



The anti-mortgage lending act

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The Mortgage Reform and Anti-Predatory Lending Act was approved by the House Financial Services Committee last week and has been sent to the floor for a vote. This piece of legislation is intended to overhaul mortgage lending and legislate our way out of the subprime mortgage crisis. Unfortunately, like most actions taken in the immediate aftermath of a high-profile event, the bill should not become law. It is fraught with peril to the housing and credit markets, and it will not help low-income housing purchasers.

Take, for example, the "federal duty of care" that the bill imposes on mortgage lenders. Explaining what this duty amounts to will, without a doubt, require hundreds of pages of complex regulations that few lenders and their employees will understand -- but nevertheless be in jeopardy for failing to obey.

Lenders must, for example, determine what loan products are "appropriate" to the consumer's existing circumstances. Does that mean that the lender has to investigate whether the borrower is telling the truth?

What if the borrower fails to understand the questions the lender is asking? The lender must also "diligently" present the borrower with options. How will that be decided? At trial? What jury will find for the lender against the borrower?

The bill also creates a federal cause of action for the lenders' failure to comply with the law. This is just what the federal courts need -- mortgage foreclosure lawsuits added to their dockets.

Lenders must make "a reasonable and good faith determination based on verified and documented information" that the consumer had a reasonable ability to repay the loan. Who will be able to say what is reasonable or taken in good faith?

Would you like to make a loan if years later you can be called before a federal agency or a jury and cross-examined as to whether your actions were reasonable? Could some aggressive prosecutor one day attempt to make his or her career by going after a lender criminally?

The law wipes out a portion of the Uniform Commercial Code by negating the concept of a holder in due course. This feat is accomplished by permitting a borrower to sue the assignees of his loan -- including securitizers -- for rescission, that is, cancellation of the debt, and for repayment of the consumers' costs, if the loan violates, for example, the statute's minimum standards for reasonable ability to repay.

Thousands of loans are packaged and sold as part of Mortgage Backed Security pools. How long will housing mortgages continue to be part of these pools after Congress creates a due diligence standard that no securitizer will want to or be able to meet?

The pièce de résistance is that all of the bill's new standards and mandates will serve borrowers as a possible defense to foreclosure. And so we enter the brave new world, where no mortgage can

be foreclosed without a trial. But not for very long, as how many lenders will offer new mortgages with this threat in the background?

If this bill becomes law, lenders who do foreclose will have to take over the property subject to leases entered into prior to the foreclosure -- even if the lease was entered into without the lender's consent, at a significantly below-market rent, and for an indefinite term. In other words, this would permit financially troubled borrowers to stave off foreclosure by entering into uneconomic or long-term leases, which would preclude lenders from foreclosing because they could not sell the property at auction.

The bill will also make it more difficult for lenders to comply with the Community Reinvestment Act, which requires all lending institutions to make credit available in low-income neighborhoods. The Mortgage Reform and Anti-Predatory Lending Act is at war with this obligation -- as it will make it more difficult, and legally perilous, for lending institutions to make loans to people who might not be able to afford them. These are of course the very people supposed to be served by the CRA.

Although the Mortgage Reform and Anti-Predatory Lending Act may have been written with intentions that are good, its consequences are not. As the members of Congress consider this bill they might think about where the money comes from that is lent to home buyers. Tens of millions of Americans' savings and pensions are tied up in the millions of mortgage loans. If Congress makes it more difficult or even impossible for lenders to foreclose on defaulting loans, it is those people whose savings and pensions have provided the financing that will be hurt.

Capital, like water, seeks its own level. If the people who buy the securitized loans, and the institutions who invest in pools of mortgage loans, are no longer secure in being able to get their money back or the interest paid, they will find other investments, and countries, where they can.

This is hardly what the troubled housing and credit markets need.

Mr. Saft is a partner at the law firm of Dewey & LeBoeuf LLP. Would you like to make a loan if years later you can be called before a federal agency or a jury and cross-examined as to whether your actions were reasonable? Could some aggressive prosecutor one day attempt to make his or her career by going after a lender criminally? The law wipes out a portion of the Uniform Commercial Code by negating the concept of a holder in due course. This feat is accomplished by permitting a borrower to sue the assignees of his loan -- including securitizers -- for rescission, that is, cancellation of the debt, and for repayment of the consumers' costs, if the loan violates, for example, the statute's minimum standards for reasonable ability to repay. Thousands of loans are packaged and sold as part of Mortgage Backed Security pools. How long will housing mortgages continue to be part of these pools after Congress creates a due diligence standard that no securitizer will want to or be able to meet? The pièce de résistance is that all of the bill's new standards and mandates will serve borrowers as a possible defense to foreclosure. And so we enter the brave new world, where no mortgage can be foreclosed without a trial. But not for very long, as how many lenders will offer new mortgages with this threat in the background? If this bill becomes law, lenders who do foreclose will have to take over the property subject to leases entered into prior to the foreclosure -- even if the lease was entered into without the lender's consent, at a significantly below-market rent, and for an indefinite term. In other words, this would permit financially troubled borrowers to stave off foreclosure by entering into uneconomic or long-term leases, which would preclude lenders from foreclosing because they could not sell the property at auction. The bill will also make it more difficult for lenders to comply with the Community Reinvestment Act, which requires all lending institutions to make credit available in low-income neighborhoods. The Mortgage Reform and Anti-Predatory

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