expanded amount of emergency mortgage assistance available for people facing foreclosure. So we very much support those.

In regard to the second half of Raised House Bill 5577, and that is the sections that sort of overlap with Senate Bill 21 and Raised Senate Bill 423.

I would encourage the committee to either turn that into a self-standing bill that centers around the content of Raised Senate Bill 423 or to pull more parts of Raise Raised Senate Bill 423 into Raised House Bill 5577.

The previous speaker mentioned some of the areas where there are differences. For

The main testimony I want to make is in regard to Raised Senate Bill 423 and Raised House Bill 5577. We support both of those bills as we also supported Senate Bill 21.

I think it's a real task for the committee to figure out how to meld these together and pull together the best pieces of each of them.

They are clearly inter-related. Raised House Bill 5577 has the first 8 sections that deal with financing sections that are different from the other two bills.

I think there may be some adjustments needed to make sure that these are going to work properly, but the concepts are certainly excellent because those are critical needs to making financing available and to make an expanded amount of emergency mortgage assistance available for people facing foreclosure. So we very much support those.

In regard to the second half of Raised House Bill 5577, and that is the sections that sort of overlap with Senate Bill 21 and Raised Senate Bill 423.

I would encourage the committee to either turn that into a self-standing bill that centers around the content of Raised Senate Bill 423 or to pull more parts of Raise Raised Senate Bill 423 into Raised House Bill 5577.

The previous speaker mentioned some of the areas where there are differences. For

example, the failure to count discount points in the APR.

I really do think that's a loophole that's going to create problems because inherently everybody will argue that a discount point is bonafide, because at least in theory you could charge a higher interest rate.

So I think it has the capacity to be an exception that essentially covers the entire rule and you might end up with nothing left in it.

Similarly, the proposal of yield spread premium should be counted as points rather than simply disclosed.

I very strongly agree that the disclosure's not going to do the trick. Effectively they are points, they should be counted as points, and that makes a difference because in some of this lending we regulate the number of points that you can have on some of the loans.

I want to note one other thing that interests me that I did not put in my written testimony. There's a section in Raised Senate Bill 423 which deals with what's called [Gap in Testimony. Changing from Tape 4B to Tape 5A.]

--this is in Raised House Bill 5577, and what that does is that it requires a housing counselor certification before somebody refinances into a sub-prime loan out of a subsidized loan. This is one of the most

pernicious kind of things that happens in this market.

Which is to say, you've gotten some sort of government assisted loan and somebody comes to your door and twists your arm trying to sell you on some great deal that's better, but it's loaded with prepayment penalties, refinancing restrictions, and with all sorts of other stuff that causes you to give up, through refinancing, this subsidized loan that you had.

And now, a year later, when there's a reset, you can't get your old loan back, you've lost it. So putting in something special that says you really have to make sure people do that with advice. I think that's a good thing and I did not see that in Raised House Bill 5577.

Thank you very much. I know my time is up. I'd be happy to answer any questions I can.

SEN. DUFF: Thanks, Raphael. Any questions? Representative Ryan.

REP. RYAN: Just one quickie. Thank you for hanging in there, Raphael. I noticed you didn't comment on the thing about giving the commissioner, and of course Commissioner Pitkin was modest obviously, but giving the commissioner the super-freeze on the foreclosure power.

My concern, and I got the sense that it might be his concern, was that maybe a dangerous thing to do, or at least not have the

commissioner do it. I don't think I saw that in your comment there.

RAPHAEL PODOLSKY: I did not try to address that. I'm not even exactly sure where that is in the bill. Is that part of the email piece? I'm sorry, I don't recall exactly where it is in there?

SEN. DUFF: It's a case-by-case basis. The commissioner can kind of wave a magic wand and put a hold on a foreclosure on a residence for up to six months.

RAPHAEL PODOLSKY: During the application process?

SEN. DUFF: No, just in general, he just can do it. IF somebody came to the commissioner and said I need you to put a hold on my foreclosure, can you do it, he could do that on a case-by-case basis—

RAPHAEL PODOLSKY: To really answer you with definiteness, I guess I would really need to look at exactly what it says in the bill. I would have though it would be a circumstance that would have had something to do with an application that was pending under one of these programs and as collateral to that you'd want to make sure that a foreclosure is stopped.

REP. RYAN: I don't mean to interrupt, but your thought is, in that context, somebody's got an application in, they're trying to close and they don't want to be facing a law date tomorrow.

SEN. DUFF: Well, we have that in the bill. It does say that while you're going forward through the programs, you basically have a hold on your foreclosure until you're either approved or not approved by the programs.

RAPHAEL PODOLSKY: Right, and that's actually in the existing [inaudible] statute. It's also something that is in the existing Foreclosure Protection Act where if you're application is approved you get a six month stay.

Now, those are done through the court. I guess my answer to your question is that I need to take a close look at it. I'd be happy to get back to you on it. But under normal circumstances I would see that as a structural part of the program, but it would not serve as a free-standing piece for the banking commissioner.

REP. RYAN: I think it's fair to say that you know when our deadline is, so if you want to send a comment back--

RAPHAEL PODOLSKY: I'll try and send it as quick as I can.

SEN. DUFF: Thank you Raphael. Any other questions? Thank you.

RAPHAEL PODOLSKY: Thank you.

SEN. DUFF: Okay. Zina Hill Malcolm, followed by Greg, and then Thomas.

ELIZABETH MATCLIFF: Good evening, hello, my name's Elizabeth Matcliff and I'm an Acorn member and resident of Bridgeport. I'm here today to make sure that working families in Connecticut are not forgotten. As this committee negotiates on the details about Raised Senate Bill 21, Raised House Bill 5577, and Raise Raised Senate Bill 423.

As many of you know Acorn is a grass-roots community organization with more than 2,500 members in Connecticut. I've been a member since the late 1970's. Acorn is more than 325,000 member families nationwide and we have offices in 104 cities.

In every one of our offices we receive calls daily from homeowners in distress. In Bridgeport and Hartford we have membership committees composed exclusively of people with bad loans, individuals with option ARMs, forward mortgages, negative amortization, prepayment penalties, and a slew of other predatory products.

We have members who are lied to by the brokers, ignored by our services, and have been failed by our government. Acorn has directly engaged the major players in this industry, reaching an agreement with Countrywide on servicing best practices that was announced on February 11.

We have met with executives from Bank of America, CitiBank, Gene Mac, [inaudible], Bear Stearns, Lehman Brothers, and others. For years Acorn has been at the forefront of the

fight against predatory lending both in Connecticut and nationally.

We have forced improvements in the practices of certain lenders over the years. Ameriquest, Household Finance, and now Countrywide. But we now have a unique opportunity to pass a strong law in Connecticut that will protect our homeowners and make the American dream a sustainable reality rather than a fleeing hope.

Our sister organization, Acorn Housing, has provided loan counseling services to thousands of families facing this crisis, including more than 100 in Connecticut delinquency counseling. It's critical in terms of lost mitigation, loan modifications, and preventing foreclosures. But we need strong protection on the front end.

I ask members of this committee to listen to the people who deal with this every day. In crafting legislation there should be emphasis placed on the real-world experience of those who have been failed by the current system as well as the advocates work daily to resolve these problems.

Please make sure that any predatory lending bill that passes this committee bans yield spread premiums, includes that rebuttal presumption that the loan was unaffordable and to total amortize of the life of the loan including insurance and taxes exceeds a 45% percent total debt-to-income ratio, prohibits negative amortization language should prohibit payment options which is less than the amount of interest on the debt for a given month.

And if the paid results in the balance of the debt servicing costs be amortized into the loan. Acorn stands committed in our mission to save as many homes as possible and we will do everything it takes to make sure Connecticut becomes a leader in requiring responsible, sustainable lending practices.

Thank you for letting me go over.

SEN. DUFF: Thank you, I appreciate your testimony. Anybody have any questions? Thank you very much. Anybody else?

AUDRA WHITE: No, that's it. Thank you for your time and thank you for staying and hearing us all out.

SEN. DUFF: So Zina, Greg, Thomas, and Michelle are not here?

AUDRA WHITE: Yeah, they all had to go to work.

SEN. DUFF: Okay, tell them we apologize for the long hearing, but thank them for coming and showing their voices and faces and everything else. Is Irving Schlauser here? No? Peter Spalthoff? Rick Tracy? Maria Santana?

MARIA SANTANA: Good evening, Senator Duff and good evening committee members. My name is Maria Santana. I am a resident of New Haven. SB 423

By describing problems I have had in keeping the condominium where I live, I hope you will have an understanding of the need for the law

RICHARD BLUMENTHAL
ATTORNEY GENERAL

55 Elm Street
P.O. Box 120
Hartford, CT 06141-0120

Office of The Attorney General
State of Connecticut

TESTIMONY OF
ATTORNEY GENERAL RICHARD BLUMENTHAL
BEFORE THE BANKS COMMITTEE
FEBRUARY 28, 2008

I appreciate the opportunity to support Senate Bill 423, An Act Concerning Foreclosure Prevention and Responsible Lending.

This legislation mandates greater responsibility for lenders and loan brokers to extend credit to borrowers who can reasonably afford to repay their mortgages and prohibits most egregious anti-consumer mortgage practices.

Under this proposal, mortgage brokers would have a clear, indisputable duty to act in the borrower's best interest. A lender must engage in fair dealing and make certain the mortgage in reasonably advantageous to the consumer. The legislation prohibits mortgage churning, and loans that borrowers have no reasonable likelihood of repaying. For subprime loans -- involved in many home foreclosures -- the legislation requires the creditor to escrow insurance and tax payments and provide the borrower with a list of housing counselors. It limits balloon or adjusted mortgage payments of more than two times the regular payments.

Importantly, Senate Bill 423 provides a private right of action by a borrower who suffers damages. In addition, the Attorney General and the Banking Commissioner may prosecute violations.

Even as the Banks Committee considers House Bill 5577 to address the immediate concerns of homeowners in distress, Senate Bill 423 seeks to ensure that the mortgage debacle will not reoccur.

Over recent months, my office has assisted numerous homeowners facing foreclosure. We have been shocked by some of the mortgage terms and lending decisions by mortgage companies. This measure will help stop them.

I urge the committee's favorable consideration of Senate Bill 423.

RICHARD BLUMENTHAL
ATTORNEY GENERAL

55 Elm Street
P.O. Box 120
Hartford, CT 06141-0120

Office of The Attorney General
State of Connecticut

TESTIMONY OF
ATTORNEY GENERAL RICHARD BLUMENTHAL
BEFORE THE BANKS COMMITTEE
FEBRUARY 28, 2008

I appreciate the opportunity to support House Bill 5577, An Act Concerning Responsible Lending and Economic Security.

This proposal establishes three separate programs to assist homeowners facing foreclosure: (1) the REAL program offers lower fixed rate mortgages to moderate and low income homeowners who face difficulty in making loan payments; (2) the HERO program purchases mortgages from lenders where the property is valued at less than the mortgage and refinances the homeowner at a lower fixed rate; and (3) the Emergency Mortgage Assistance Program provides assistance to homeowners who are in very difficult financial straits.

House Bill 5577 also places restrictions on mortgage brokers, requiring them to act in the best interest of the borrower, and prohibiting any refinanced loan that does not have a net tangible benefit to the borrower. Subprime loans are more tightly regulated, prohibiting prepayment penalties or interest rate increases after default.

This program is not a bailout. It is not a handout. It is a hand up for homeowners, so they can take responsibility for their mortgages at fair market rates. It enables banks to sell loans at steep discounts, avoiding even steeper discounts that occur at foreclosure.

I urge the committee to consider establishing a temporary Connecticut Home Ownership Loan Authority (CHOLA) to issue $100 million in bonds to fund assistance programs and its operations. With a clear sunset provision, CHOLA would provide loans only for two years and then function solely as a mortgage collector for another 20 years. All funds would be segregated from taxpayer monies.

The advantage of CHOLA is:

- no taxpayer money for operating expenses or bond payments
- sunset authority for issuing loans after 2 years -- stabilize market and end
- limited existence to maximum 20 years while mortgages are repaid

Federal officials have boasted of offering a lifeline to homeowners in crisis, but it's more like a shoelace. With our entire economy on the brink of catastrophe, citizens need more effective aid to avoid foreclosure -- and they need it now. House Bill 5577 would keep people in their homes, but impose accountability on them and lenders. This refinancing system, modeled after a successful depression-era program, could spare homeowners from devastation without expense to taxpayers. A nationwide debt crisis is devastating citizens -- not simply irresponsible deadbeat delinquents, but families who have lost jobs, homeowners victimized by unscrupulous brokers and lenders, and responsible borrowers hit by sudden unfortunate financial challenges.

I urge the committee's favorable consideration of House Bill 5577.

February 28, 2008

TO: Banks Committee

FROM: The Connecticut Mortgage Bankers Association, Inc.

RE: Statement Regarding Raised Bill No. 5577, (LCO No. 2138), An Act Concerning Responsible Lending and Economic Security

The Connecticut Mortgage Bankers Association, Inc. ("CMBA"), which numbers over one hundred seventy five organizations and 750 individuals, is a non-profit association formed in 1984. The two principal purposes of the CMBA are to promote the welfare of the mortgage lending industry in Connecticut and to improve its service to the citizens of Connecticut. The CMBA is Connecticut's only trade association dedicated exclusively to the mortgage banking industry in the State of Connecticut.

BACKGROUND

The CMBA recognizes the problems arising from the "subprime crisis", the financial challenges facing many Connecticut homeowners, and the need to insure the proper functioning of the residential mortgage credit markets to serve current and prospective borrowers.

The CMBA has had the opportunity to review Raised Bill No. 5077 and other legislative proposals. The CMBA supports measures to benefit Connecticut consumers by encouraging responsible lending and economic security and maintaining residential mortgage credit availability for the citizens of Connecticut. Accordingly, the CMBA is supportive of many of the provisions of Raised Bill No. 5577 but opposes other provisions, as described below, that could restrict credit availability to Connecticut's citizens. The CMBA would welcome the opportunity to work with the Banks Committee to address its concerns with Raised Bill No. 5077 and other legislative measures under consideration.

- Loan Programs Benefiting Existing Borrowers. The CMBA support Sections 1 to 4 of Bill 5577 which would establish the REAL Program, the HERO program, and an EMAP Program. These programs would have the potential to provide much needed help to many borrowers who are at risk of foreclosure.

- Mandatory Mortgage Foreclosure Notices and New Pre-conditions to Foreclosure. The CMBA recognizes the financial challenges facing many homeowners. Section 5 of the bill would require a new, additional notice prior to commencement of a foreclosure, would require that foreclosure actions cease if a borrower applies for participation in one of the new programs, and would permit borrowers to seek a six month moratorium on a foreclosure. As a federal constitutional matter, the "contract clause" of the U.S. constitution prohibits states from enacting legislation that would impair the obligation of existing contracts. As a result, the proposed provisions in Section 5 of the Bill as applied to existing mortgages may not be effective and might only serve to give many homeowners the false hope of relief. Moreover, the proposed limitations on a mortgage lender's ability to foreclose on a mortgage would serve as a

disincentive for mortgage lenders to make new loans in Connecticut and could contribute to a contraction in the availability of credit to Connecticut residents, particularly to those residents who need higher than average loan to value ratio loans or who have below average creditworthiness. For those reasons, the CMBA opposes those provisions of Bill 5577.

- Provisions Concerning Nonprime Home Loans. The CMBA supported the state's "high cost home loan" statute, which was originally codified as the Abusive Home Loan Lending Practices Act. The CMBA supports many of Bill 5577's provisions regarding "nonprime home loans" (provided that the rate triggers for a loan to constitute a "nonprime home loan" are set at somewhat higher levels). Some provisions of Bill 5577, however, warrant changes to avoid unnecessarily restricting the availability of credit to Connecticut residents. Those provisions include the Section 9(d) requirement for borrowers to attend accredited courses before obtaining a nonprime mortgage loan, the requirement that borrowers qualify for a loan based on the highest possible interest rate over the loan term, and the voiding of loans which violate Section 9.

- Provisions of General Applicability. While well-intentioned, several provisions of the bill would subject mortgage lenders to obligations which exceed the industry norm and would have an adverse impact on mortgage lending. Those provisions (which the CMBA opposes) include the Section 9(b) imposition of fiduciary duties on mortgage lenders and brokers, the inclusion of the successors and assigns of a "lender" within the definition of "lender", the coverage of only licensed mortgage lenders within the scope of covered lenders under Section 9 and Sections 10 to 15, the requirement for a "tangible net benefit" for all refinance loans, the mandatory termination of foreclosure proceedings upon the borrower's cure of defaults, the required notice to all tenants in connection with a foreclosure coupled with the tenants' right to terminate a lease upon receipt of a lender's notice of a foreclosure, the adoption of a $5,000 statutory damages provision, the availability of the remedy of a rescission of a mortgage and an injunction barring foreclosure for violation of Sections 9 to 14 of the bill, and the imposition of liability upon the assignee of a loan. While such provisions may be warranted for loans subject to the state's current "high cost home loan" law and in some instances for "nonprime home loans" based on the "subprime crisis" which we are now experiencing, such provisions are not warranted in connection with mortgage lending generally and would have a chilling effect on such lending.

- Bonding. The CMBA supports the proposal to increase the dollar amount of the required surety bond, provided that the effective date of the increase is delayed for existing licensees to the date when an existing license expires.

