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TESTIMONY OF MASSACHUSETTS ATTORNEY GENERAL
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U.S. HOUSE FINANCIAL SERVICES COMMITTEE

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Lenders and Servicers' Promises of Loan Modifications in Massachusetts are Not Matched by Meaningful Actions That Promote Sustainable Loans

I thank Chairman Frank and the Committee for allowing me the opportunity to submit testimony on this important issue of foreclosure mitigation efforts as it relates to the predatory lending crisis that has permeated our nation.

By way of background, I would like to provide a brief overview of our office's commitment to combating predatory lending and guarding against the impact of the foreclosure crisis. In Massachusetts, as in many parts of the country, we are experiencing a dramatic surge in home mortgage foreclosures, due in large measure to unsound and predatory lending practices. In fact many foreclosures have resulted from loan practices and products that were destined to fail because too many lenders departed from the bedrock lending principle that one should reasonably assess the borrower's ability to repay before lending money.

In response, our office has sought accountability through litigation, regulation and other advocacy. On the enforcement side, we have brought predatory lending cases against two major subprime lenders, Fremont Investment & Loan/Fremont General and H&R Block/Option One Mortgage Corporation. In the Fremont action, we obtained an



unprecedented injunction that restricts foreclosure on certain loans that were doomed to foreclosure because of the specific combination of ultra risky loan features used by Fremont. The injunction is one of the first pronouncements by a court that it is an unfair trade practice to sell mortgage loans that require borrowers to refinance while making such refinancing virtually impossible to obtain, at least absent a perpetual increase in home values. We have also brought enforcement actions against mortgage professionals who engaged in loan application fraud and other loan origination misconduct.

On the regulatory side, our office enacted regulations to prevent predatory lending and worked together with the Massachusetts Division of Banks for the enactment of legislation that provides additional protections for borrowers facing foreclosure. Our office issued new regulations, effective in January 2008, governing the mortgage brokers and mortgage lenders in Massachusetts. These regulations, 940 CMR 8.00, amended and expanded regulations first issued in 1992, and significantly extended the applicability of the regulations to purchase-money and refinance mortgage loans. These consumer protection regulations now address an array of unfair and deceptive practices in home lending that have contributed to the ongoing foreclosure crisis and harmed thousands of Massachusetts residents and their communities.

Our office also has joined other states to seek real progress from lenders and servicers on the issue of loan modifications. We have coordinated training efforts for attorneys willing to take pro bono case assignments to help homeowners avoid foreclosure. In addition, we have advocated for stringent federal regulation of mortgage lenders and brokers. We recognize that combating the current foreclosure crisis will require the resources and cooperation of federal, state and local authorities.

A critical aspect of our enforcement efforts, specifically in the Fremont case, has been the successful demand that lenders' loan origination misconduct—selling loans that were doomed to foreclosure and selling loans without assessing a borrower's ability to repay—must be taken into account before a foreclosure proceeds. In February 2008, we obtained a preliminary injunction that prevents Fremont or its assignees from foreclosing on certain risk-layered loans until our office has reviewed the loan, and if we object, Fremont must obtain the court's approval. I am pleased that other enforcement agencies—State Attorneys General and last week the Federal Trade Commission—have seen fit to follow this law enforcement approach to combating unfair and deceptive lending and servicing practices. In lieu of always resorting to litigation, we have tried to combat unnecessary foreclosures in Massachusetts by engaging lenders and urging them to “do the right thing”—to modify loans in order to staunch the public harms of foreclosures while still protecting their economic interests. Federal authorities have urged the same thing, in a very public way. Regrettably, this approach has not been successful. Indeed, the “voluntary” approach to loan modifications has failed. In Massachusetts, our office, Governor Deval Patrick, and the Legislature have focused on avoiding unnecessary foreclosures for more than a year. Based on our experience in Massachusetts—and we have no reason to believe we are unique—we have reached the following conclusions:

- Loan modifications are not being achieved in significant numbers. When compared to the number of foreclosures in process, far too few borrowers are able to restructure their loans to generate a sustainable loan; and
- When so-called loan modifications do occur, they often do not result in a sustainable loan. Lenders and servicers routinely offer and complete so-called loan modifications that increase monthly payments and increase overall debt. They do not meaningfully avoid foreclosure. At best, they

temporarily delay the inevitable delinquency and eventual foreclosure—they “kick the can down the road.”

Put simply, lenders, holders and servicers have not lived up to their very public promises of avoiding foreclosures by achieving loan modifications. As this Committee, and federal agencies, and state law enforcement continue to combat foreclosures and the unfair lending practices that caused this crisis, that reality should impact your decisions.

I would like to explain our office’s experience with respect to loan modifications as well as the specific bases for my conclusions.

Very early in my involvement in the subprime lending crisis, as our office was developing enforcement actions, we realized, like many others, that a vital part of combating foreclosures was to work with lenders to modify loans. Our office has explored wide scale loan modifications in the litigation we are conducting against predatory subprime lenders, with some success (discussed below). We also have been part of the States Foreclosure Prevention Working Group that has collected data from most of the nation’s top twenty subprime servicers and engaged them in discussions on implementing wide scale loan modifications. Iowa Attorney General Tom Miller, among others, has testified before this Committee on that group’s goals and findings. More recently, the Massachusetts legislature enacted a 90 day right to cure period, requiring that lenders provide 90 days of breathing room before foreclosure during which, hopefully, borrowers and servicers would explore ways to restructure a sustainable loan and avoid foreclosure. Together with Governor Deval Patrick and Banking Commissioner Steve Antonakes, on May 1, 2008 we urged lenders and servicers to use that 90 day period as a real opportunity for loan modifications, not simply a new procedural hurdle for foreclosing attorneys. We state officials used that initial 90 day

