

Statement for the Record

On Behalf of the

AMERICAN **BANKERS** ASSOCIATION

Before the

Subcommittee on Housing and Community Opportunity

Committee on Financial Services

United States House of Representatives



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April 16, 2008

The American Bankers Association is pleased to submit for the record this statement regarding H.R. 5679, the Foreclosure Prevention and Sound Mortgage Servicing Act of 2008, introduced by the Chairwoman of this subcommittee, Representative Maxine Waters (D-CA). ABA brings together banks of all sizes and charters into one association. ABA works to enhance the competitiveness of the nation's banking industry and strengthen America's economy and communities. Its members – the majority of which are banks with less than \$125 million in assets – represent over 95 percent of the industry's \$12.7 trillion in assets and employ over 2 million men and women.

We share Representative Waters's concerns about rising foreclosures and appreciate the desire to limit such actions wherever possible in order to preserve homeownership. Everyone suffers – lenders, investors and borrowers – when a foreclosure occurs. It is, therefore, in all our interests to find ways to avoid such an outcome. In fact, banks are actively engaged in voluntary loan modifications and other loss mitigation programs both on an individual basis and as part of broad industry efforts such as the HOPE NOW initiative.

While we all seek appropriate solutions for reducing foreclosures, and we commend Representative Waters for putting forward ideas for public consideration, we believe that the H.R. 5679 would create significant disruptions in the mortgages markets. It would replace the current efforts by banks to avoid foreclosure with a mandated set of requirements which would

detrimentally impact the safety and soundness of banks, raise privacy and litigation concerns, and ultimately increase loan costs for all borrowers. As a consequence, the ABA must oppose H.R. 5679.

There are three key points we make in this statement:

- H.R. 5679 would raise the cost of any new mortgage loan as it would undermine contract law, increase expected losses to lenders and investors, and lead to greater litigation.
- H.R. 5679 would raise serious safety and soundness issues because it shifts the risks associated with a change in the borrower's circumstances from the borrower to the lender well after the mortgage contract has been signed.
- H.R. 5679 raises both implementation and privacy issues as some notification requirements would be virtually impossible to meet and others could violate the borrower's privacy rights.

H.R. 5679 Would Increase the Cost of Any New Mortgage

H.R. 5679 would require that no foreclosure could be initiated against any federally-related mortgage without the lender or servicer first engaging in specified loss mitigation activities. The requirements of the legislation would apply to any foreclosure or attempted foreclosure occurring after the enactment of the legislation without regard to when the mortgage at issue was originated. This requirement has the potential to abrogate the current contract between the lender and borrower, as well as the contract between the lender and any investors in the loan. Placing new requirements on a lender or servicer not contemplated in the pricing or other terms of the original contracts will lead to safety and soundness concerns and would undermine contract law including raising constitutional issues relating to the right to contract.

This would destabilize our mortgage market system by putting the willingness of investors to purchase securities backed by mortgages at risk. If mortgage contracts can be altered after they are made, investors will be less willing to purchase them or investors will demand a higher rate of return to compensate for the additional uncertainty. This will make mortgages harder to obtain and/or more expensive for all borrowers.

Additionally, the bill prohibits foreclosure if "at any time" the lender or servicer fails to engage in loss mitigation. This requirement will lead to litigation over the adequacy of any

mitigation undertaken, which will in turn lead to further costs for all consumers as lenders and investors price the risk of litigation into future loans.

H.R. 5679 Would Raise Safety and Soundness Issues

A serious safety and soundness concern raised by the legislation is the provision relating to determination of loan affordability which gives a borrower the right to elect to use current income information rather than that provided at the time of loan origination. Again, this provision undermines the existing contract. If a borrower has had a decline in income, they can seek to have the loan terms changed through loss mitigation. The lender/servicer/investor would then bear the risk of any economic changes to the borrower. In addition to the safety and soundness concerns that arise when giving the borrower the ability to rewrite the terms of a mortgage contract, this provision is likely to drive investors from the marketplace, as there will be no certainty in a mortgage lending contract.

H.R. 5679 Raises Both Implementation and Privacy Issues

The legislation raises a number of privacy concerns. First, the bill requires that 60 to 120 days prior to any interest rate reset for any federally related mortgage loan with an adjustable rate, a notification to the borrower both in writing and via telephone. Existing laws limit which messages can be left on answering machines and with third parties. If a lender cannot reach a borrower by telephone (and is prohibited from leaving a message), they have failed to comply with this provision of the legislation. Second, it will be very difficult for a lender or servicer to determine 60 to 120 days in advance of an interest rate reset what rate will be applicable at the time of reset. The legislation requires only a “projection” based upon “prevailing rates” but the fact remains that lenders cannot control interest rates, and requiring this notice so far in advance will lead to information being provided to the consumer that is inexact at best, and alarmingly misleading at worst.

Another privacy concern relates to a provision in the legislation requiring a lender or servicer to notify a counseling agency when a loan becomes 60 days past due. While the legislation seems to contemplate the borrower choosing a counseling agency of their preference (at least for loans closed after the effective date of the bill), it does not specify that the borrower authorizes such counseling agency to receive communications about the delinquency status of any loans. Additionally, the legislation gives the borrower the ability to change which counseling agency they prefer at any time,

so the likelihood of a miscommunication to the wrong party is significant. For existing loans, it is unclear when or how a borrower would be required to specify a counseling agent of their choice. Certainly for borrowers who are making timely payments, any notification that they must choose a housing counselor who may be contacted should they fall past due on payments may be very unsettling.

Finally, we would note that there are a number of compliance burdens in the legislation which are either impossible to achieve and or which will significantly increase costs for lenders – costs which will inevitably be borne by consumers. These include a requirement that each account statement on a federally related mortgage loan include a telephone number of a person whom the borrower may contact for direct access to the information and authority to answer questions and fully resolve issues related to loss mitigation activities. It is unlikely that any institution will be able to provide direct access to a single person with such abilities. Loss mitigation tends to be a complicated process with many bank staff involved and levels of approval required for safety and soundness.

Another provision calls for monthly reports to the Secretary of the Treasury from each lender or servicer reporting on the extent and scope of loan loss activities. These are likely to be detailed, labor intensive descriptions of activities which may take months to resolve. It is unclear what benefit such detailed accounts will provide to the either the government or the public.

ABA appreciates this opportunity to comment on H.R. 5679. While we understand the motivation behind this legislation, and our members, in fact, engage in many of the loss mitigation activities it prescribes, we must oppose it. Making loans to eligible borrowers on terms that are fair and affordable is the essence of banking. When situations arise which lead to the need for loss mitigation, banks voluntarily take appropriate action. Mandating such activities inflexibly in the manner prescribed by H.R. 5679 would lead to instability in the mortgage markets, higher costs for all borrowers, and troubling privacy and litigation concerns for lenders and borrowers alike.