- Provisions Enabling Department of Banking to Adopt Regulations and Need for Consistency with Changes in Federal Laws. The CMBA recognizes the experience and qualifications which the Connecticut Department of Banking possesses in connection with the regulation of the mortgage industry in Connecticut. The CMBA generally supports those provisions of Bill 5577 which enable the Department of Banking to adopt regulations. In addition to the Connecticut legislature's efforts to provide better regulation of the mortgage industry, both the U.S. Congress and federal regulators (primarily the Board of Governors of the Federal Reserve System) have pending proposals which would also change the regulations applicable to the mortgage industry. By virtue of an exemption under federal law, the

Connecticut Department of Banking has the authority to oversee state-chartered and state-licensed mortgage lenders. This local oversight is beneficial to Connecticut consumers and is desired by both the Department of Banking and the industry. The changes proposed in the Connecticut legislature (namely Bill 5577) as well as the federal proposals could, however, lead to a loss of the current exemption. Moreover, the adoption of proposals at the state and federal levels could subject Connecticut regulated lenders to potentially duplicative and/or inconsistent disclosure obligations (which could ultimately be confusing to not only lenders but more importantly to borrowers as well). To avoid such problems, the CMBA would support a broader authorization for the Department of Banking to adopt regulations which would have the objective of: (1) maintaining Connecticut's exemption (and preserve the oversight of the industry by the Department of Banking); and (2) avoiding the adoption of duplicative or inconsistent disclosure obligations which could arise from changes at both the federal and state level.

Leon Bailey, Chair
Denise T. Davidoff, *Vice Chair*
Joseph M. Carbone, *President and Chief Executive Officer*

350 Fairfield Avenue
Bridgeport, CT 06604

Phone: (203) 610-8500
Fax: (203) 610-8501
TTY: (203) 367-7424
www.workplace.org

February 28, 2008

Connecticut General Assembly
Banking Committee, 11 a.m., Room 2B

Senator Bob Duff, Co-Chairman
Representative Ryan P. Barry, Co-Chairman
Senator Joseph J. Crisco, Vice Chair
Representative Douglas McCrory, Vice Chair

I am here to speak on behalf of House Bill 5577: An Act Concerning Responsible Lending and Economic Security.

What brings me here today is the component of HB 5577 that I feel is both forward thinking and essential: inclusion of the Workforce Development Boards and by extension the CT*Works* Career Development Centers as part of the strategy to help borrowers already in foreclosure and to prevent more foreclosures from happening.

The state of Connecticut is to be commended for its efforts to date including convening the Sub-Prime Mortgage Task Force and creating the $50 million CT FAMILIES program through Connecticut Housing Finance Authority.

In its final report, the Taskforce acknowledged that a stable housing market is critical to a strong and growing economy. I submit that a stable and clear career path is critical to stable housing.

In ongoing studies in Chicago and Minneapolis-St. Paul, surveys of borrowers reveal that loss of a job or decreased income are top reasons for delinquency. In a study by Chicago's Home Ownership Preservation Initiative, loss of a job was cited by 47 percent of borrowers as the cause of their delinquency, while just 20 percent cited unfair loan terms.

In Connecticut, a review of unemployment rates in the 30 communities with the largest number of active sub-prime loans revealed that the metropolitan

centers topping the sub-prime list also have the highest unemployment rates. We took an average of the benchmarked unemployment rates for the years 2001-2006, the same years studied by the Taskforce. Bridgeport, New Haven, Waterbury, and Hartford (which rank first, second, third and fifth in the number of sub-prime loans in Connecticut) had the highest average unemployment rates. The smaller city of New Britain made the top 10 for number of subprime loans and had the fifth highest average unemployment rate between 2001-2006. (see attached table).

Partnering with the Workforce Development Boards by funding the Mortgage Crisis Job Training Teams will allow us to focus on these pockets of unemployment. State dollars would be unencumbered by income restrictions imposed by the federal Workforce Investment Act, or WIA. For instance, a family of four earning more than $46,102 a year is ineligible under WIA for most services at CT*Works* (for a full description of WIA income guidelines, see attached). The Mortgage Crisis Job Training Teams will allow us to open our doors to sub-prime borrowers in every community regardless of income.

We already have a presence where the need is the greatest. Bridgeport, New Haven, Waterbury, Hartford, New Britain and 12 other cities on the Top 30 sub-prime list have CT Works Centers located within their borders, including Stamford, Danbury, Meriden, East Hartford, Bristol, Manchester, Hamden, Norwich, Torrington, Enfield, Middletown and New London.

We can create a program that is statewide, or pilot this program in the Workforce Development Board regions hardest-hit – Southwest and North Central – to develop a track record of success that can be duplicated in every CT*Works* Center. From the list of Top 30 towns, the Southwest region has the greatest number of active sub-prime loans at 13,721, while the North Central region has 11,453. South Central follows close behind with 11,218. The North West region has 8,059 and the Eastern region has 1,584.

The Workforce Development Boards have a mandate to help employees and job seekers, but it is also part of our mission to foster strong relationships with businesses in our regions, including those in financial services and banking. Each Workforce Board can build upon relationships with local lending institutions to enable good faith community re-investment.

The Taskforce estimates that the 71,000 active subprime mortgages in Connecticut are worth a combined $1.5 billion. The latest estimate is that at 8.4 percent are seriously delinquent, meaning they are at least 90 days past due. In the coming 12 to 24 months, delinquencies will be affected by the growing number of adjustable rate mortgages reaching their initial reset dates. The Taskforce estimates that just over 21,000 adjustable rate sub-prime loans in Connecticut will reach their reset dates between October 2007 and October 2009. The National Center for Responsible Lending estimates that 10 to 16 percent of resets in metro areas of Connecticut will result in foreclosure.

This is troubling news not only for borrowers, but for the financial institutions that made the mortgages. The financial services industry is a crucial part of the Connecticut economy, especially in the Southwest and North Central regions.

In pursuing the dream of homeownership, studies have shown sub-prime borrowers are younger, have lower credit ratings, and live in cities with high unemployment rates. Young borrowers are more likely to have less personal wealth, less established careers, and lower income. Many may be unemployed, underemployed or in need of a second job. Many have greater potential than what they are working or earning at now. The Mortgage Crisis Job Training Teams can build on the outplacement, apprenticeships, incumbent training and tax incentive programs already in place at CT*Works*, plus specialize to include financial literacy and credit repair training, as well as help borrowers find ways to meet their financial obligations.

In closing, you have a choice to test this for a year in regions most acutely affected, or to fund Job Training Teams across the entire state. We estimate the cost to provide effective retraining, case management and family services to be $3,000 to $4,000 per family. We estimate starting the program in one region would cost $500,000, $1 million for a pilot in the two hardest-hit (Southwest and North Central). If it is your wish to begin on a statewide level, we estimate that somewhere between $2 and $2.5 million would be needed. I am confident that either project can begin as soon as July 1.

We anticipate that the banks to be active partners in this endeavor. We expect they will refer to the Workforce Boards those borrowers who would like to be part of the program. The Workforce Boards can work with the

lending institutions, particularly those that are part of the federal banking system, to arrange for support under their philanthropic programs.

This strategy of helping borrowers through a partnership with the state, the Workforce Boards and the lending institutions is cutting edge. It can be a model for the nation. It will help people to combat this issue, get beyond it, and do so with hope and dignity.

Thank You.

Respectfully submitted by Joseph M. Carbone, President & Chief Executive Officer, The WorkPlace, Inc.

000533

THE WORKPLACE, INC.
Southwestern Connecticut's Regional Workforce Development Board

Top 30	Town	Active Sub-Prime Loans	Estimated Resets Likely To Foreclose: 10-16 Percent (NCRL)	2001-2006 Average Unemployment Rate	2007 December Unemployment Rate	Workforce Board Region
1	Bridgeport	5,213	512-834	7.2	7	SW
2	New Haven	3,998	400-640	6.5	7.1	SC
3	Waterbury	3,333	333-533	7.3	7.6	NW
4	Stamford	2,599	260-416	3.9	3.6	SW
5	Hartford	2,573	257-412	9.1	9.3	NC
6	West Haven	1,946	195-311	5	5.1	SC
7	Norwalk	1923	192-308	3.9	3.9	SW
8	Danbury	1854	185-297	3.7	3.6	NW
9	Meriden	1757	176-281	5.1	5.5	SC
10	New Britain	1717	172-275	6.9	7.2	NC
11	Easton	1614	161-258	3.1	3.3	SW
12	E. Hartford	1504	150-241	5.2	5.9	NC
13	Bristol	1377	138-220	5	5.1	NC
14	Manchester	1126	113-180	4.4	4.4	NC
15	Hamden	1064	106-170	4.2	4.3	SC
16	Darien	986	99-158	3	2.8	SW
17	Milford	972	97-156	4	3.8	SC
18	New Milford	969	97-155	3.4	3.3	NW
19	Naugatuck	953	95-152	5.2	5.4	NW
20	Norwich	953	95-152	5	5.3	East
21	Torrington	950	95-152	5.4	5.1	NW
22	Enfield	905	91-145	4.6	4.9	NC
23	Windsor	843	84-135	4.4	4	NC
24	Middletown	813	81-130	5.1	4.3	SC
25	Greenwich	776	78-124	3	2.9	SW
26	Bloomfield	727	73-116	5.5	5.2	NC
27	W. Hartford	681	68-109	3.9	3.9	NC
28	Wallingford	668	67-107	3.9	3.9	SC
29	New London	631	63-101	5.5	5.9	East
30	Shelton	610	61-98	4.2	4	SW

Sources:
Unemployment Rates, CT Department of Labor
Subprime Communities List: Governor's Sub-Prime Mortgage Taskforce Final Report

My name is Dan Duffy and I am speaking on behalf of the Connecticut Association of Mortgage Brokers. I am here today to discuss several proposed bills that relate to the mortgage industry. These bills include House bills 5023, 5494 and 5577 and Senate bill 423. Before I address these bills I would like to remind the committee that CTAMB spoke in support of Senate Bill 21 last week and a position paper from our association was included in the submitted documents from that public hearing.

In regards to the proposed legislation for today's hearing, CTAMB is opposed to all four bills as they are proposed today. Rather than speak about each bill individually I would like to address some of the major themes covered by the bills. The first area is education and testing requirements. CTAMB has always supported the implementation of an entry test to obtain a license. We have some concerns with the continuing education piece. We believe that in reviewing the practices of other states and also other industries that mandate education, there are issues with the value and relevance of the courses. Proposals seem to be designed to fill a predetermined hour amount rather than what is essential to know. The amount of legislative change that occurs over a two year period varies greatly and rarely if ever would entail 8 – 10 hours to cover. We are also concerned that the only people that would truly benefit are organizations that would provide the education, as the mandatory classes will simply become a money maker. Our recommendation would be to have a test administered by the Banking Department. Starting with the entry exam and then adding in a test on Federal and State legislation. Establish a task force made from an equal representation from industry organizations that would help design the test and then continually review it for accuracy and relevance. If an applicant wants to take courses to prepare for the test it would be their choice.

Several of the bills look to define a subprime loan along with assigning duties of the mortgage broker and the use of a tangible benefit to determine whether a refinance can happen. The bills define subprime loans based on the yield of a like treasury note plus a margin. Our concern with this is that the proposed margin would be too restrictive and would have the possibility of conventional prime loans falling into that category. Fannie Mae and Freddie Mac continue to increase add-ons to interest rates for loan purpose, ltv and document type amongst other things. The bill could also place many prime jumbo loans and multi family loans into the subprime category. Legislation on the duties and responsibilities of a broker and a tangible benefit for the consumer has led to many lenders and brokers pulling out of practicing in some states. Having language in legislation that is open to interpretation is too risky as in the end a court of law will most likely define what constitutes "acting in the best interest of" a client. In HB5577 the tangible benefit provision does not allow for many refinances that would be advantageous to the consumer. It states that for it to be a tangible benefit as a cash out refinance, the borrower must receive at least 5 percent of the appraised value as cash back. This does mot appear to take in to account that many times the refinance will pay off debt with little cash going to the consumer. A borrower who wants to take on a larger payment to reduce the term of the loan would not meet the defined tangible benefit definition. Similarly a person who is looking to relieve a cash flow problem and thus reduces their payment but extends the loan would also not fit into the definition of a tangible benefit.

Also included in these bills is a provision for the disclosure of yield spread premium. Yield spread continues to be the most misunderstood and mischaracterized item in the mortgage world. Yield spread is currently disclosed in the Good Faith

Estimate and on The HUD at closing. Yield spread is what allows for choice for the consumer. It allows for a borrower to put less money in or get more money out of the loan. The misconception is that the borrower would have gotten a lower rate of interest if the broker was not making yield spread. The reality is that the borrower could have gotten a lower rate but it would have cost more up front. As do the banks, a mortgage broker must determine the amount of revenue generated per loan to keep the doors open and the originators able to earn a living.

In General, CTAMB has been a part of many task forces, committees, and sub committees on lending practices in the State of Connecticut. We have spoken in support of increasing bond requirements, net worth requirements and the inclusion of Connecticut in a national registry. We have also gone on record as supporting an entrance exam to gain a license. Today we ask the committee to carefully review the proposed legislations to look at the impact of restricting lending in this state. Many of the issues that these bills address no longer exist. Subprime lending has all but disappeared. The subprime adjustable rate mortgage no longer exists. Many of the problems that consumers are experiencing today are due to the fact that so many programs are gone. Many states are feeling the impact that restricting lending has caused. There are fewer programs with less qualified buyers and home values are dropping. The latest reports indicate that home prices have dropped nearly 9% over the past three months. Although Connecticut has been luckier than most states in this regard, the effect of declining markets on lending has recently occurred in pockets around the state. I thank you for your time.

Respectfully submitted,
Dan Duffy

Testimony—HB 5577
Representative Minnie Gonzalez

February 28, 2008

State of Connecticut

HOUSE OF REPRESENTATIVES

STATE CAPITOL
HARTFORD, CONNECTICUT 06106-1591

REPRESENTATIVE MINNIE GONZALEZ
THIRD DISTRICT

LEGISLATIVE OFFICE BUILDING
ROOM 4039
HARTFORD, CT 06106-1591
HOME: (860) 236-9654
CAPITOL: (860) 240-8585
FAX: (860) 240-0067
E-mail: Minnie.Gonzalez@cga.ct.gov

DEPUTY MAJORITY WHIP AT LARGE

MEMBER
APPROPRIATIONS COMMITTEE
JUDICIARY COMMITTEE
PUBLIC SAFETY AND SECURITY COMMITTEE

Testimony
Representative Minnie Gonzalez
3rd District, Hartford
February 28, 2008

HB 5577, ***"AN ACT CONCERNING RESPONSIBLE LENDING AND ECONOMIC SECURITY"***

Chairman Duff, Chairman Barry, and Honorable Members of the Banks Committee, I wish to express my strong support for House Bill #5577, and I would like to thank the chairmen and committee members for bringing this proposal forward for a public hearing. However, I would like for you to consider the following concepts to be included in this bill:

Predatory sub-prime lenders have issued mortgages without such escrow accounts which forced the purchasers into tax foreclosures. Purchasers were unaware that the escrow accounts were never opened. I believe **all mortgages which do not have an insurance and property tax escrow account should be outlawed.**

Sub-prime lenders have also been found to have used unscrupulous practices amounting to deception and even fraud. We should require stricter License and regulation of all mortgage brokers and their agents. This includes: **1) All must be bonded; 2) All must maintain an office within the state of Connecticut; 3) Brokers must have a net worth of at least $10 million or must have posted a surety bond for that amount; 4) Agents must post a surety bond equal to the mean single-family house price in Connecticut as posted by the State Banking Department each year; 5) Agents must have at least 4 weeks of training, including ethics classes; 6) All brokers and agents must have national background checks.**

Predatory lenders have also issued mortgages to borrowers with no documentation of their income or ability to pay the mortgages. Proper underwriting standards must be required to ensure that potential borrowers can meet the 30% standard at the highest interest level that the mortgage can attain.

Testimony—HB 5577
Representative Minnie Gonzalez

February 28, 2008

It must be required that no mortgage may be underwritten with payments which exceed 30% of the borrower's household income. Such payments must include all principle and interest, property taxes, insurance, and all utilities. In distressed cities and communities FHA underwriting standards must be followed.

Additionally, predatory lenders offered mortgages to unqualified purchasers at low teaser rates. Those rates would quickly escalate to unaffordable levels, and the prepayment penalties would make it impossible for the purchasers to pay off the original mortgage. **The prepayment penalties that predatory lenders require, which have been outlawed in other states, need to be outlawed here in Connecticut.**

The governor's task force reported that it is estimated there are about 71,000 active sub-prime mortgages in Connecticut, with outstanding balances totaling more than $15 billion. Over 8% of these mortgages are now seriously delinquent. The task force also reported that there is a concentration of sub-prime mortgages in communities with a higher than average number of low and moderate income households, minority households, and affordable single-family housing.

In closing, I would like to reiterate the importance of this legislation and thank the chairs and members for giving me the opportunity to testify today.

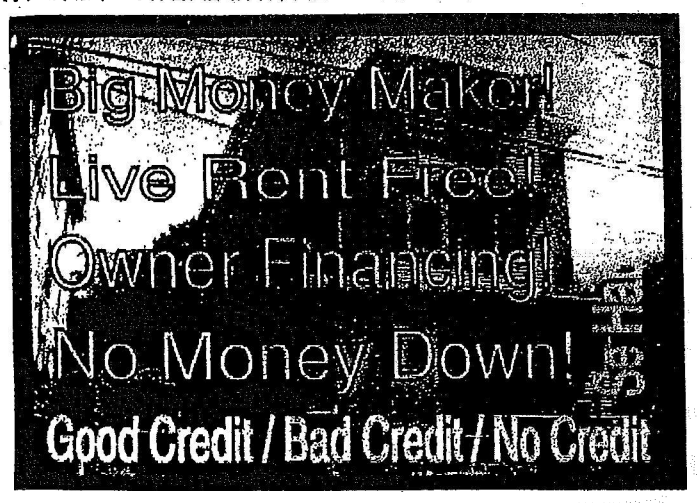
Truly yours,

Minnie Gonzalez
State Representative

000543

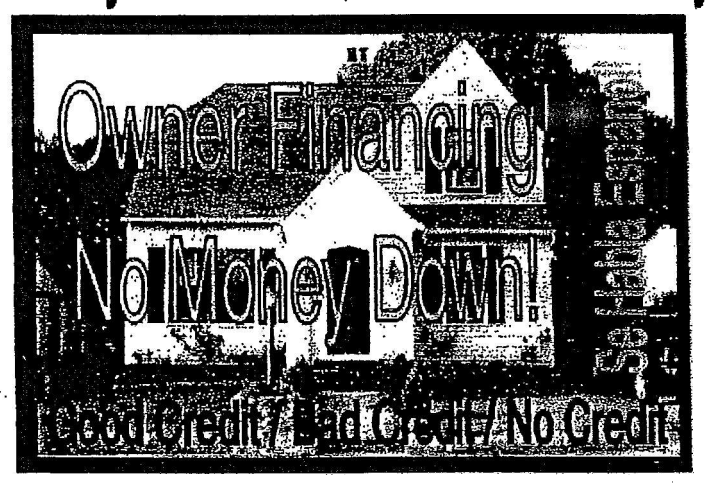
HARTFORD, WATERBURY, NEW BRITAIN, MERIDEN, NEW HAVEN, BRIDGEPORT, HAMDEN, BLOOMFIELD

HARTFORD, WATERBURY, NEW BRITAIN, MERIDEN, NEW HAVEN, BRIDGEPORT, HAMDEN, BLOOMFIELD, WEST HARTFORD



2 & 3 fAMILY
1st Time Buyer's
WELCOM!

