TESTIMONY OF

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“MORTGAGE LENDING DISPARITIES”

Before the

FINANCIAL SERVICES COMMITTEE

UNITED STATES HOUSE OF REPRESENTATIVES

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Roxbury Community College

Introduction

Good morning, Chairman Frank and distinguished members of the Committee. My name is Deval L. Patrick, and I serve as the Governor of the Commonwealth of Massachusetts. I want to thank the Chairman for conducting this important field hearing today in Roxbury, where, like so many other communities in Massachusetts and across the nation, families have been forced to leave their homes due to foreclosure.

Home ownership, like education, is a key to accessing and expanding opportunity in Massachusetts and in the United States. The ability of our citizens to build wealth and assets is vital to the stability of families and communities, and can be a promise to the next generation for a better life. For our economy, homeownership creates workforce potential and commercial activity around a stable base of resources, allowing for robust, sustainable growth.

Over the past 15 to 20 years, improvements in technology and delivery systems, automated underwriting, increased competition, securitization, the development of the subprime market, and an explosion in product types have resulted in a greater availability of mortgage credit than ever before. This has led to significant increases in homeownership rates throughout the United States, especially among African-American, Latino, and Asian populations.

We have seen these trends at work here in Massachusetts. In 1992, the Federal Reserve Bank of Boston issued findings on mortgage lending in the Greater Boston area. The study concluded that minority applicants, generally African American and Latino were denied credit more often than white applicants even when controlling for differences in borrower income and loan size.

Over time, strengthened home mortgage data disclosure requirements and enhanced efforts to use Federal and state CRA laws, especially in instances of merger activity, led to the development of more inclusive products to serve minority residents and residents of low and moderate income communities.

At the time of the 1992 study, traditional banks, covered by the Federal and State Community Reinvestment Act, accounted for 78% of the home mortgage loans made in the Commonwealth. By 2001, that number had dropped to approximately 26% of home mortgage loans. Mortgage companies, which are non-depository in nature and thus not covered by either Federal or State CRA laws, accounted for nearly 74% of such loans.

Unfortunately, these changes have held unintended consequences, most notably the growth in predatory lending practices. Specifically, the evolution of the subprime market and the securitization of subprime loans, especially loans with increased risk layering, helped create an environment of negligence in lending practices and increased borrower confusion. As the housing market began to turn, underwriting further weakened as lenders attempted to maintain origination volume.

Black and Latino borrowers throughout the state were much more likely to receive those subprime mortgages than were their white or Asian counterparts. According to data compiled and reported by the MCBC, in Greater Boston the subprime mortgage loan share was 57.1% for blacks and 58.3% for Latinos as compared to only 14.9% for whites. Similar patterns can be seen in the refinancing market. This pattern was present at state levels as well.

In the enthusiasm to promote homeownership in minority communities, many of the risks involved with these mortgage products were overlooked. In the short-term we were able to minimize the disparate treatment inherent in traditional lending. We have since learned, however, that over the long-term, these new market practices were practically unsustainable, and potentially more damaging to homeownership for minority and low-income communities. Advances in homeownership among our minority citizens are now at serious risk, and opportunities to break into the middle class have suddenly become perilous investments that could result in crippling debt and credit damage.

The link between disparate mortgage treatment and the foreclosure crisis that we are all forced to confront is clear and compelling. Many families facing foreclosure have been concentrated in particular neighborhoods throughout the commonwealth, and the resulting vacuum left in affected communities has driven up crime and fractured the economic stability of surrounding businesses. Furthermore, the impact on the social capital of communities is profound, as the community stability that results from home ownership has been dramatically compromised by this crisis.

Subprime lending can prove to be beneficial to consumers trying to access capital necessary to purchase a home. A variety of products and loan options increases the likelihood of finding a loan in any unique financial situation. Unfortunately, the pace of product innovation has exceeded the pace of consumer education and understanding, as well as industry oversight. Given the increasing complexity of various mortgage products, existing disclosure requirements may not provide the level of clarity necessary for consumers. Perhaps the greatest tragedy is the number of borrowers who would have qualified for prime financing, but were steered toward subprime loans. With home values dropping and subprime adjustable rate mortgages resetting upwards, these homeowners are being significantly challenged. This is something we should view with urgency.

