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Unfair Lending Practices

Good morning, and thank you for the opportunity to present comments on the critical issue of unfair mortgage lending practices as we have witnessed them here in Chicago.

The Legal Assistance Foundation of Metropolitan Chicago is the largest provider of civil legal services to low-income residents of Chicago and Cook County. Our Home Ownership Preservation Project has been representing low-income homeowners for almost 15 years. Over those 15 years we have counseled tens of thousands of homeowners, and we have represented thousands of them in court.

Most of these homeowners have been victims of predatory lending, that is, some type of negligent or abusive subprime lending. Today the multitrillion-dollar subprime lending industry is dead, or at least it lies in ruins. And of course the implosion of the subprime market has had severe adverse effects on the larger financial markets, both here and abroad, and has played a major role in fueling the rising tide of foreclosures, depressed real estate values, and other related economic woes. Now, many thousands of homeowners face foreclosure not necessarily because they were victims of predatory lending, but often because they are simply victims of a larger economic crisis.

But as we continue to experience these wider patterns of economic strife, it is critical not to forget how it all began. It is critical to focus on the problem of unfair mortgage lending—predatory lending—irresponsible subprime lending—call it what you will—because this is where the crisis began. And it is critical to take steps now, and moving forward, to ensure that we do not face another similar cycle, by whatever name, five or ten or twenty years down the road.

The phenomenon of irresponsible and out-of-control subprime lending took off in the 1990's, and it skyrocketed in the 2000's, until its inevitable demise in 2007. I say "inevitable" because we advocates were seeing practices back in the late 1990's which we knew to be unsustainable. In the late 1990's and early 2000's we felt like lone voices in the wilderness telling stories of unaffordable loans being made to low-income homeowners, and foretelling an economic disaster in the making, but nobody was listening—at least, nobody with the power to regulate at the federal level. Why? Because, for a long time, too many people were making too much money, based on a system that was all about volume. The more lending the better. Period.

Let me share the story of one of our clients. This story focuses on a loan product that was at the heart of volume-based, irresponsible subprime lending. I am speaking of “stated income” loans, also known as “no doc” or “reduced doc” or “doc lite”—loans where brokers or loan officers could close loans simply by writing down a borrower income figure on a loan application, with no legitimate income verification required. These loans were known early in the industry by the name “liar loans.” Brokers and loan officers were literally invited to fraudulently misstate borrower income in order to make a loan look affordable on paper. Arguably, this single practice of intentionally loose underwriting did the most to fuel the subprime boom and bust.

Ms. Aikens was a 79-year-old African-American woman of diminished capacity. She was issued a loan based on a broker’s statement that she made \$7,000 *a month* acting as a “housekeeping supervisor.” In fact, Ms. Aikens earned \$7,000 *a year* doing part-time housekeeping for a neighbor. In this particular case the fraud was not solely on the broker, for the loan file contained a document showing that an employee of the lender called to verify Ms. Aikens’ employment—but, quite intentionally, the loan processor did not verify the *amount* of Ms. Aikens’ income. The lender in this case was Countrywide, once the highest-volume issuer of subprime loans in the country.

We were able to save Ms. Aikens’ home, and we have been able to save the homes of many low-income borrowers. In most of these cases we have challenged predatory lending practices such as inflated income, loan flipping, bait and switch, hidden interest rate increases, home improvement fraud, lack of meaningful disclosure of loan terms and fees, and the exploitation of non-English speakers, seniors, and the disabled.

But for every home we have saved, another 50 to 100 have been lost in Chicago alone. Not surprisingly, these homeowners are disproportionately minorities and seniors. Predatory lending was overwhelmingly targeted at minority neighborhoods. In these neighborhoods there existed—and still exists—an absence of responsible credit, due in large part to the historic practice of redlining. Capitalism abhors a vacuum. So, where responsible lending is absent, irresponsible credit floods in. In this case, subprime mortgage capital, fueled by a toxic combination of hyper-deregulation and hyper-securitization, flooded in.

What we all must do is make sure that irresponsible mortgage credit does not flood in again. I have shared Ms. Aikens’ story before. I was among those who testified at a Federal Reserve Board hearing held here in Chicago in 2006. The Fed was considering how it might amend the Truth in Lending Act to curb irresponsible subprime lending. I shared Ms. Aikens’ story, focusing on the phenomenon of liar loans. So did others, at other Fed hearings held in other cities. As a result the Fed passed a regulation in 2008 which significantly limited the use of stated income loans. A good result, but by 2008 the market it sought to regulate was already gone. Too little, too late. In the future, one hopes that the voices of our most vulnerable citizens and their advocates will be heeded sooner; that policy-makers and regulators will be proactive instead of reactive; that we will not face another financial crisis in which protected classes of citizens—minorities, seniors, the disabled—again bear the brunt of economic oppression and again serve as the harbingers of economic peril for us all.

Thank you.