Why Rent When You Can Buy And Live Rent free?



1 fAMILY
1st Time Buyer's
WELCOM!

Good Credit / Bad Credit / No Credit

450 - 540 - 580 - 620 NO MINIMUM SCORE!

Free Moving Expenses!

Toll Free: 1-888-888-1422

100% Financing, No money Down, Owner Pay's All Closing !!!

Ask 4: David Azran

HARTFORD, WATERBURY, NEW BRITAIN, MERIDEN, NEW HAVEN, BRIDGEPORT, HAMDEN, BLOOMFIELD, WEST HARTFORD

HARTFORD, WATERBURY, NEW BRITAIN, MERIDEN, NEW HAVEN, BRIDGEPORT, HAMDEN, BLOOMFIELD

Testimony of Joshua Grant

Banks Committee

February 28, 2008

My name is Joshua Grant. I am a business owner, Bridgeport resident, and am facing foreclosure. I'd like to thank Representative Barry and Senator Duff for the time and energy you have spent on finding solutions to the foreclosure crisis we are facing as a state and a nation. I know that you are proposing HB 5577, and I am here as an ACORN member to testify on that bill, as well as Senate Bill 423.

By and large, HB 5577 is a good bill, but it lacks several critical components that are included in SB 423. We look forward to working with the co-chairs and members of this committee to ensure that whatever legislation passes out of this committee includes all of the following provisions—without which the law will be weak and insufficient:

1) Yield spread premiums must be completely eliminated for all loans, not merely disclosed or regulated. Yield spread premiums are bonuses for brokers who steer borrowers into higher cost loans than they qualify for. Yield spread premiums provide a direct monetary incentive a broker to sell me a loan at 8% even if I qualify for a 6% loan. This practice increases costs homeowners tremendously, increases the number of high cost loans and the likelihood of default, and rewards brokers for predatory lending. I challenge any mortgage broker to stand me and explain why it is fair or just for them to earn a profit by charging a higher interest rate than a borrower qualifies for.

2) pre-payment penalties must be prohibited in all high cost loans, and should conform to Federal Reserve policy for all adjustable rate loans,

whether prime or subprime. Pre-payment penalties trap families and prevent people from refinancing into affordable loan products. Prepayment penalties should be eliminated entirely from all high cost and non-traditional mortgage products. For traditional and prime loans with adjustable rates, we would accept a modest prepayment penalty of 3% in year one, 2% in year two, and 1% in year three—BUT ONLY ON THE CONDITION THAT ANY PREPAYMENT PENALTY WOULD BE WAIVED FOR REFINANCES WITHIN 60 DAYS OF AN INTEREST RATE RESET. This would allow borrowers to maintain affordable payments, and this is consistent with current Fed policy.

3) Flipping – the refinancing of a loan without a net tangible benefit to the borrower—must be banned. It should be illegal to encourage a borrower to default; and it should be illegal for a bank or servicing company to raise the interest rate on a loan as a direct result of delinquency.

4) Negative amortization on a mortgage loan must be prohibited.

5) Brokers should be required to act in the best interest of borrowers. This should be a fiduciary relationship.

6) Low documentation and no documentation loans must be outlawed. All loans must be based on the borrowers ability to repay, based on the fully indexed rate over the life of the loan, including taxes and insurance. Language in this section must include a rebuttable presumption that a borrower was unable to pay if the fully amortized repayment schedule exceeds forty-five percent of the borrowers verified monthly gross income.

ACORN stands firmly committed to the dream of home ownership for all Americans who can afford it. We support banks in their efforts to provide credit for lower income families; but we condemn practices that put a family

into a home for two years with no reasonable expectation that the loan will be affordable over the long haul. For brokers who make their money on the front end, there must be strong accountability. For banks and investors who are in this for the long haul, it is far better to offer a product a family will be able to afford and make payments on for 30 years, than to keep families in erratic loan products that cause havoc for families and instability in the market.

There is and will continue to be great pressure from the banking industry, from servicing companies, and mortgage brokers to maintain as much of the status quo as possible. But when the system is broken, it has to be fixed. Allowing brokers to have the final word on these questions is like letting the fox guard the hen house. Our proposals are consistent with the long term interest of homeowners, banks, and investors. What we're dealing with here in most cases are risky loan products, not risky borrowers. We cannot allow mortgage originators to continue selling products that ultimately decimate our neighborhoods by leaving homes vacant and cities blighted.

I ask all members of this committee to work with ACORN on these proposals, and I thank you for your time.

Joan McDonald
Commissioner

DECD

State of Connecticut
Department of Economic and
Community Development

TESTIMONY SUBMITTED TO THE BANKS COMMITTEE
February 28, 2008

Joan McDonald, Commissioner
Department of Economic and Community Development

HB 5577 AN ACT CONCERNING RESPONSIBLE LENDING AND ECONOMIC SECURITY

The Department of Economic and Community Development (DECD) offers the following comments and concerns regarding HB 5577, *An Act Concerning Responsible Lending and Economic Security.*

DECD understands the local and national problem regarding the increase in foreclosures and defaulting mortgages, and also realizes something must be done in order to assist qualified homeowners.

Although HB 5577 may have been drafted with the best of intentions, some of its language could lead to unintentional negative consequences in the near future. Nowhere in the proposed bill is staffing or administrative costs mentioned. Introducing a multi-million dollar program to DECD would require significant resources and administrative costs in order to properly administer the program in a timely manner. Additionally, either existing or new staff will need to be trained to properly underwrite single-family loans, set-up a phone hotline, and conduct outreach/marketing. The effective date of July 1, 2008 as the date to start implementing the three programs would create a very small timeframe for training.

The separation of the Emergency Mortgage Assistance Program Committee from the DECD is another area of concern. The bill currently states that the Committee will be making the decisions as to which homeowners get funded and will also be tasked with determining program eligibility, standards and procedures. It would seem more logical for the agency that administers the program to determine program eligibility, standards and procedures.

Taking bond proceeds from the Connecticut Housing Finance Authority (CHFA) could also be detrimental. In April 2007, Governor Rell convened a Task Force of housing, banking and mortgage lending and consumer experts to examine and make recommendations regarding the issue of sub-prime lending in Connecticut. As many of you are aware, the most critical recommendation was to immediately implement a

program that could financially ease the burden of homeowners that were in danger of losing their homes due to subprime mortgages. The program, called "CT Families", is a $50 million initiative that was just launched in December 2007.

Transferring $40 million from CHFA to DECD in order to run a very similar program would impact CHFA's overall ability to do business and could also unduly harm their bond rating. As a member of the CHFA board, DECD can not support such transfer.

The underwriting criteria of "flexible credit underwriting" would also need adjusting. Not only are we concerned with the total debt of a homeowner, but we also need to bear in mind the homeowner's monthly housing costs as a percentage of their gross income (DECD/HUD current policy is 30%). Additionally, the credit score threshold of 620 might not be adequate. Homeowner counseling sessions might also need to be conducted to educate the homeowner so this type of situation is not replicated in the future.

In closing, I would like to say that DECD not only appreciates your willingness to want to help homeowners but also understands the complexities of this situation.

Unfortunately, this is not something that is going to be fixed overnight, but we are confident that Governor Rell's CT Families program will help assist our state's residents and trust that it will be given the opportunity to do so.

Thank you for your time and consideration of my comments.

HEARING BEFORE THE COMMITTEE ON BANKING,
CONNECTICUT GENERAL ASSEMBLY
FEBRUARY 28, 2008

WRITTEN TESTIMONY OF PATRICIA A. McCOY
George J. and Helen M. England Professor of Law
University of Connecticut School of Law
Hartford, Connecticut

HB 5577 SB 21
SB 423

Thank you for the opportunity to testify today. My testimony today will focus on why Connecticut needs stronger home mortgage legislation to revive trust in the residential mortgage market and the broader economy.

Subprime mortgages are high-cost loans designed for borrowers with impaired credit. These loans pose a heightened risk of default. In the past ten years, press reports of abusive subprime loans have prompted regulators to institute repeated enforcement actions against subprime lenders and servicers for unfair practices and fraud.[1] Despite the seriousness of these

1. For instance, in 2004, Citigroup Inc. and its subprime mortgage subsidiary, Citifinancial Credit Company, agreed to a cease-and-desist order in which the Board of Governors of the Federal Reserve System imposed a $70 million civil money penalty for alleged predatory lending practices. Timothy L. O'Brien, *Fed Assesses Citigroup Unit $70 Million in Loan Abuse*, N.Y. Times, May 28, 2004, at C1; Press Release, Bd. of Governors of the Fed. Reserve Sys. (May 27, 2004), www.federalreserve.gov/boarddocs/ press/enforcement/2004/20040527/default.htm. The 2004 Citigroup order followed on the heels of an earlier $215 million settlement by Citigroup Inc. in 2002 to resolve FTC charges of predatory lending. Press Release, Federal Trade Comm'n, Citigroup Settles FTC Charges Against the Associates Record-Setting $215 Million for Subprime Lending Victims (Sept. 19, 2002), www.ftc.gov/opa/2002/09/associates.htm. Also in 2004, the Office of Thrift Supervision entered into a supervisory agreement with Ocwen Federal Bank to prohibit alleged predatory loan servicing practices. Supervisory Agreement, Ocwen Fed. Bank FSB and Office of Thrift Supervision, OTS Docket No. 04592 (Apr. 19, 2004), www.ots.treas.gov/docs/9/93606.pdf. The Federal Bureau of Investigation has pursued mortgage fraud aggressively. *See, e.g.*, Fed. Bureau of Investigation, *Statement of Chris Swecker Before the House Finan. Services Subcomm. On Housing and Community Opportunity* (Oct. 7, 2004), www.fbi.gov/congress/congress04/swecker100704.htm; Fed. Bureau of Investigation, Financial Crimes Report to the Public Fiscal Year 2006, www.fbi.gov/publications/financial/fcs_report2006/financial_crime_ 2006.htm#Mortgage (reporting on investigations into equity skimming, property flipping and mortgage-related identity theft).

Between 1998 and 2008, the Federal Trade Commission prosecuted predatory lending cases against home mortgage lenders and brokers including Action Loan Co., Amor Mortgage, Abacus Mortgage, Associates First Capital Corp., Barry Cooper Properties, Capital City Mortgage Corp., Capitol Mortgage Corp., Chase Financial Funding, Inc., CLS Financial Services, Inc., Delta Funding Corp., Fairbanks Capital Corp., First Alliance Mortgage Company, First Plus Financial Group, Inc., Fleet Finance and Home Equity U.S.A., Granite Mortgage, LLC, Interstate Resource Corp., LAP Financial Services, Inc., Mark Diamond, Mercantile Mortgage Co., Mortgages Para Hispanos.Com Corp., Nationwide Mortgage Corp., NuWest, Inc., PWR Processing, Inc., R.A. Walker & Assocs., and Wasatch Credit Corp. *See* Prepared Statement of the Federal Trade Commission on Foreclosure Rescue Fraud before the Senate Special Committee on Aging, Feb. 13, 2008, www.ftc.gov/os/testimony/P064814foreclosure.pdf; Fed. Trade Comm'n, *Prepared Statement of the Federal Trade Commission on Efforts to Combat Unfair and Deceptive Subprime Lending Before the Senate Special Committee on Aging,* 3-8, Feb. 24, 2004, www.ftc.gov/os/2004/02/02242004subprimelendingtest.pdf; Letter from Donald S. Clark, Sec'y, Fed. Trade Comm'n, to Sandra F. Braunstein, Dir., Fed. Reserve Sys. Div. of Consumer and Cmty. Affairs (Feb. 23, 2005), www.ftc.gov/os/2005/03/050301enforcemntrpt.pdf; Press Release, Fed. Trade Comm'n, Capital City Mortgage Corp. Defendant Settles with FTC (May 14, 2004), www.ftc.gov/opa/2004/05/sanne.htm; Press Release, Fed. Trade Comm'n, Capital City Mortgage Settles FTC Charges (Feb. 24, 2005), www.ftc.gov/opa/2005/02/capitalcity.htm; Press Release, Fed. Trade Comm'n, FTC Challenges Bogus Mortgage Loan Brokers (June 1, 2004), www.ftc.gov/opa/2004/06/pwrprocessing.htm; Press Release, Fed. Trade Comm'n, FTC, DOJ and HUD Announce Action to Combat Abusive Lending Practices, (Mar. 30, 2000), www.ftc.gov/opa/2000/03/deltafunding.htm; Press Release, Fed. Trade Comm'n, FTC: Mortgage Broker's Deceptive Claims Tricked Consumers Looking for a Good

charges, the harm from these problems originally appeared to be confined to a relatively obscure corner of the consumer finance market. Until mid-2007, there was little concern that defective subprime loans would spill over into the larger economy.

That changed last July, when subprime losses sank two Bear Stearns hedge funds and pushed a regional German bank named IKB Industriebank to the brink of failure. World markets trembled as stock markets plunged in the United States and Europe, subprime lenders failed in droves, sales of subprime bonds crashed, and the market for interbank credit seized up. As markets deteriorated, write-downs on U.S. subprime bonds triggered such a severe bank run at Northern Rock plc, a British bank, in September 2007 that the Bank of England felt compelled to issue a blanket guarantee for all deposits at British banks and ultimately had to nationalize Northern Rock. Nor were Northern Rock and IKB Industriebank alone. So many foreign investors bought toxic subprime bonds that even the small Arctic town of Narvik, Norway (pop. 18,000), went insolvent in December 2007 due to investments in bad subprime securities.

Back at home, skyrocketing subprime foreclosures pushed the United States to the edge of a recession. By February 2008, panic over credit quality had paralyzed the markets for term auction securities, leveraged financing, and asset-backed bonds securitizing commercial real estate loans, jumbo mortgages, and even student loans. Private-label mortgage-backed securitizations and subprime lending dwindled and no one knows what future form these markets will take. Financial services companies have taken approximately $150 billion in subprime write-downs to date since the beginning of 2007. In February 2008, the Group of Seven estimated that financial institutions worldwide face up to $400 billion in write-downs resulting from subprime losses.[2]

Market failures in the U.S. subprime mortgage industry lie at the root of these problems. My testimony begins by describing how the compensation systems for subprime mortgage professionals and investment banks created perverse incentives to artificially increase the risk of subprime loans. Next, the testimony chronicles how these incentives caused the subprime industry to spiral downward due to lax underwriting and outright loan fraud.[3] Finally, I discuss

---

Rate (June 2, 2004), www.ftc.gov/opa/2004/06/ chasefinancial.htm; Press Release, Fed. Trade Comm'n, Home Equity Lenders Settle Charges that They Engaged in Abusive Lending Practices; Over Half Million Dollars To Be Returned to Consumers (July 29, 1999), www.ftc.gov/opa/1999/07/hoepa.htm; Press Release, Fed. Trade Comm'n, Home Mortgage Lender Settles "Predatory Lending" Charges (Mar. 21, 2002), www.ftc.gov/opa/2002/03/famco.htm; Press Release, Fed. Trade Comm'n, Midwest Mortgage Lender Agrees to Settle Illegal Lending Charges Brought by FTC, HUD, and State of Illinois, (July 18, 2002), www.ftc.gov/opa/2002/07/ mercantilediamond.htm; Fed. Trade Comm'n, FTC Subprime Lending Cases (since 1998), www.ftc.gov/opa/2002/07/subprimelendingcases.htm (last visited Feb. 28, 2007).

State attorneys general and state banking regulators have also instituted aggressive enforcement actions for subprime abuses. While the individual state proceedings are too numerous to all name, two nationwide settlements stand out. In 2006, forty-nine states and the District of Columbia reached a $325 million settlement with Ameriquest Mortgage Company over alleged predatory lending practices. *See, e.g.*, Press Release, Iowa Dep't of Justice, Miller: Ameriquest Will Pay $325 Million and Reform its Lending Practices (Jan. 23, 2006). In 2002, state attorneys general from forty-four states and the District of Columbia secured a $484 million settlement from Household Finance Corporation to dismiss charges of deceptive subprime loans. *See* Press Release, Iowa Attorney General, States Settle With Household Finance: Up to $484 Million for Consumers (October 11, 2002).

[2] *G-7: $400 billion newest subprime tab*, INVESTMENT NEWS, Feb. 11, 2008, www.investmentnews.com/apps/pbcs.dll/article?AID=/20080211/REG/772519581.

[3] For a fuller treatment of the topics discussed in this testimony, see Kathleen C. Engel & Patricia A. McCoy, *Turning a Blind Eye: Wall Street Finance Of Predatory Lending*, 75 FORDHAM L. REV. 2039 (2007); Kathleen C.

how the breakdown in credit markets results from a breakdown in trust by investors. I close by discussing why strong legislation is needed to restore that trust and bring the credit markets back to life. In particular, our new research findings indicate that lowering the annual percentage rate triggers in state home mortgage laws – and possibly adding assignee liability provisions – helps expand access to subprime credit.