Administration's Response

The impact of this growing challenge is a primary concern of my administration. Although the complex issues surrounding foreclosure and abuses within the mortgage lending industry are national in scope, there are important steps that can be taken at the state level to protect consumers while maintaining a viable, competitive mortgage lending industry in Massachusetts. I want to thank you for allowing me to share with you some initiatives we are undertaking to provide comprehensive short-term solutions to assist homeowners and develop long-term strategies to prevent foreclosure crises and address potential disparities in loan access and pricing.

In April of this year, I directed our Division of Banks to seek, on a case-by-case basis, brief stays for consumers facing foreclosure. The goal is to provide some time allowing the Division to refer homeowners to reputable homeownership counseling firms and encourage mortgage lenders and servicers to use this time to work with homeowners who are unable to make their mortgage payments. To date, through a hotline we established to help homeowners gain access to our services, the Division has fielded calls from nearly 1,100 Massachusetts residents either in the foreclosure process or having difficulty managing their mortgage obligations. Voluntary stays have been secured in nearly 500 cases.

MassHousing, in collaboration with Fannie Mae, has designed and implemented what arguably the most aggressive foreclosure prevention product in the country. The program includes a $250 million commitment with $190 million in funds from Fannie Mae and a $60 million contribution from MassHousing through the sale of bonds. No taxpayer funds will be used for the program. Through this program, borrowers may be up to 60 days delinquent with credit scores as low as 560 and still be able to refinance their existing mortgage loan under manageable terms.

Through our Division of Banks, Massachusetts will be one of the first states in the country to implement a nationwide database of mortgage professionals. Nearly four years in the making, the system will go live on January 1, 2008 to provide a uniform application process for mortgage lenders and brokers operating across state lines and will be a central repository of information about licensing and enforcement actions. The database will substantially improve the existing regulatory framework and reduce fraud on a nationwide basis.

I have also filed legislation which seeks to criminalize mortgage fraud, prohibit abusive foreclosure rescue schemes, and update various provisions of the laws that currently govern the foreclosure process. The bill also establishes a central repository of foreclosure information at the Division of Banks to allow us to track foreclosures by product, geographic region, and originator, broker, and lender. Furthermore, the legislation will prohibit a lender from making an adjustable rate subprime loan unless a consumer affirmatively opts-out of a fixed rate product and completes a homebuyer counseling program.

In addition, we also continue to support legislative initiatives to license mortgage loan originators and extend provisions of the Massachusetts Community Reinvestment Act to certain licensed mortgage lenders. The establishment of a CRA-like requirement for non-bank mortgage lenders will result in public evaluations and ratings summarizing non-bank lenders' performance in meeting housing credit needs and compliance with state and federal fair lending laws. I believe this increased level of scrutiny will significantly decrease impact disparities in mortgage pricing.

Finally, my staff and I have held ongoing meetings with lenders, industry trade groups, community and housing advocates and others to discuss possibilities to assist homeowners and housing counselors. It is clear that a comprehensive response to the complex problems of foreclosure and mortgage lending abuses will require the ongoing participation of mortgage lending industry members and other non-governmental entities. My staff will continue to work with all participants in the mortgage lending process to discuss and determine what further steps can be taken.

In an effort to expand on some of these initiatives, we will later this week announce six municipalities who will take part in a pilot program designed to cover a range of possible needs for homeowners. We have developed a 5 point plan to bring together government, lenders, homeowners, and non-rofits to develop and raise awareness about alternatives to foreclosure, create support systems for transition assistance where necessary, and keep neighborhood homes occupied. The 6 cities and towns will be selected based on number and concentration of foreclosures, as well as the overall fiscal needs of the region. Through that program we will be able to implement and refine strategies to help homeowners stay in their homes and keep communities stable.

To date, we have been fortunate to work in collaboration with the various concerned members of the Massachusetts Legislature, Attorney General Martha Coakley and Boston Mayor Thomas Menino. We are making a coordinated effort in Massachusetts, and look forward to working with federal authorities in any way that we can to keep people in their homes and put an end to the destabilization of families, communities, and our economy. I thank you for the opportunity to offer testimony today and would be pleased to answer any questions you may have.