Perverse Incentives Toward Heightened Risk

In the past twenty years, the home mortgage industry underwent fundamental changes that increased its incentives to take reckless risks with subprime loans. Specifically, the mortgage lending industry evolved from one in which the lender retained the full risk that a loan would default to one in which lenders, mortgage brokers, and investment banks were paid upfront while passing off the risks onto borrowers and investors.

Securitization altered the structure of mortgage lending and the financial incentives of its players in ways that were underappreciated at the time. Before securitization, lenders usually did it all: they solicited loan applicants, underwrote the loans, funded those loans, serviced the loans, and held the loans in portfolio. Lenders earned profits on loans mostly in the form of interest payments, not upfront fees. If the loans went into default, the lenders bore the losses. Default was such a serious financial event that lenders took care when underwriting loans.

All that changed with securitization. Securitization allowed lenders to outsource parts of the lending process. This phenomenon, known as *unbundling,* reduced lenders' incentives to exercise care when making loans. With securitization, a lender could make a loan and sell it to investors, who would bear the financial brunt if the loan went belly-up. Unlike in the past, lenders mostly made their money on upfront fees collected from the borrowers and the cash proceeds from securitization offerings, not on the interest payments on loans. Lenders liked the security of being paid in advance, instead of having to wait for uncertain monthly payments over the life of the loan.

Lenders also knew that their risk from securitization was only a fraction of the risk they otherwise would assume from holding whole loans on their books. Besides, lenders rationalized, securitization sliced the risks that they passed on into finer and finer pieces that were diversified among investors. Because they knew they could pass the lion's share of subprime risks onto faceless investors, lenders had less reason to care about how well a loan performed. Some lenders even had two sets of underwriting standards: high underwriting standards for the loans they kept on their books and lax underwriting standards for the loans that they securitized. All the while, investors were clamoring for higher-yield bonds, which required backing those bonds with higher-risk home loans. Together, these dynamics encouraged lenders to make ever riskier loans and to pass off the worst loans onto investors.

Investors tried to protect themselves by requiring lenders to retain the riskiest parts of subprime securitizations. Lenders became able to dispose of that retained risk, however, by repackaging those interests and securitizing them all over again, this time as bonds known as collateralized debt obligations (CDOs).

Engel & Patricia A. McCoy, *A Tale of Three Markets: The Law and Economics of Predatory Lending*, 80 TEX. L. REV. 1255 (2002).

Most lenders used investment banks to underwrite their subprime securitizations. Of the major Wall Street firms, Lehman Brothers, Bear Stearns, Merrill Lynch, J.P. Morgan, Morgan Stanley, Citigroup, and Goldman Sachs underwrote most private-label subprime securitizations.[4] After IPO offerings dried up during the three-year bear market from 2000 through 2002, mortgage-backed securities deals and CDOs stepped into the breach and became one of the hottest profit centers for investment banks.[5] By 2006, Wall Street had cornered the subprime business, securitizing over two-thirds of subprime loans.[6]

Investment banks profited from subprime underwriting by collecting a percentage of the sales proceeds, either in the form of discounts, concessions, or commissions. Once an offering was fully distributed, the underwriter collected its fee in full. This compensation system for the underwriters of subprime securitizations caused Donna Tanoue, the former Chairman of the Federal Deposit Insurance Corporation, to warn: "[T]he underwriter's motivation appears to be to receive the highest price and best execution possible on behalf of the issuer - not to help curb predatory loans."[7]

Tanoue's warning proved prophetic. Earlier this month, Fitch Ratings projected that fully *forty-eight* percent of the subprime loans securitized by Wall Street in 2006 would go into default.[8] Despite that dismal performance, 2006 produced record net earnings for Goldman Sachs, Morgan Stanley, Merrill Lynch, Lehman Brothers, and Bear Stearns.[9] That year, manager pay reflected the bottom-line importance that investment banks placed on private-label mortgage-backed securities, with managing directors in the mortgage divisions of investment banks earning more on average in 2006 than their counterparts in other divisions.[10]

As part of their duties, underwriters for subprime bond offerings drafted prospectuses and offering memoranda that were supposed to inform investors about the underwriting criteria and risks of the subprime loans in the loan pool. These documents usually stated that the lenders reserved the right to make exceptions to their underwriting standards in individual cases. But in 2006 and 2007, some offering documents failed to say that the exceptions – in other words, loans that flunked the lender's underwriting standards – far outweighed the number of loans that met those standards.[11] Ratings agencies have asserted that investment banks withheld due diligence reports from them that quantified the size of these exceptions. One due diligence firm has

---

4 Gretchen Morgenson, *Crisis Looms in Market for Mortgages,* NEW YORK TIMES, March 11, 2007; *Scorecard – Everyone Out of the Pool,* INSTITUTIONAL INVESTOR, Sept. 17, 2007.

5 Laura Mandaro, *Investment Banks Stay Busy,* INVESTOR'S BUSINESS DAILY, Feb. 21, 2006, at A14.

6 Gretchen Morgenson, *Crisis Looms in Market for Mortgages,* NEW YORK TIMES, March 11, 2007.

7 Remarks by Donna Tanoue, Chairman, Federal Deposit Insurance Corporation, Before the Annual Conference, National Congress for Community Economic Development, New Orleans, LA, October 13, 2000, www.fdic.gov/news/news/speeches/archives/2000/sp13Oct00.html.

8 For loans in the 2007 subprime vintage, Fitch estimates that forty-three percent will go into default. *Fitch Places $139B U.S. Subprime RMBS On Watch Negative on Worsening Mortgage Performance,* REUTERS, Feb. 1, 2008, www.reuters.com/article/pressRelease/idUS203638+01-Feb-2008+BW20080201.

9 2006 Annual Reports for Goldman Sachs, Morgan Stanley, Merrill Lynch, Lehman Brothers, and Bear Stearns.

10 Jenny Anderson & Vikas Bajaj, *Wary of Risk, Bankers Sold Shaky Mortgage Debt,* NEW YORK TIMES, Dec. 6, 2007.

11 Vikas Bajaj & Jenny Anderson, *Inquiry Focuses on Withholding of Data on Loans,* NEW YORK TIMES, Jan. 12, 2008.

further alleged that some investment banks ordered it to cut its random samples of subprime loan pools by half when checking for compliance with loan underwriting guidelines in order to permit those banks to turn a blind eye to the wide prevalence of exceptions.[12]

The major rating agencies also had financial incentives to understate the risks of subprime mortgage-backed securities and CDOs. The investment banks that underwrote subprime securitizations paid the rating agencies that provided them with investment-grade ratings. After an investment bank divided a subprime bond offering into different buckets (called tranches) according to default risk, the rating agencies rated each tranche. The rating agencies touted their top-rated subprime bonds – ranging from AAA down to A -- as hardly ever defaulting. These ratings lured droves of investors in the United States and abroad who were in search of higher yields to buy the top-rated subprime bonds and CDOs. The more good ratings that the agencies issued, the more deals that were sold, reaping profits for the rating agencies and the investment banks who hired them.

Securitization was not the only form of outsourcing in the subprime industry. Increasingly, subprime lenders, through their wholesale loan divisions, used independent mortgage brokers to solicit potential customers and process loan applications. Lenders even outsourced loan underwriting to contract underwriters for as little as $10 per loan application. Both sets of players had incentives to close loans at any cost and to deceive participants down the line about the risks of those loans.

Contract underwriters, for instance, were only paid a small flat fee per loan. Often that fee was too low to verify incomes and carefully evaluate credit risk. Contract underwriters, as a result, had economic incentives to dispense with verification and instead underwrite mortgages as stated-income or no-documentation loans.

The perverse incentives were even worse for brokers. Mortgage brokers only got paid if they closed a loan. Furthermore, subprime brokers were paid solely through upfront fees at closing, meaning that if a loan went bad, the losses would fall on the lender or investors, not the broker. In the most pernicious practice of all, lenders paid brokers thousands of dollars per loan in fees known as yield spread premiums (or YSPs) in exchange for loans saddling borrowers with steep prepayment penalties and higher interest rates than the borrowers deserved, based on their incomes and credit scores.

YSPs, by driving up interest rates, substantially increase the likelihood that subprime loans will default and go into foreclosure. Economists have estimated the size of this risk. For every one percent that the initial interest rate on a home mortgage goes up, the likelihood that a household will lose its home rises by sixteen percent a year. For adjustable-rate mortgages (ARMs), these statistics are even worse. When the interest rate on an ARM resets, every one percent increase in the reset rate makes it thirty percent more likely that a household will lose its home.[13] Many recent subprime hybrid ARMs have initial resets of three percentage points,[14] which drives home how much overpriced subprime loans put homeowners and investors at risk.

---

[12] Jenny Anderson & Vikas Bajaj, *Loan Reviewer Aiding Inquiry Into Big Banks*, NEW YORK TIMES, Jan. 27, 2008.

[13] Donald R. Haurin & Stuart S. Rosenthal, The Growth Earnings of Low Income Households and the Sensitivity of Their Homeownership Choices to Economic and Socio-Demographic Shocks (U.S. Department of

The compensation structure for mortgage brokers encouraged numerous subprime brokers to do whatever it took to close a loan. Sometimes this involved padding a borrower's income or assets. Sometimes this was with the borrower's involvement, but more often it was not. Sometimes doing whatever it took meant commissioning an inflated appraisal; other times it meant duping borrowers with overpriced loans. Many of these borrowers had credit scores that were high enough to qualify them for cheaper prime loans.[15] Moreover, if a broker put a borrower into a loan that the homeowner could not afford, the broker could always offer to refinance that loan and pocket another round of fees. In all of these ways, brokers had financial incentives to boost the risk of subprime loans and to foist that risk onto borrowers, lenders, and investors. In theory, these injured parties could sue careless or fraudulent brokers, but in reality, most of those brokers had meager capital, leaving them judgment-proof.

Lenders looked the other way because they profited from higher loan volumes and planned to securitize the loans anyway and shift the risk to investors. To maximize their loan volume from brokers, many lenders relaxed their quality controls on brokered loans. In fact, one subprime lender, Novastar Financial, made no bones about that fact when it reportedly sent a brochure to its brokers trumpeting, "Did You Know NovaStar Offers to Completely Ignore Consumer Credit!"[16]

At the end of the day, securitization and its sister forms of outsourcing gave financial incentives to actors in the mortgage industry to originate unduly risky subprime loans. Mortgage brokers originated faulty loans because they knew they could shift the credit risk onto lenders while collecting their pay at closing. Lenders agreed to make defective loans because they got paid upfront while dumping those loans onto investors. Investment banks and rating agencies glossed over the risks of subprime loans because they knew they would get paid from the securitization proceeds. Investors took the ratings on blind faith because they were greedy for high returns and did not insist on closer scrutiny of loan pools. To the contrary, relentless demand by investors at home and abroad for high-yield subprime bonds required shunting a continuous stream of borrowers into subprime loans.

The Subprime Surge and Bust

From 1994 to 2005, subprime loans rocketed in growth at twenty-six percent a year. In order to maintain this meteoric rate of growth, the subprime sector needed to deliver a steady stream of customers for high-cost loans. To ensure that stream of customers, the subprime industry came to rely on – and fueled – looser and looser underwriting standards.

In the early years, it was easy for the subprime market to grow fast because it started out so small. Back in 1994, subprime mortgages accounted for less than five percent of home loans.

Housing and Urban Development April 2005): vii, 18, www.huduser.org/Publications/pdf/EarningsOfLow-IncomeHouseholds.pdf

[14] Statement of Sheila C. Bair, Chairman, Federal Deposit Insurance Corporation, on Strengthening the Economy: Foreclosure Prevention and Neighborhood Preservation; before the Committee on Banking, Housing and Urban Affairs, U.S. Senate, 538 Dirksen Senate Office Building, January 31, 2008, www.fdic.gov/news/news/speeches/chairman/spjan3108.html.

[15] Rick Brooks & Ruth Simon, *Subprime Debacle Traps Even Very Credit-Worthy*, WALL STREET JOURNAL, Dec. 3, 2007.

[16] Gretchen Morgenson, *Creative Loans, Creative Compensation*, NEW YORK TIMES, Nov. 18, 2007.

Even by 2001, subprime mortgages only made up nine percent of total home loans. During those early years, from the viewpoint of macroeconomists, subprime mortgages were just a drop in the bucket compared to home mortgages overall in most parts of the country.

But with the traumatic events of 2001, everything changed. The previous year, the dot-com bubble had burst, plunging the U.S. economy into recession. By August 2001, the S&P 500 Index was off twenty-six percent from its previous high. Then tragedy struck. On September 11, al-Qaeda attacked the World Trade Towers and the Pentagon, striking at the very heart of Wall Street. As the country grieved, the faltering economy attempted to revive, only to sustain another blow in December 2001, when Enron filed for bankruptcy. As one corporate scandal after another came to light, public confidence in the stock markets crumbled. The S&P 500 slid another fifteen percent and did not begin to bounce back until the fall of 2002, after Congress passed the Sarbanes-Oxley Act.

Throughout it all, the housing market was the one bright spot in the economy. In mid-2000, with the dot.com bubble about to burst, the Federal Reserve Board exercised its "Greenspan put" and slashed interest rates, causing housing prices to grow at a steady clip of ten percent a year nationally. After the 9/11 attacks, with the recession in full swing, the Federal Reserve Board ordered further rate cuts in order to jump-start the economy.

Between August 2001 and January 2003, the Fed lowered the discount rate from 3 to 0.75 percent. Mortgage rates followed suit and sank to new lows. By May 2003, rates on thirty-year fixed mortgages had fallen to their lowest point in decades. Mortgage lenders did land office business and were flooded by consumers who wanted loans to buy or refinance homes. On the sidelines, Fed Chairman Alan Greenspan heaped praise on consumers for fueling consumer spending by taking out adjustable-rate loans in order to extract equity from their homes.

The mortgage boom was good for prime loans, but it was even better for subprime loans. Between 2001 and 2005, subprime lending's market share doubled in size, to twenty percent of consumer originations, and it stayed at twenty percent through 2006. Nationally, home prices grew at double-digit rates in 2004 and 2005. As housing prices rose, consumer confidence soared and lenders plied homeowners with offers of easy credit.[17]

Rising home prices created problems of their own. On the coasts, spiraling home prices outpaced family incomes, threatening to put home-buying out of reach for many aspiring homeowners. Meanwhile, interest rates began to go up. Between July 2004 and July 2006, the Federal Reserve Board raised the federal funds target rate by four percent and did not start lowering it until July 2007, which made mortgages more expensive and pushed up the index rates on adjustable-rate mortgages. Lenders found it harder and harder to qualify borrowers using standard underwriting criteria for safe fixed-rate mortgages.

---

[17] Statement of Sheila C. Bair, Chairman, Federal Deposit Insurance Corporation, on Strengthening the Economy: Foreclosure Prevention and Neighborhood Preservation; before the Committee on Banking, Housing and Urban Affairs, U.S. Senate, 538 Dirksen Senate Office Building, January 31, 2008, www.fdic.gov/news/news/speeches/chairman/spjan3108.html; Federal Reserve System, Truth in Lending, 73 Fed. Reg. 1672, preamble (Jan. 9, 2008).

As consumers became financially stretched, housing starts started to decline.[18] In the industrial Midwest, plant closings and job losses pushed many middle-income homeowners into default. Lenders and brokers, seeing the handwriting on the wall, changed their mix of loan products to keep loan originations – and their fee income – from falling off the cliff. To keep initial monthly payments within affordable reach, lenders began making more adjustable-rate mortgages (ARMs) and qualifying the borrowers only at the lower introductory rates. These subprime ARMs were not your parents' ARMs of yore, with low reset rates and manageable lifetime caps. Instead, the introductory rates on these subprime adjustable-rate loans started at seven to nine percent. Indeed, for mortgages originated in 2006, the average starting rate for subprime adjustable-rate mortgages – 8.29% -- was *higher* than the average 8.06% rate on subprime fixed-rate loans.[19] After the introductory period – normally, two or three years – when rate reset, high margins on these loans caused borrowers' monthly payments to go up overnight by fifty to one hundred percent or more. Far from the exception, these subprime "hybrid" ARMs accounted for three-fourths of subprime loans securitized in 2004 through 2006.[20]

Other ARMs had even more exotic features. Interest-only ARMs allowed borrowers to pay only interest, not principal, for an initial period. Even worse were option payment ARMs with negative amortization, which were peddled to prime borrowers and designed to make the borrowers' principal *grow* over time. Over three-fourths of borrowers with option payment ARMs only made the minimum payments, which increased the principal they owed on their loans.[21]

Lenders also dealt with rising home price appreciation by approving loans without verifying the borrowers' incomes or assets. If the borrower's income was too low to qualify, no problem. The lender could simply reach into its bag of tricks and pull out a stated-income loan, a NINA loan – no income, no assets – or even a NINJA loan – no income, no job, no assets -- based on the house value alone. Lenders even made these loans when borrowers gave them full documentation of their assets and income because lenders earned higher interest rates on low- and no-documentation loans. By 2006, more than forty percent of subprime loans and eighty percent of "Alt-A" loans that were securitized consisted of these sorts of "liar loans."[22]

As competition intensified, lenders and brokers scrambled for loan customers by reaching down the credit scale while loosening their underwriting standards. For borrowers with no down

---

18 Statement of Sheila C. Bair, Chairman, Federal Deposit Insurance Corporation, on Strengthening the Economy: Foreclosure Prevention and Neighborhood Preservation; before the Committee on Banking, Housing and Urban Affairs, U.S. Senate, 538 Dirksen Senate Office Building, January 31, 2008, www.fdic.gov/news/news/speeches/chairman/spjan3108.html.

19 Remarks by FDIC Chairman Sheila Bair, University of Connecticut School of Law, Hartford, Conn., Feb. 14, 2008.

20 Federal Reserve System, Truth in Lending, 73 Fed. Reg. 1672, preamble (Jan. 9, 2008).

21 Statement of Sheila C. Bair, Chairman, Federal Deposit Insurance Corporation, on Strengthening the Economy: Foreclosure Prevention and Neighborhood Preservation; before the Committee on Banking, Housing and Urban Affairs, U.S. Senate, 538 Dirksen Senate Office Building, January 31, 2008, www.fdic.gov/news/news/speeches/chairman/spjan3108.html.

22 Statement of Sheila C. Bair, Chairman, Federal Deposit Insurance Corporation, on Strengthening the Economy: Foreclosure Prevention and Neighborhood Preservation; before the Committee on Banking, Housing and Urban Affairs, U.S. Senate, 538 Dirksen Senate Office Building, January 31, 2008, www.fdic.gov/news/news/speeches/chairman/spjan3108.html; Gretchen Morgenson, *Crisis Looms in Market for Mortgages,* NEW YORK TIMES, March 11, 2007.

payment, 100 percent financing was easily had, generally by using piggyback second mortgages. Loans for the full property value or more went to people with tight incomes and spotty payment records. Loan terms were stretched out to forty or even fifty years. Desperate to keep origination volumes up, lenders layered risk upon risk, making no-documentation ARMs with high payment shock and no down payments to cash-strapped borrowers with low credit scores. The low initial payments on these loans lured numerous unsuspecting borrowers into larger loans than they could afford.[23]

There were warning signs in late 2006 that the subprime market was on the verge of collapse. Delinquencies were rising and so were foreclosures. That fall, Goldman Sachs and Balestra Capital placed lucrative bets that subprime investment vehicles would fall in value.[24] Investors began to insist that lenders buy back failed subprime loans. Funding sources began to dry up and in December 2006, Ownit Mortgage Solutions and Sebring Capital Partners became the first in a long line of subprime lenders to fail.[25]

In 2007, the house of cards came tumbling down. For the first time since the Great Depression, housing prices declined nationwide, sharply in some markets, and distressed borrowers found that they had limited options.[26] Rising interest rates, stricter underwriting, falling home prices, and harsh prepayment penalties made it difficult for borrowers to refinance. Falling real estate values prevented delinquent borrowers from paying off their loans in full by selling their homes.

Defaults soared and so did foreclosures. By November 30, 2007, one-fifth of subprime ARMs nationwide were ninety days or more delinquent or in foreclosure, many due to early payment defaults. Foreclosures are expected to rise as more loans come due to reset.[27]

Breakdown in Investor Trust

Even in isolation, the current rash of foreclosures would provide ample reason for concern. The repercussions from the subprime crisis, however, have been much more severe. To the disbelief of many observers, subprime loans that proved defective – due to lax underwriting or, worse yet, fraud -- have triggered a domino effect, causing multiple credit markets to become paralyzed worldwide. These credit markets broke down because investors lost confidence in the performance of subprime loans and any credit market and institution possibly tainted by them.

There are three major reasons why delinquent subprime loans mushroomed into contagion. The first is *leverage*, which refers to the fact that bad subprime loans often served as

---

23 Gretchen Morgenson, *Crisis Looms in Market for Mortgages,* NEW YORK TIMES, March 11, 2007.

24 Jenny Anderson & Vikas Bajaj, *Wary of Risk, Bankers Sold Shaky Mortgage Debt*, NEW YORK TIMES, Dec. 6, 2007; Nelson D. Schwartz & Vikas Bajaj, *How Missed Signs Contributed to a Mortgage Meltdown*, NEW YORK TIMES, Aug. 19, 2007.

25 Vika Bajaj & Christine Haughney, *Tremors at the Door*, NEW YORK TIMES, Jan. 26, 2007; see also The Mortgage Lender Implode-O-Meter, http://ml-implode.com/.

26 Anna Bernasek, *When Does a Housing Slump Become a Bust?*, NEW YORK TIMES, June 17, 2007; David Leonhardt & Vikas Bajaj, *Drop Foreseen in Median Price of U.S. Homes*, NEW YORK TIMES, Aug. 26, 2007.

27 Speech by Federal Reserve Board Randall S. Kroszner at the American Securitization Forum 2008 Conference, Las Vegas, Nevada, Feb. 4, 2008, www.federalreserve.gov/newsevents/speech/kroszner20080204a.htm.

collateral for several subprime bonds. Assume, for example, that Lender X makes a subprime residential mortgage to the Harris family and then securitizes that loan. The Harris family home will serve as collateral for the original mortgage-backed securities. In addition, Lender X may separately securitize any prepayment penalty on the Harris loan as a net interest margin security (a NIMS) for which the Harris home also serves as collateral. Sometime later, the issuer may take some of the original subprime mortgage-backed securities backed by the Harris family home, bundle them together with other subprime mortgage-backed securities, and resecuritize the bundle as a collateralized debt obligation (CDO). The Harris family home will serve as collateral for the CDO too. Finally, the investment bank that underwrote the CDO may resecuritize the CDO into a CDO of CDOs, with the Harris loan again serving as part of collateral. In this way, Lender X and investment banks *leverage* the Harris loan to serve collateral for multiple bonds.

If the Harris loan is defective and the family is forced into default, it will jeopardize repayment not just for one bond issue, but for several. The default of the Harris loan will boost the credit risk on four bond issues: (1) the original mortgage-backed securities; (2) the NIMS; (3) the CDO; and (4) the CDO of CDOs. Of course, these instruments are backed by hundreds or thousands of other subprime loans as well. If a large percentage of those subprime loans go into default – which is happening as we speak – then these bond issues faced deep losses and rating agency downgrades. Anyone who made the wrong derivative bets on the direction of these subprime mortgage-backed securities also sustained losses. As these dynamics came to fruition, the subprime mortgage-backed securities market dried up and so did subprime loans. The drought of mortgage credit became so severe that any mortgage not insured by Fannie Mae, Freddie Mac, or the federal government became highly costly or just plain unavailable. The most important example, of course, is jumbo home loans. In the process, banks once more must hold their non-conforming loans in portfolio, which puts their safety and soundness at risk.

Collateral is the second reason why subprime loans infected other markets. Many investors who bought subprime bonds later pledged those bonds as security for other types of credit. These investors included large institutional investors, both here and abroad, such as banks, hedge funds, state and local governments, insurance companies, and other large corporations. Some of these investors used their subprime securities as collateral for loans. Banks, for instance, pledged their subprime bonds as security for short-term loans from other banks on the market for interbank credit. Major corporations borrowed money from other corporations on the short-term commercial paper market by issuing paper backed by subprime bonds. Some money market funds purchased subprime-backed commercial paper as well. In recent months, concern about the underlying collateral caused the interbank credit market and the asset-backed commercial paper market to seize up. Some money markets that invested in commercial paper backed by subprime bonds have had to struggle to avoid "breaking the buck."

General investor panic is the third reason for contagion. Even in transactions involving no subprime collateral, concerns about the subprime crisis have had a ripple effect, making it difficult for companies and cities across-the-board to secure financing. Banks do not want to lend to other banks out of fear that undisclosed subprime losses may be lurking on their books. Investors do not want to buy other types of securitized bonds, such as bonds backed by student loans or car loans, because they have lost faith in the ratings issued by the rating agencies. Stocks in commercial banks, insurance companies, and Wall Street investment firms have taken a beating because investors fear that these companies have more subprime-related write-downs

in their future. Cities are having trouble floating municipal bond offerings because the AAA ratings of municipal bond insurers are in jeopardy due to mounting subprime liabilities at those insurers. In recent weeks, investor panic has crippled the leveraged financing market and the market for auction-rate securities. Initial public offerings have become a rarity. In a flight to safety, investors have flocked to U.S. Treasury bonds and gold. Increasingly, markets that have no subprime involvement are faltering due to generalized investor mistrust and flight. Because they do not know exactly who is tainted by subprime, investors have stopped trusting almost everyone.

Restoring Investor and Borrower Confidence

Going forward, what is necessary to restore public trust? While a number of measures are needed, one thing is for certain: people need assurance that in the future, home mortgages will be properly underwritten and free from fraud. The Connecticut General Assembly cannot turn around the economy by shaping national monetary policy. However, it *can* assure that home mortgages made in Connecticut are sensibly underwritten and not conducive to fraud.

Some might argue that the mortgage market has recently corrected the problem. If anything, the pendulum has swung too far the other way. According to press reports, it is now hard to get a residential mortgage unless you have a credit score of 700 or higher and at least six months' savings in the bank. These standards are so demanding that half of American households or more would flunk them on the spot.

In the meantime, history tells us that two things are certain. First, the subprime market will spring back in some form. Subprime loans disappeared for awhile in 1998 due to bankruptcies of subprime lenders, but eventually those loans came back. Subprime securitizations experienced a dent around 2001 to 2002, but later roared back to life. It may take awhile, but some way, in some form, the subprime market will return.

Second, history also proves that the subprime industry lacks sufficient incentives to guard against lax underwriting and fraud. It is too late to go back to the days when the lender marketed customers, underwrote loans, serviced those loans, and held them solely in portfolio. The unbundling of the mortgage market is a fact of life. Unbundling and the compensation structures that come with it create irresistible incentives for reckless lending and fraud. Even at this late date, moreover, the mortgage broker industry and the mortgage lending industry continue to resist effective self-regulation in the form of strong rules with binding effect and outside examinations for compliance.

Thus, if anyone is to restore confidence and trust to the home mortgage market, it will have to be the government. All three mortgage lending bills pending before the Committee – RHB 5577, SB 21, and SB 423 – would go a long way toward helping restore the faith of investors and borrowers in the Connecticut home mortgage market.

A new study that I coauthored with Kathleen Engel and economists at The Wharton School, the University of Southern California, and Marquette University sheds light on the effect

that state anti-predatory lending laws have on the flow of subprime credit.[28] In our study, we compared the effect of anti-predatory lending laws in different states on the likelihood that a subprime loan would be originated in 2004 and 2005. Surprisingly, we found that lowering the annual percentage rate (APR) triggers in state laws to regulate more loans *increased* the likelihood that a lender would originate a subprime loan.[29] Moreover, lowering those triggers helped offset any negative effect on access to credit that might flow from restrictions on loan practices such as prepayment penalties and balloon clauses in those laws.

In a follow-up study, my coauthors and I specifically examined the effect of assignee liability provisions in the state laws on access to credit.[30] We found no definitive evidence that assignee liability laws, even the strongest ones, restricted access to subprime loans. In six of the states with assignee liability laws, subprime origination probabilities went up consistently, while in the other three states, those probabilities went up using one definition of "subprime" and went down using a second definition of "subprime."

Our results help provide confidence that expanding regulation of home mortgages will increase access to credit, not restrict it. Lower triggers and assignee liability provisions in state anti-predatory lending laws may increase access to credit by providing lenders legal certainty and protecting them from competitive pressures to relax underwriting standards. Lower triggers and assignee liability provisions may also give consumers who previously had stayed on the sidelines the confidence to apply for home mortgages.

All three bills before the Committee would lower the triggers for coverage, while two of those bills would provide assignee liability to injured borrowers. Our research suggests that these provisions – particularly lowering the triggers – would help expand access to credit for borrowers who have the ability to pay for home mortgages.

For questions, contact Patricia A. McCoy at 860-570-5056 or patricia.mccoy@law.uconn.edu.

---

[28] Raphael W. Bostic, Kathleen C. Engel, Patricia A. McCoy, Anthony Pennington-Cross & Susan M. Wachter, *State and local anti-predatory lending laws: The effect of legal enforcement mechanisms*, 60 JOURNAL OF ECONOMICS & BUSINESS 47-66 (2008), http://www.sciencedirect.com/science?_ob=PublicationURL&_cdi=5851&_pubType=J&_auth=y&_acct=C000050221&_version=1&_urlVersion=0&_userid=10&md5=99e5dcd694a5f8f00fb8c8283f73e621&jchunk=60#60.

[29] In our study, we held the definition of a subprime loan constant, regardless where the APR triggers were set.

[30] Raphael W. Bostic, Kathleen C. Engel, Patricia A. McCoy, Anthony Pennington-Cross & Susan M. Wachter, *The Impact of State Anti-Predatory Lending Laws: Policy Implications and Insights* (working paper Jan. 25, 2008).

CT FAIR HOUSING CENTER

STATEMENT OF ANDREW PIZOR
IN SUPPORT OF S.B. 423

My name is Andrew Pizor. I am a staff attorney with the Connecticut Fair Housing Center. Thank you for the opportunity to speak in support of S.B. 423, which is designed to protect Connecticut homeowners from predatory mortgage loans. In addition to my support for S.B. 423, I also wish to state that another bill before the Committee today, H.B. 5577, also includes many similar provisions and would also do a great deal to protect borrowers from abusive practices that are unfortunately legal under existing law. Due to the similarities between the bills, my testimony will focus on one of the differences between the two bills – that is regulation of Yield Spread Premiums.

Yield spread premiums are a form of mortgage broker compensation paid by lenders. The size of the payment is largely based on the interest rate charged on a borrower's loan. The higher the interest rate, the larger the yield spread premium payment. Brokers can also earn higher YSPs for certain types of loans and when the amount of money borrowed exceeds a certain threshold. A more traditional method of broker compensation is when the borrower pays the broker directly based on a percentage of the loan principal. Yield spread premiums, however, are much more common in residential mortgages because they are more profitable to the brokers.

S.B. 423 would include YSPs in the existing 5% cap on prepaid finance charges allowed in home mortgages. H.B. 5577 only calls for disclosing YSPs, which is generally already done in most loans. The Governor's anti-predatory lending bill, S.B. 21, is silent on YSPs. Currently Minnesota, Illinois, North Carolina, Maine, New Jersey, Georgia, Massachusetts, and New York all regulate YSPs – mostly with different forms of caps.

YSPs should be capped because they are essentially kickbacks from the lender to the broker for getting homeowners into more expensive loans. While the industry defends YSPs by saying borrowers recoup the cost of YSPs through lower direct payments to brokers, research disproves that argument. Instead, a study recently published in the Stanford University Journal of Law, Business & Finance by a Harvard Law School professor shows that YSPs are often abused to over-charge unsophisticated consumers, including indications that minorities are especially at risk.[1]

[1] Howell Jackson, Kickbacks or Compensation: The Case of Yield Spread Premiums, Stanford J. of Law, Bus. & Finance (Spr. 2007) (all facts cited in my testimony are from this article unless otherwise noted).

221 Main Street, Hartford, CT 06106
Phone (860) 247-4400 • Fax (860) 247-4236

Toll Free (888) 247 4401

900 Chapel Street, 10th Floor, New Haven, CT 06510-2865
Phone (203) 772-3247 • Fax (203) 562-7107

It is often difficult for borrowers to protect themselves from unreasonable YSPs. The amount of the YSP is frequently unknown until the closing where it is usually disclosed as being paid by the lender. Most borrowers don't even know what a YSP is and, because it is paid by the lender, it is difficult for the average borrower to understand that the YSP ultimately comes out of their wallet in the form of higher interest rates. A 2002 survey by Fannie Mae[2] showed that over a third of all borrowers (and half of minority borrowers) incorrectly believed their broker was legally required to help them get the best interest rate. From my personal experience as a practicing attorney, I have found that the vast majority of borrowers believe brokers are acting in the borrower's best interests. Instead, any broker who is paid a YSP is actually working against the borrower's best interest by getting the borrower a more expensive loan.

The previously mentioned Stanford study examined between two and three thousand mortgages made between 1996 and 2001 and found the value of YSPs to vary widely among loans. That was in contrast to direct payments, which were more consistent in value. The author found this to be one indication that YSPs are manipulated to take advantage of less sophisticated borrowers. Comparing loans having direct broker compensation to those with YSPs revealed that brokers usually get paid more when they are paid by YSP. The estimated difference between direct payments and YSPs ranged from $600 to $1200 per loan.

Instead of recouping YSPs in the form of lowering other closing costs, the study found borrowers get less than thirty-five cents of value for every dollar of yield spread premium. Put another way, "for every additional dollar that a mortgage broker receives in yield spread premiums, that broker's total compensation appears to increase by somewhere between sixty-five and eighty cents." If the industry's argument regarding YSPs was true, every additional dollar of YSP would be matched by a dollar decrease in other closing costs paid to the broker. Analysis of actual lending practices show this is not the case.

Yield Spread Premiums are too often used to over-charge borrowers. They work as an incentive for brokers to act against the borrower's best interests. Mere disclosure of YSPs will not help borrowers protect themselves due to opaque and complicated pricing methods and lack of negotiating power. I encourage you to include a cap on YSPs in any bill that you enact.

Thank you for your time.

---

[2] THE GROWING DEMAND FOR HOUSING: 2002 FANNIE MAE NAT'L HOUS. SURVEY, available at http://www.fanniemae.com/global/pdf/media/survey/survey2002.pdf.

TESTIMONY SUBMITTED TO THE BANKS COMMITTEE
February 28, 2008

Commissioner Howard F. Pitkin
Department of Banking

HB 5577, AN ACT RESPONSIBLE LEADING AND ECONOMIC SECURITY and SB 220 AN ACT REQUIRING A SALES AND USE TAX EXEMPTION FOR CERTAIN SALES BY CONNECTICUT CREDIT UNIONS.

Good morning Chairman Duff, Chairman Barry, members of the committee, my name is Howard F. Pitkin and I am the Commissioner of the Connecticut Department of Banking. I am here to testify in favor of two pieces of legislation, but first I would like to clarify an oversight in my testimony last week. When I was speaking on ***SB 21, AN ACT CONCERNING MORTGAGE LENDING,*** I stated that 20% of sub prime loans are seriously past due and in likelihood of foreclosure. The actual number is about 8%. I want to apologize to the committee, hopefully no confusion resulted. The two ratios I cited were simply different measurements and I will respond to any questions on this matter.

Moving forward to the legislation before the committee today, ***HB 5577, AN ACT RESPONSIBLE LEADING AND ECONOMIC SECURITY*** is a bill designed to try and address the current mortgage crisis. While the department appreciates the time and effort it took to craft HB 5577, the agency cannot support the bill. Instead, we would like to ask the committee to endorse ***SB 21, AN ACT CONCERNING MORTGAGE LENDING*** a Governor's bill and the agency did work with her office in drafting the bill. I spoke in detail on the bill during last week's banks committee public hearing. I will not go into specific aspects of the merits of SB 21 again, but I did want to convey the agency has being working with other interested parties and will be submitting substitute language on the bill which we believe is acceptable to all involved. This language should be provided to the committee by the end of the week.

The agency would like to lend its voice to support ***SB 220, AN ACT REQUIRING A SALES AND USE TAX EXEMPTION FOR CERTAIN SALES BY CONNECTICUT CREDIT UNIONS.*** This bill would allow an exemption from the sales and use tax for sales of tangible personal property to state chartered Connecticut credit unions.

Currently, only federally chartered credit unions benefit from this tax exemption. To level the playing field between the state and federally chartered credit unions, I fully endorse the elimination of this tax. According to estimates researched by the agency, the loss in tax dollars to the General Fund would be less than $500,000 per fiscal year. This is a minimal loss to promote fairness in the private sector and continue to encourage

Legal Assistance Resource Center ❖ of Connecticut, Inc. ❖

44 Capitol Avenue, Suite 301 ❖ Hartford, Connecticut 06106
(860) 278-5688 x203 ❖ FAX (860) 278-2957❖ RPodolsky@larcc.org

S.B. 423 -- Foreclosure Prevention and Responsible Lending

Banks Committee Public Hearing -- February 28, 2008
Testimony of Raphael L. Podolsky

Recommended Committee action: **JOINT FAVORABLE**

This bill, which overlaps Sections 9 through 23 of H.B. 5577 and parts of S.B. 21, contains strong and effective requirements to minimize the likelihood of a repetition of the present mortgage and foreclosure crisis. We urge passage of S.B. 423 as a separate bill or, in the alternative, the merging of its provisions into Sections 9 through 23 of H.B. 5577.

Among its most important provisions, S.B. 423 includes the following:

- Lender and broker duties: S.B. 423 prohibits the "churning" loans (refinancing loans without providing any tangible benefit), requires reasonable efforts to avoid making loans not advantageous to the borrower, prohibits making loans in the absence of a reasonable belief that the borrower will be able to repay, and requires termination of a foreclosure action and reinstatement of the mortgage if all defaults are cured during the course of a foreclosure.

- Subprime and non-traditional mortgages: For subprime and non-traditional mortgages, S.B. 423 requires tax and insurance escrows, requires referral for pre-loan counseling, mandates counseling if the loan will refinance a subsidized ("special") mortgage, prohibits prepayment fees, prohibits any payment being more than double the other payments, prohibits negative amortization, prohibits restriction of dispute-resolution forums with less-than-full remedies, prohibits raising the interest rate after default, and requires verification of income at the fully-indexed rate for the loan.

- Remedies: S.B. 423 provides effective remedies for homeowners who are the victims of violations of the act, including statutory damages, the right to raise non-compliance with the act as a defense in a foreclosure action, and a significantly higher bond requirement for licensed lenders and brokers.

The provisions of this bill set strong standards for the lending industry and significantly reduce the risk that the overextension of credit that has caused such havoc in the housing market will recur. They give effective enforcement powers to the Banking Commissioner, to the Attorney General, and to consumers themselves. It is important that they be a part of any legislation coming out of the Banks Committee.

Legal Assistance Resource Center ❖ of Connecticut, Inc. ❖

44 Capitol Avenue, Suite 301 ❖ Hartford, Connecticut 06106
(860) 278-5688 x203 ❖ FAX (860) 278-2957❖ RPodolsky@larcc.org

H.B. 5577 -- Responsible Lending and Economic Security

Banks Committee Public Hearing -- February 28, 2008
Testimony of Raphael L. Podolsky

Recommended Committee action: **JOINT FAVORABLE**
with addition of protections from S.B. 423

We support this bill, which contains both an expansion of programs to help finance homeowners out of unreasonably costly loans and an increase in protections for borrowers, especially in the subprime market. In particular, we support the creation of refinancing programs (REAL and HERO) and the expansion of the existing EMAP program. We also suggest that the Committee consider dividing H.B. 5577 into two bills. One, comprised of Sections 1-8, would have the financing sections. The other, Sections 9-23, would regulate the making of mortgage loans and could be merged into S.B. 423 (along with some portions of S.B. 21). In the alternative, parts of S.B. 423 could be merged into H.B. 5577. If the latter approach is taken, then at least the following parts of S.B. 423 should be included in H.B. 5577:

- Discount points (l. 376-378): H.B. 5577 does not include "bona fide" discount points in the interest rate (the APR). In practice, a lender will almost always be able to claim that points are in lieu of a higher interest rate and are therefore bona fide. Since some of the protections in the bill apply only to "nonprime" (i.e., high interest) loans, leaving this loophole in the bill will result in evasion of its protections.

- Non-traditional mortgages and open-end loans (l. 334-338): The bill's definition of "nonprime" excludes open-end and non-traditional mortgages (i.e., mortgages in which the payments do not reduce the principal balance, such as negative amortization and interest-only loans). They are part of the problem and should not be excluded.

- Yield-spread premiums (l. 583-597): Yield spread premiums (i.e., payments by the lender to the broker for placing the homeowner into a higher-cost mortgage than is required by his credit rating) are really upfront payments made by the borrower to obtain the loan. S.B. 423 properly includes them in calculating the number of points charged for the loan. H.B. 5577 merely requires disclosure. For subprime mortgages, however, disclosure is insufficient. Failure to include these premiums will allow these loans to dodge existing statutory requirements limiting the number of points that can be charged.

- Ability to repay (l. 406-407, l. 576-582): H.B. 5577 provides that lenders and brokers have a fiduciary duty to borrowers and requires mortgage brokers to make reasonable efforts to secure loans that are in the best interests of their borrowers. H.B. 5577 should give specificity to this requirement by creating a rebuttable presumption that a loan is not in the best interest of the borrower if it will make his total debt obligation in excess of 45% of his income.

Chairpersons Duff and Barry, members of the committee; my name is Richard Tracy and I represent the Connecticut Society of Mortgage Brokers. Today I wish to comment on Raised Bill 5577.

I commend the committee for developing a Bill that includes such innovative programs as REAL, HERO and EMAP. It is my hope that when implemented these programs will provide relief and hope for Connecticut homeowners experiencing distress because of difficulties related to their mortgage. On behalf of the Society, I offer our assistance.

I also am encouraged as I read the balance of the bill. The approach of the bill's authors in crafting a bill directed at addressing the challenges facing the mortgage business is balanced and fair. I am particularly pleased with the inclusion of section sixteen that introduces the concept of required education for participants in the mortgage industry. There are two sections the committee may wish to address. First, the wording looks to education requirements for "licensed entities in the mortgage lending business." Please consider that mortgage Originators are not at this time licensed and might therefore be exempt from this section. Second, the Society suggests that the required content be more specifically developed to include topics focusing on State and Federal regulations. Perhaps it might be appropriate to assign to the Commissioner's office the responsibility to decide on subject topics.

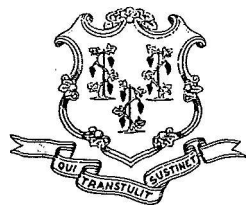
Finally, I urge the committee to consider the impact of defining a Non-prime loan based on the triggers included in the current draft. These triggers mirror Federal Reserve guidelines. It is our position that these triggers levels, originally developed four years ago are no longer appropriate. The economic environment at the time these trigger were settled on was one of more available credit and significantly lower costs of credit. The spread between mortgage interest rates and Treasury yields was much lower. One impact of the credit crunch is that the costs of securing mortgage financing have increased.

Mortgage interest rates and costs are now affected by an increase in mortgage insurance premiums and the application of risked based pricing by FNMA and Freddie Mac that is FICO score based. It is significant to note that FNMA's risked based pricing now adds to the cost of loans with FICO scores less than 700. Because the FICO threshold for the best pricing is set at 700 Connecticut mortgage applicants will be affected given that the average FICO score in Connecticut, based on the web site freecreditreport.com, is 694. The result of these increased costs is that the spread between mortgage rates and treasury yields is higher, thus setting the beginning point of the trigger calculation closer to the non-prime threshold.

I respectfully request that the committee consider changing the threshold numbers to five and seven. Alternatively, given the affect that changes in the economy and mortgage costs have on the spread between mortgage interest rates and treasury yields perhaps the responsibility for setting the trigger levels should be assigned to the Commissioner and be required to be reviewed annually.

I am also concerned regarding identifying the measurement index and I ask that you more clearly define the source of the data against which a trigger will be measured. Treasury instruments are reported in many places and often in a different format. The committee may wish to also rely specifically on H-15.

Room 3300
Legislative Office Building
Hartford, Connecticut 06106-1591



860-240-8600
Williams@senatedems.ct.gov
www.senatedems.ct.gov

State of Connecticut
SENATOR DONALD E. WILLIAMS, JR.
Twenty-ninth District
President Pro Tempore

Testimony

HB 5577 AAC Responsible Lending and Economic Security

Banking Committee

Thursday, February 28, 2008

Senator Duff, Representative Barry, and the members of the Banking Committee,

I want to thank and commend you for your diligence in preparing such a comprehensive package that addresses the impact of the sub-prime mortgage crisis on Connecticut residents.

The proposals in HB5577 are innovative and comprehensive. They address the root causes of the crisis by improving regulations over lenders and brokers who market non-prime mortgages. Moreover, they have the potential to reach far more of those who have been victimized by the crisis than current government programs that have been hastily put into place.

Earlier this week, the National Realtors Association reported more indications that the sub-prime mortgage crisis refuses to wane. For the 6th month in a row, the number of home sales dropped across the nation and the median home sale price dropped by 4.6%.

Closer to home, the indicators show that Connecticut has not been sheltered from this crisis. There were 1,733 foreclosures in December, an increase of 61% over December of last year. The foreclosure rate in our state has risen to one in every 821 households.

The impact of the sub-prime mortgage crisis goes beyond the borrowers who face unmanageable increases in their home loans, or worse, foreclosure. The crisis affects the neighbor whose home value dropped just when they had planned to leverage their equity to send a child to college. It forever alters the future of empty nesters who planned to sell their home and downsize toward retirement. It affects young families who wanted to purchase their first home, but can't because of so much uncertainty and the market's overcompensating aversion to risk.

The national mortgage crisis has caused an economic ripple effect, impacting us at the local level. Foreclosures and tight credit increase the supply of housing in a way that does not

Printed on recycled paper

contribute to economic growth. Instead, it diminishes property values and ultimately property tax revenues. The pattern of homeowners taking portions of the equity they've earned on their home and reinvesting it through improvements that spur the local economy has been broken. And, the 38% drop in new housing permits over the past year negatively impacts the real estate and construction sectors.

As the members of this committee know all too well, government's response thus far has been insufficient. It has done nothing to prevent such a crisis from happening again.

Your bill, HB5577 AAC Responsible Lending and Economic Security, has as its goals, protecting borrowers from unscrupulous lenders and brokers who act against consumers' best interests. More importantly, it seeks to provide relief to those who have been victimized by the crisis, ultimately helping to dampen its impact on Connecticut residents.

Remarkably, there are some who would criticize provisions of this bill on the grounds that by helping people save their homes, you would be bailing out those who assumed the inherent "risk" that is part of the mortgage market. Under normal circumstances, this would be true. However, given what we know now about the deceitful practices of some sub-prime brokers and lenders, these arguments are in many cases unfounded.

The lenders and brokers that triggered this crisis artificially inflated borrowers' income documentation, unduly influenced appraisal process, hid insurance charges, and obscured the impact of balloon and variable interest rates from the borrowers they advised.

A significant portion of our economy relies on the health of the housing market. With the housing market shaken, and the economic well-being of the state at stake, governmental action is necessary – just as it was when government stepped in to purchase at-risk mortgages and provide more affordable long-term financing to borrowers during the Great Depression and the mortgage crisis of the 1980s.

I support the goals of HB5577, which are to diminish the economic uncertainty in Connecticut triggered by the sub-prime mortgage crisis and provide relief to those who were unjustly harmed by it. My caucus and I are committed to achieving these goals and are eager to work toward passage of a relief package that protects homeowners and restores confidence in the housing market.

HB5165

STATEMENT OF
Michael J. Ward
Administrator – Planning and Budget
CONNECTICUT HOUSING FINANCE AUTHORITY
ON FEBRUARY 28, 2008
BEFORE THE BANKS COMMITTEE
Regarding Raised Bill 5577
An Act Concerning Responsible Lending and Economic Security

Chairman Duff and Chairman Barry, Members of the Banks Committee, I am Michael J. Ward, Administrator for Planning and Budget at the Connecticut Housing Finance Authority. In 1969, the Connecticut Housing Finance Authority (CHFA) was created by legislation with the mission to help alleviate the shortage of affordable housing for low- and moderate-income families and persons in Connecticut. CHFA is a self sustaining, quasi-public organization, which uses its resources to provide below market interest rate mortgages for single family homeownership and multifamily rental properties. Tax exempt bonds are the primary source of mortgage capital for the Authority's housing programs. I am here today to discuss Raised Bill 5577, An Act Concerning Responsible Lending and Economic Security.

However, I would like to note that Governor Rell has also introduced S.B. 21, An Act Concerning Mortgage Lending which incorporates legislative changes to address sub-prime lending practices. This legislation embodies recommendations of the Governor's Sub-prime Mortgage Task Force which Gary King of the Authority had the honor of co-chairing with Commissioner Pitkin, who is here to speak to several important aspects of the sub-prime issue addressed in RB5577. I would second his testimony on these matters.

Before making specific comment on RB5577 I want to thank the Committee for the opportunity to be here this morning to discuss this important proposed legislation. While we have very serious concerns about some of what is proposed in this bill we acknowledge the Committee's efforts in proposing legislation to help address the serious challenges faced by many Connecticut homeowners. CHFA understands the nature of the problem that the Committee and our State is facing and would like to work with the Committee to address these challenges. The job we all face in addressing this matter is certainly daunting. The numbers of Connecticut homeowners affected and the significant cost of assistance programs require that we all, including mortgage servicers and investors, work together if we are to help as many homeowners as possible.

It is this spirit that the Authority offers these comments to the Committee this morning.

Summary points:

- The Connecticut Housing Finance Authority (CHFA) must strongly oppose the taking of bond proceeds pledged to Authority bondholders as a means to fund the HERO and REAL Programs.
- The CTFAMILIES Program is a good, fundamentally sound, program that will succeed in utilizing the resources available and should not be ended to fund the REAL Program.

- The mortgage assistance approach embodied in the HERO program authorized by the RB5577 is a good idea and the Authority would like to work with the Committee in developing such a program.
- Emergency Mortgage Assistance has an important role to play in Connecticut's overall approach to the Sub-prime crisis. The Authority suggests that the Committee consider funding this initiative through non-profit housing organizations already working with the Authority on sub-prime mortgage relief efforts.

CHFA strongly opposes the taking of $40 million in CHFA mortgage revenue bond proceeds ("Pre-Ullman" proceeds) to fund the HERO and REAL programs authorized under the R.B. 5577.

This taking of Authority mortgage revenue bond proceeds is a direct threat to the Authority's bond rating which would negatively impact the pricing of $3.5 billion in outstanding Authority debt as well as the interest rate on the nearly $740 million in additional new bonds the Authority plans to issue in 2008 to support its programs-- including any new programs developed to address sub-prime lending. This would be especially damaging at a time when the credit markets upon which the Authority relies on to finance its housing programs are in severe turmoil. Its current AAA bond rating is **the** factor that is allowing the Authority to navigate in this market without serious limitations on its ability to fund ongoing programs in a reasonable cost.

This type of taking is viewed very negatively by bond rating agencies which provide public rating to support the sale of Authority bonds. Authority bond proceeds are private investor funds that are pledged by the Authority to be repaid to these investors with interest. Authority bond documents and covenants are documents of trust. Investors in Authority bonds have the right to expect that the proceeds will be used for housing program activities that the Authority has disclosed in official public offering statements to investors. The CTFAMLIES program is consistent with these disclosures, the REAL program authorized by RB5577 and which carries a significantly higher risk profile, is not.

Also, the Committee needs to be aware that there is a relationship between Authority's bond rating and State of Connecticut's bond rating. The State of Connecticut provides contingent backing to the Authority, making the Authority contingent liability of the State. Currently the Authority's bond rating is higher than the State's bond rating and not a negative consideration relative to raising the State's bond rating. Should the Authority's rating be lowered to the same or lower than the State's rating this would no longer be true.

Many, including members of the General assembly have urged CHFA to increase its level of bonding activity to support multifamily housing development and rehabilitation programs. Public Act 07-234 required the Authority to utilize 10 percent of its annual statutory authorization to fund affordable multifamily rental housing. During the Fall, the Authority worked hard to develop a program for 2008 that would increase funding for multifamily rental housing as well as provide the maximum amount of affordable home mortgage funding possible to continue to address homeownership needs and sub-prime issues in our state within the limits of the Authority's resources and maintaining its bond rating. The CTFAMLIES program and other sub-prime lending initiatives are a part of this overall program. The taking of Authority

assets in RB 5577 is a direct threat to this overall program. A lowered Authority bond rating would drive up the Authority's cost of funds and the mortgage interest rate for all CHFA borrowers, under both the single family and multifamily programs - including the $80 million the Authority plans to issue to support affordable multifamily rental housing.

Additionally, by statute the Authority may undertake up to $1 billion in uninsured lending. The Authority is currently close to reaching this limit and has reserved this capacity to support financing for the development and preservation of affordable multifamily rental housing. The bond proceeds that RB 5577 takes to fund the REAL Program would be utilized on an uninsured basis and thus would count against the Authority's uninsured lending cap at the expense of supporting affordable multifamily rental housing.

Over the past several years CHFA has been able to combine new and recycle bonding Authority to assist the 4,000 new low- and moderate-income first time homebuyers each year. Due to the effect of federal tax rules on the Authority we will be able to assist only about 2,750 borrowers in 2008. Increasing CHFA's cost of funds will damage its efforts to raise the $500 million required to help these new lower- and moderate-income first-time homebuyers in 2008. Keeping such homebuyers in the marketplace is important to maintaining stability in our neighborhoods and communities. Over the years, the Authority has financed significant levels of homeownership activity in communities and neighborhoods deeply impacted by the sub-prime mortgage crisis. If not for the Authority's home mortgage programs there would be significantly more sub-prime mortgages in these communities. We have attached two maps that show historic lending patterns for the Authority's Home Mortgage Program as well as the recent sub-prime lending in Connecticut.

It is important to note that the Governor's Sub-prime Mortgage Task Force Report recognized the importance of the Authority's Home Mortgage Program lending in serving borrowers and communities that may have otherwise resorted to sub-prime mortgages. The Task Force recommended that the Authority maintain and expand home mortgage lending programs to assist such low- and moderate-income first-time buyers and communities. Consistent with the recommendations of the Governor's Sub-prime Mortgage Task Force the Authority is currently reviewing ways to increase affordable funding available to assist Connecticut home buyers that in the past may have relied on sub-prime mortgage lending. Any lowering of the Authority's bond rating would also significantly impede these efforts as well.

For these reasons the CHFA must strongly oppose the taking of Authority funds under RB 5577.

The CT FAMLIES program is a good approach to refinancing sub-prime borrowers and will utilize all funds made available.

The CTFAMLIES program uses flexible individual underwriting of loans to assist borrowers on a case-by-case basis consistent with underlying Federal Housing Administration (FHA) mortgage insurance. CHFA strongly believe that the CTFAMLIES Program, using this approach, reaches more borrowers and offers better terms than the REAL program authorized by RB 5577. The CTFAMILIES program does not rule out applicants based on FICO score, is

easier on credit, and allows for higher debt to income ratios with compensating factors. The Authority does not believe that the household income and mortgage limits have proven to be a significant factor in limiting demand for the program. The progress of this program has been similar to other States, and better than most. It's just too early to prejudge the success of this program. For example the Pennsylvania REAL program upon which RB 5577 is modeled has been open since July 2007 and currently has 33 reservations and 14 closed loans. We are confident that the CTFAMLIES program will progress more quickly.

The CTFAMLIES program was implemented closely following the recommendations of the Governor's Sub-prime Mortgage Task Force. The initial targeted group of homeowners to be assisted through the CTFAMLIES program has been those low- and moderate-income first-time homebuyers that used an adjustable rate sub-prime mortgage to acquire their first home but could no longer afford homeownership due to the increase in mortgage payments under their sub-prime adjustable rate mortgage. The CTFAMLIES program started with this group of homeowners as they are the targeted homeowners that have been traditionally assisted by the Authority's and the State of Connecticut's homeownership programs.

Given the demand and need for the program the Authority is currently considering broadening eligibility for this program and is confident that given some additional time and adjustments to the program, the CT FAMLIES program will utilize all of the $50 million made available.

If RB 5577 proceeds it would be necessary for the Authority to halt the CTFAMLIES program just as it is gaining momentum in order to reserve that funding to be taken for the REAL program that would not be available to the public before the fall of 2008.

The Authority believes that making some changes in the eligibility criteria for the CTFAMLIES program is will result in exhaustion of available funds prior to the REAL program becoming available.

The loan purchase approach embodied in the HERO Program authorized by R.B. 5577 is a good way to help additional CT homeowners stay in their homes.

The loan purchase approach embodied in the HERO program authorized by R.B. 5577 was reviewed and discussed by the Governor's Sub-prime Mortgage Task Force.

The Authority has taken initial steps in discussing this approach with mortgage servicers and FHA and would like to work with the Banks Committee, as well as other interested parties, in developing a program that the Authority could offer to supplement CT FAMLIES. However, we should not underestimate the difficulty and complexity that we will face in developing a viable program. The complicated network of mortgage servicers and investors and mortgage pool agreements with complicated webs of rights, privileges and protections make devising a program a real challenge.

The Authority is exploring ways it may be able to raise additional new mortgage capital to implement such a program that would supplement the mortgage revenue bond funding already allocated for the CT FAMLIES program.

It important to emphasize once again that a reduction in the Authority's bond rating due to the taking of Authority proceeds to fund the REAL program would also negatively impact the cost of funds with this mortgage purchase program, limiting the amount of benefits that could be provided to the homeowner.

The Authority believes that an important consideration to the success of such efforts would be the ability of the Authority to acquire Connecticut sub-prime mortgages at some discount. This discount would enable the lower mortgage balance to be financed at an affordable fixed rate for the current homeowner. Additionally, it may be more cost effective to implement such a program with a wholesale rather than retail approach, acquiring pools of mortgages that could be rewritten according to an established set of parameters.

The Authority believes, and the committee may wish to consider, that some discounting and concessions on the part of current mortgage investors is an important equity consideration in development of such a program. It does not seem equitable for the State of Connecticut or the Authority to provide significant public resources to make investors "whole" in order to provide needed assistance to stressed Connecticut homeowners - particularly when in the absence of such assistance the investors face the likelihood even greater loss through the foreclosure process. Making investors whole, by somehow ensuring no loss, typically benefits the highest yield investors in the underlying mortgage pool. Typically, those investors that took the first loss position receive the highest interest rate yield in the pool. Relief to the borrower, without concessions from investors, insulates these high yield investors from market discipline. Providing mortgage assistance coupled with concessions from the investors would balance market discipline with some relief to the homeowner.

An emergency mortgage assistance program such as that authorized by the R.B. 5577 can play an important role in Connecticut's overall approach to the Sub-prime mortgage crisis.

The Authority suggested in testimony on RB5165 An Act Inserting Emergency Mortgage Assistance Program that, if the Committee proceeds with this legislation authorizing an emergency mortgage assistance program, the Committee look to non-profit housing organizations, such as Neighborhood Housing Service (NHS) offices, as the entities to implement the new proposed funding for the EMAP program.

In light of the language in RB 5577 we continue to suggest that the Committee consider funding emergency mortgage assistance through local nonprofit housing organizations already active in the sub-prime area. This approach would be similar to the manner in which the Authority originates a mortgage loans through its network of participating lenders.

We believe that this approach has two advantages. First it will save government agencies the overhead cost gearing up to run this program directly. Second, program fee income could be used to further strengthen the capacity of these important non-profit agencies to be of service to their communities.

These organizations are already involved directly with the Authority on a daily basis in counseling applicants for the CT FAMLIES program as well as providing foreclosure and delinquency counseling and other secondary loan programs. This experience places such organizations in a good position to assist the state's overall effort by providing emergency mortgage assistance in close coordination with other initiatives offered by the state, and possibly the federal government.

It was noted by CHFA that Neighborhood Housing Services of New Haven offers a rescue program which could help borrowers be able to refinance and possibly look to the CT FAMLIES program. Its approach is consistent with the general terms for emergency mortgage assistance outlined in RB 5577.

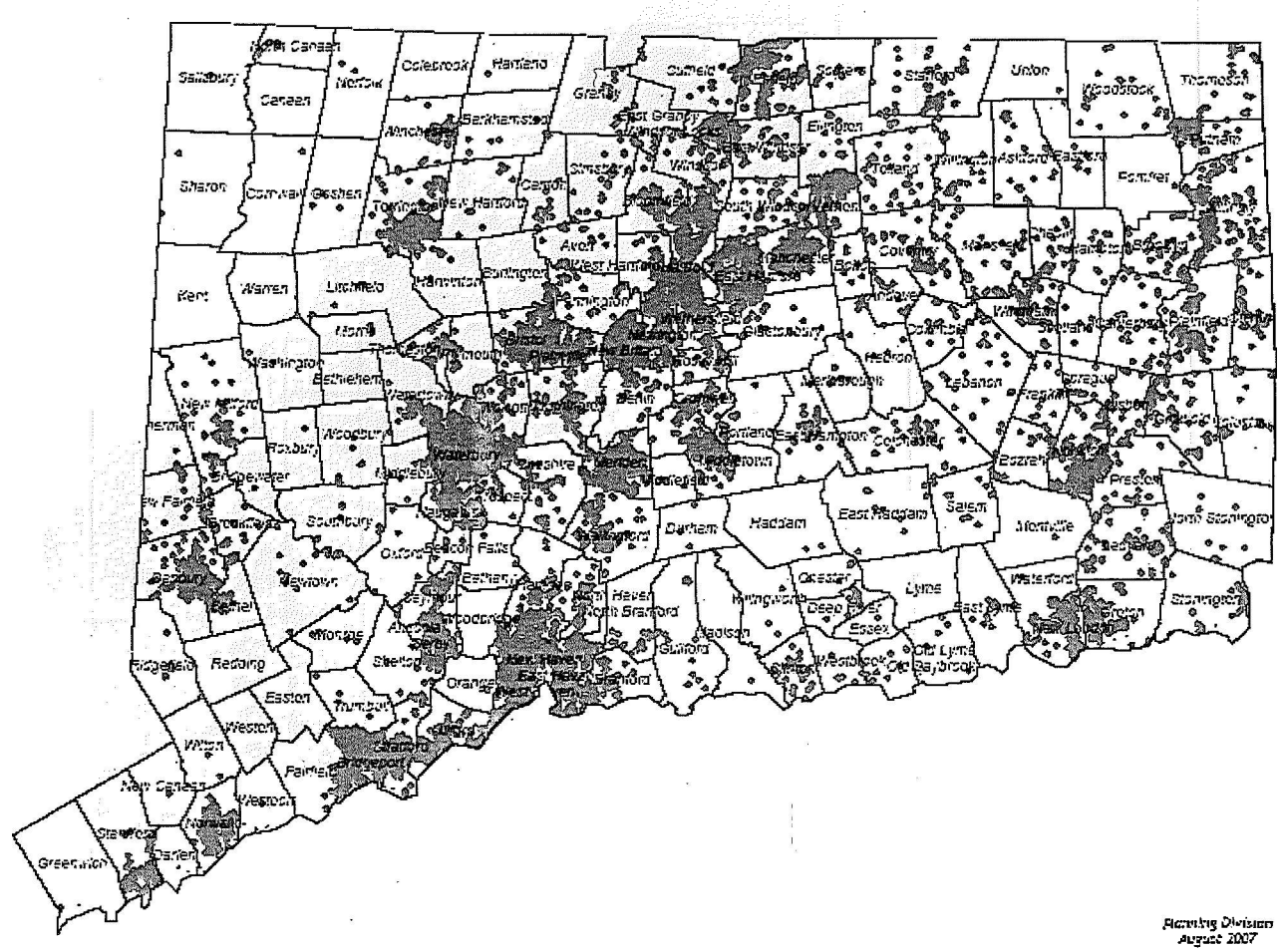
Additionally, the Committee may wish to consider whether or not it believes some equity consideration on behalf of mortgage holders and investors would also be appropriate in the area of emergency mortgage assistance. While assisting the homeowner, emergency mortgage assistance is also insulating the investor from direct risk of loss. It seems appropriate that the investor should provide some consideration for this reduced risk. For example, the Committee may wish to consider whether or not the lender should be required waive any prepayment penalty that an assisted homeowner incur once they have been returned to good standing and have moved on to refinance their sub-prime mortgage with another lender. Such a waiver would be consistent with concessions that many in the mortgage industry are now urging, out of self-interest, in order to provide relief to distressed homeowners, and in the long-run mitigate investor losses.

We are available to work with the Committee in developing an approach to emergency mortgage assistance that would utilize such nonprofit housing organizations as an origination network for emergency mortgage assistance loans in much the same way the Authority uses participating lenders across the state. As these organizations are already working with the Authority on the sub-prime and foreclosure issues this appears to be an efficient and direct approach.

Thank you very much to the Committee for the opportunity to provide these comments and I'll do my best to answer any questions you may have.

000596

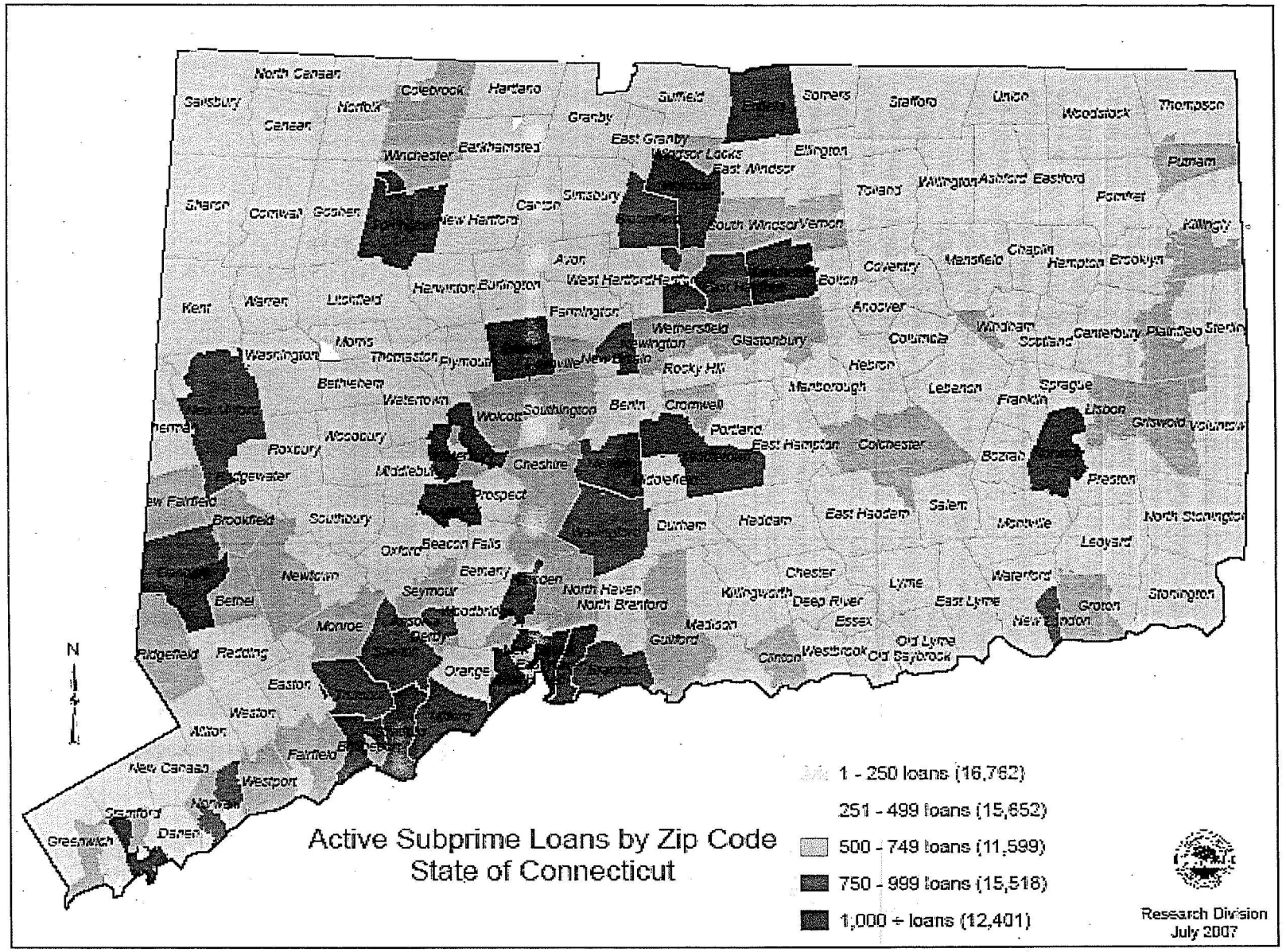
CHFA Single Family Mortgages



Planning Division
August 2007

Based on Authority single family mortgage loans

000597



Source -- Loan Performance -- based on 71,932 mortgage loans

Prepared by: L. Zajac

000598

DIRTY DEEDS

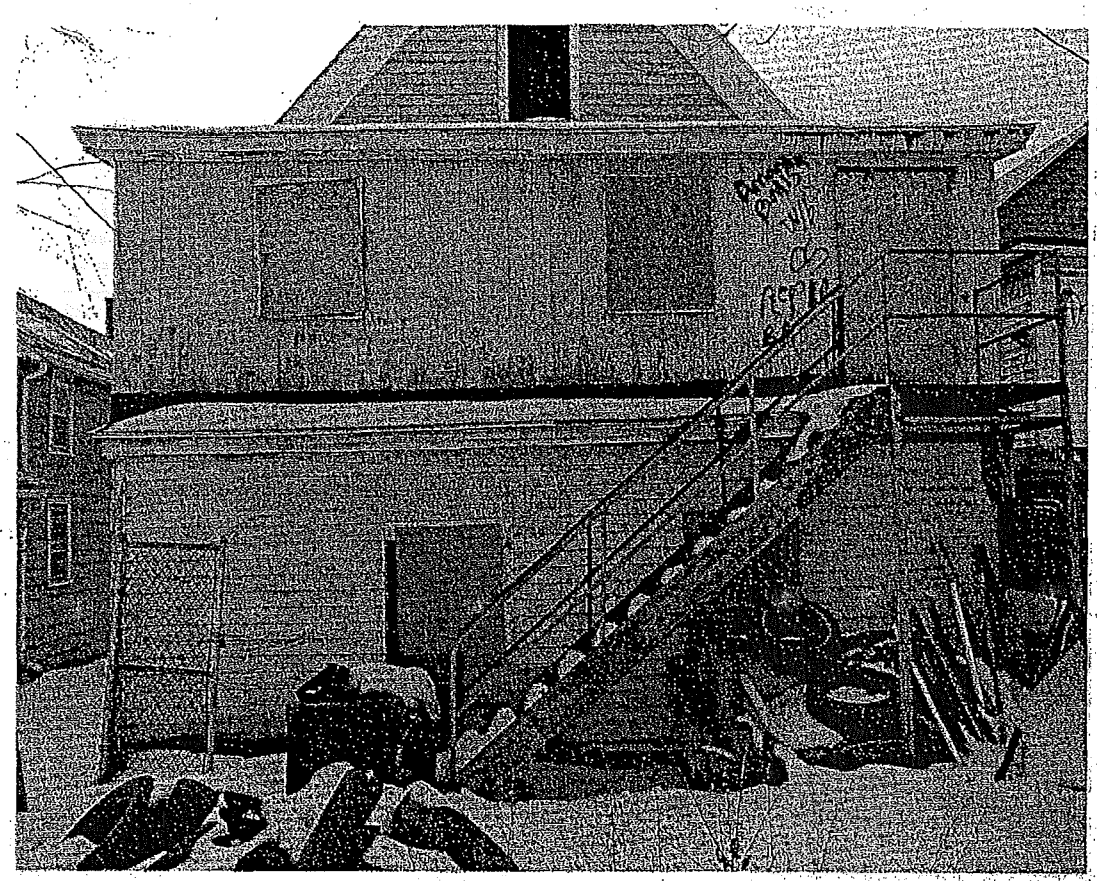
047

The mortgage crisis has blighted the landscape with boarded-up houses. Now a few cities are holding giant lenders accountable for what foreclosure leaves behind

By Michael Orey
Photography by Michael Todd

On Dec. 17 in a windowless Buffalo courtroom, Cindy T. Cooper, a prosecutor for the city, buzzes among a dozen men in suits, cutting deals. "You've got to unboard [the house], go in, and clean it out," she tells one. "If all the repairs are done quickly, I wouldn't ask for any fines." To another, she says, "the gutters weren't done right," and asks to see receipts for the work. It's "Bank Day" in Judge Henry J. Nowak's housing courtroom, more typically a venue where landlords and tenants duke it out over evictions and back rent. Instead, Cooper is asking lawyers for CitiFinancial, JPMorgan Chase, and Countrywide Financial to fix problems like peeling paint, broken masonry, and overgrown or trash-filled yards at houses the city says the banks are responsible for maintaining. It may be surprising to find these financial-services giants hauled before this obscure local tribunal. In fact, Cooper and Nowak are at the forefront of a pioneering effort to deal with a vexing problem: the surging number of vacant and abandoned homes resulting from the mortgage market meltdown. The vacancies occur when lenders bring foreclosure suits against delinquent borrowers. Mere notice that such an action might be filed often sends residents packing. In Buffalo and other Rust Belt cities, the problem has been particularly acute, because in many cases banks are abandoning the houses, too, after determining that their value is so low that it's not worth laying claim

Buffalo city prosecutor Cooper is fighting back against deadbeat banks



Homeowners may flee, but banks still retain liens on abandoned houses

to them. When city officials try to hold someone responsible for dilapidated properties, they often find the homeowner and bank pointing fingers at each other. Indeed, the houses fall into a kind of legal limbo that Cleveland housing attorney Kermit J. Lind calls "toxic title" (table, page 50). While formal ownership remains with a borrower who has fled, the bank retains its lien on the property. That opens up a dispute over who is responsible for taxes and maintenance. Even when lenders do complete the foreclosure, they may walk away from the property, leaving it to be taken by a city for unpaid taxes, a process that can take years. Orphaned properties quickly fall into disrepair, the deterioration sometimes hastened by vandals who trash the interiors, lighting fires and ripping out wiring and pipes to sell for scrap. Squatters or drug dealers may move in.

The impact goes far beyond the defaulting homeowner, as neighbors and entire communities confront a spreading blight. Vacant residences deprive cities of tax revenue and can cost them thousands to maintain. A 2001 Temple University study in Philadelphia found that simply being within 150 feet of an abandoned property knocked $7,600 off a home's value.

In Buffalo, prosecutor Cooper is bringing lenders before Judge Nowak to hold them accountable. Wielding the threat of liens, which can hold up the lenders' other real estate transactions, she aims to make banks keep foreclosed homes in good condition until a buyer can be found. As an alternative, Cooper or Nowak may try to get lenders to donate properties to community groups or to pay for demolition when houses are beyond repair. "At least in Buffalo," says Cooper, "the days are gone when you can do a foreclosure and walk away without taking care of the property."

"THE DAYS ARE GONE WHEN YOU CAN DO A FORECLOSURE AND WALK AWAY WITHOUT TAKING CARE OF THE PROPERTY," SAYS COOPER

Those charged with violations by Cooper include participants all along the complex mortgage-industry food chain, from loan originators to servicers to the Wall Street trusts that buy up the vast majority of home loans and then securitize them. A similar initiative is under way in Cleveland, where

Judge Raymond L. Pianka puts lenders on trial in absentia when they fail to respond to charges.

Even places with high property values, like Chula Vista, Calif., a San Diego suburb, are taking steps to avoid the neglect that can occur during lengthy foreclosures. "It seems like a number of the lenders aren't even doing things that are in their own best interest to preserve the asset," says Pianka—a problem he attributes to the fragmented nature of the business. "It's not an address. It's not a property. It's just a loan number," he says. "So they'll push a button in San Francisco, and it will set things in motion to do things with [a] property that don't even make sense."

SPREADING THE PAIN

The proceedings in Pianka's and Nowak's courtrooms offer a sobering reminder that underlying the attenuated ownership and esoteric products spun out of mortgages are actual buildings, some with leaky roofs or broken porch railings. The industry denies responsibility for properties to which it has not taken title. "The notion that a mortgage company has an obligation to make repairs on a property that it doesn't even own is very hard to comprehend," says Marco Cercone, a Buffalo attorney who represents a range of lenders before Nowak in the courtroom. Cooper says that banks and other financial firms once extolled houses as the best possible collateral for a loan. Now they're stuck with that collateral, and they don't like it.

If there ever is a national response to the messy legacy left by foreclosures, it might include something like the Buffalo system, which seeks to take action before the presence of abandoned houses hurts entire neighborhoods and which spreads the pain among many players. "We're kind of a crystal ball into what might happen" elsewhere, Cooper says.

Lenders may rue the day the State University of New York at Buffalo admitted Cooper to pursue a PhD in sociology and a law degree. The subject of her doctoral thesis, submitted in December, 2006: the role of banks in residential abandonment w y ey s l - able for property-code violations. The fourth-generation Californian says she quickly became attached to Buffalo for its history and architecture. Now 33, Cooper and her husband are rehabilitating a house that she bought after getting an IRS tax lien removed from the property. "My passion for this work is because I love this town," she says.

While researching her thesis, Cooper interned for Judge Nowak. Tall, soft-spoken, and unfailingly courteous, the judge, 39, began holding Bank Day earlier this year and schedules it once a month. The civility of the proceedings and the large number of bank lawyers in attendance belie a noteworthy fact: They are there under coercion. A e ye g , a sa s, "th city became increasingly frustrated with the banks' role" in contributing to Buffalo's abandoned-property problem. (Estimates put the number of abandoned homes in the city at between 5,000 and 10,000.) In 2004, New York State amended the definition of "owner" in its property maintenance code to include not just titleholders but others who had "control" over a premises.

While the statute makes no reference to lenders, Nowak contends that the letters banks send to defaulting homeowners threatening to boot them from their houses show that they have begun to "assert some measure of control." On this premise, Nowak says, Buffalo began contacting banks "en masse" about foreclosed properties, but "a lot of times we'd just be rebuffed and ignored."

Cooper, as an intern, suggested a tactic that the judge adopted. When banks ignored summonses for code violations, Nowak began entering default judgments against them and imposing the maximum fine, which can reach $10,000 to $15,000. For a big bank, that's not much. The real pain comes because the fines give the city a lien that impedes the banks' ability to buy or sell other properties in the area. In addition, when lenders come to his court to get residents evicted from a particular property, Nowak refuses to grant the request until the bank addresses violations outstanding on other properties. Judge Pianka employs similar tactics in Cleveland. On Dec. 10, for example, he assessed a $50,000 fine against an absentee defendant, Mortgage Lenders Network USA, for 21 code violations at a home.

Even far from the Rust Belt, in places where empty houses retain significant value, the lending industry seems to have trouble preserving its collateral when homes are abandoned during foreclosure. In Chula Vista, a number of houses have been trashed by college students who have held parties in the vacant properties. In other cases, pillagers pull up in rental trucks to cart away cabinets, wood flooring, and fixtures stripped from the homes. But in October, an ordinance qu ing l de s to register and maintain houses that have been abandoned during foreclosure.

Compliance, says Chula Vista code enforcement manager Doug Leeper, has been spotty. "What I need them to do is keep the water on and keep the lawn green," he says, noting that the first sign of abandonment is often a yard that has turned brown and a pool that has gone murky green.

That slide into decrepitude is exactly what Cooper is trying to head off in Buffalo. In February, she joined the city's law department, where one of her duties is prosecuting banks. She and Nowak each say their main obj c ive is no col-

Nowak may fine lenders if foreclosed homes t ri rat

lecting fines but bringing banks to the table to try to find constructive solutions for dealing with abandoned property. That doesn't mean borrowers are off the hook. Cooper typically charges both borrowers and lenders, and Nowak may fine homeowners or sentence them to community service. "Can both be responsible?" asks Cooper. "Absolutely."

The approach in Buffalo is paying dividends. In a case on Dec. 17, attorney Cercone addressed the status of a house that had gone into foreclosure in 2006. Cercone was representing JPMorgan Chase and Ocwen Loan Servicing (which in turn were representatives of a securitized trust that had purchased the mortgage). Cercone submitted an affidavit showing that Ocwen, which had been cited for violations in December, 2006, had spent $30,000 to repair the property, including scraping lead paint from the entire house. In September, the affidavit notes, JP Morgan Chase sold the property at a loss of $19,500, not including the cost of repairs. "The bank in this case dealt with the property as well as could be done under the circumstances," Nowak said from the bench, and he agreed not to impose any fines.

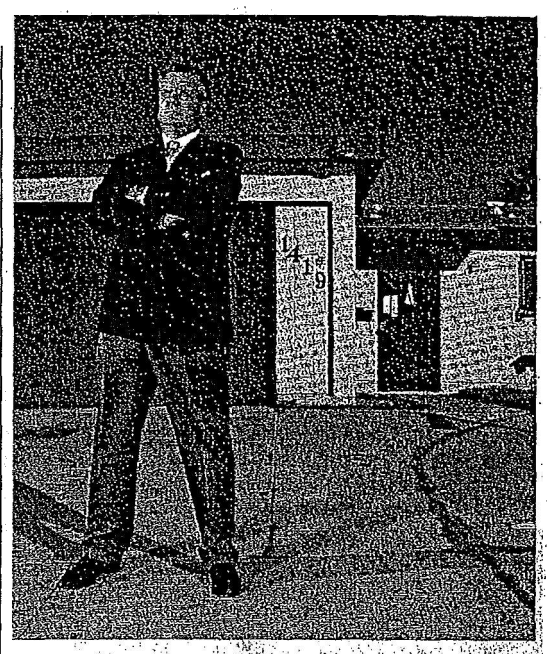
TORTUOUS TRAILS

Still, even with novel and aggressive tactics, the path to resolution for many properties in Buffalo can be tortuous and protracted. A house at 1941 Niagara St.—one o doze properties that Cooper examined as a graduate student—has yet to see its final chapter, though it may be close.

In 1998, Elizabeth M. Manuel obtained a $34,500 mortgage on the property from IMC Mortgage (since acquired by Citibank). By 2002, the loan had been sold into a securitization trust administered by Chase Manhattan (now JPMorgan Chase) as trustee. It also went into default, and Chase began foreclosure proceedings. In a court filing, Manuel (who could not be located for comment) said she left the home while the foreclosure action was pending. More than five years later, though, the title remains in her name. The house, although still standing (photo, page 48), has become a fire-gutted wreck.

In May 2007, Nowak issued a default judgment against Chase for $9,000. But these cases can be notoriously difficult to untangle. Thomas A. Kelly, a spokesman for the bank, notes that Chase sold its trustee business to the Bank of New York Mellon in October, 2006, and couldn't locate anyone at Chase able to comment. But he reiterates the industry view that Chase can't be held responsible for maintaining a property it never owned. He acknowledges that if a home didn't seem worth taking as collateral, the bank may have made a decision to "just walk away."

The value of 1941 Niagara, estimate city assessors, is $4,500, of which $4,300 represents the value of the land. The home, Cooper says, is slated for "imminent" demolition. (BW)



Vandalism is up in Chula Vista, Calif., says code enforcer Leeper

THE STORY OF AN ORPHANED HOME

How properties descend into legal limbo—and how communities are trying to deal with the problem.

1. ABANDONMENT
The borrower leaves the house. Sometimes this happens as soon as the lender sends a letter announcing that a mortgage has gone into default; sometimes it happens after the lender begins to foreclose.

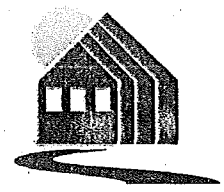
2. NEGLECT
The foreclosure process, which gives the bank the legal right to seize the house as collateral, can take 12 months or more. If the property is left unprotected, it can become a magnet for vandalism and decay.

3. OWNERSHIP LIMBO
The lender decides that the value of the loan, plus legal costs of foreclosure, back taxes, and repairs, exceeds the potential sale price. So the lender stops foreclosure efforts. The title remains in the name of the borrower.

4. PUBLIC NUISANCE
Housing inspectors finally crack down. Consulting property records, they cite the borrower for violations, which can lead to fines and even jail. But the borrower appears in court and says he thought the bank took the house.

5. RESOLUTION
Officials are expanding the definition of who owns a house. In Buffalo, prosecutors are hauling banks that abandon foreclosure proceedings into court and seeking stiff fines. If the house is unsalable, lenders may have to pay for demolition.

BRAD SWONETZ/REDUX; (BOTTOM) ILLUSTRATIONS BY ALBERTO MENJIVAR



CT FAIR HOUSING CENTER

STATEMENT OF ERIN KEMPLE FROM
THE CONNECTICUT FAIR HOUSING CENTER
IN SUPPORT OF S.B. 423

Thank you for giving me the opportunity to speak about the importance of passing S.B. 423, An Act Concerning Foreclosure Prevention And Responsible Lending. The Connecticut Fair Housing Center was also pleased to see all of the reforms and changes to mortgage lending origination that were proposed in H.B. 5577, the legislation authored by Co-Chairs Barry and Duff, and S.B. 21, the legislation proposed by the Department of Banking. The bills share many similarities and there is much that the Center supports. I would like to use my time today to highlight a few areas in which there are differences and to explain the need for all of the protections contained in S.B. 423.

The Connecticut Fair Housing Center is a state-wide organization that addresses housing discrimination and fair lending issues. Beginning in 2004, the Center began receiving calls from borrowers in danger of losing their homes because of loans they could not afford. Unfortunately, the Center was not able to assist many of these homeowners because the lending practices which made the loans unaffordable were legal under current law.

In an effort to prevent these abuses from continuing, the Connecticut Fair Housing Center has been working with national consumer advocates to create a bill which addresses many of the unethical and biased practices that now exist in the market but does not impact the majority of the institutional lending industry, which does business in an ethical and respectful manner. S.B. 423:

- ***Primarily regulates mortgage products that increase the risk of foreclosure*** such as sub-prime and non-traditional mortgages. Non-traditional mortgages, such as Option ARMS, are not regulated by H.B. 5577 or S.B. 21, which we believe could result in abuses in the future. According to the *Interagency Guidance on Nontraditional Mortgage Product Risks,* "More than traditional ARMs, mortgage products such as payment option ARMs and interest-only mortgages can carry a significant risk of payment shock and negative amortization that may not be fully understood by consumers." Major investment banks are predicting another wave of foreclosures when non-traditional mortgages begin their payment adjustments.

221 Main Street, Hartford, CT 06106
Phone (860) 247-4400 • Fax (860) 247-4236

Toll Free (888) 247 4401

900 Chapel Street, 10th Floor, New Haven, CT 06510-2865
Phone (203) 772-3247 • Fax (203) 562-7107

- ***Bans abusive practices*** such as churning (refinancing with no tangible net benefit to the borrower), lending when a borrower does not have the ability to repay, and encouraging default when refinancing. These bans on abusive practices are also contained in H.B. 5577 and S.B. 21.

- ***Prohibits lending without verification of the borrower's reasonable ability to repay the loan*** at the *fully indexed rate* and a *fully amortizing* payment schedule. Income must be verified by the best means of documentation available. This provision is especially important given the current foreclosure crisis. Too often borrowers were qualified for a mortgage based on a "teaser" or "introductory" rate. Once those rates expired, the interest rate increased making the loan unaffordable resulting in the foreclosure crisis we face today. S.B. 423 would require lenders to qualify a borrower, not based upon the teaser rate, but based upon fully indexed rate and a fully amortizing payment schdule thus ensuring that the borrower can afford the loan even after adjustments are made.

- ***Bans certain loan terms that greatly increase the incidence of default,*** such as prepayment penalties, balloon payments, negative amortization, and default interest rates. These loan terms are also banned in H.B. 5577 and S.B. 21 which we are very happy to see. These terms make it nearly impossible for borrowers with unaffordable loans to re-finance out of them. One borrower assisted by the Center has an adjustable rate mortgage with a two-year 5% pre-payment penalty. Until that penalty expires, he will be forced to make unaffordable payments each month and is at risk of losing his home.

If passed, the law proposed here today will protect Connecticut cities and towns from massive foreclosure rates in the future. The Center hopes to work that we can work with this Committee and the Department of Banking to ensure that we pass strong protections for Connecticut borrowers.