

TESTIMONY OF NEW JERSEY INSTITUTE FOR SOCIAL JUSTICE

By Ken Zimmerman, Executive Director

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Re Proposed Amendments to the New Jersey Home Ownership Security Act  
Before Senate Commerce Committee

Thank you for the invitation to appear before this Committee to offer the New Jersey Institute for Social Justice (NJISJ)'s expertise and perspective on the proposed amendments to the New Jersey Home Ownership Security Act (NJ HOSA). For the reasons detailed below, we believe the proposed amendments are both unnecessary and harmful to New Jersey's citizens since the law is now working as will be demonstrated in the coming weeks when rumor about its effects gives way to reality about its operation.

NJISJ is an urban research and advocacy organization based in Newark, New Jersey, that focuses upon addressing systemic barriers that prevent urban residents and areas from reaching their full potential.<sup>1</sup> Predatory lending has been a focus of NJISJ's activities because of its devastating effect upon low-income, elderly, urban, and minority homeowners. Our activities have included significant research on the issue, including the detailed analysis I co-authored in conjunction with researchers at Rutgers University of Predatory Lending in New Jersey: The Rising Threat to Low-Income Homeowners (February 2002)(see [www.njisj.org](http://www.njisj.org)). Our work has been relied upon by a broad range of entities and institutions, as reflected in recent invitations to present at Fannie Mae's Fair Lending Conference and Governor McGreevey's Conference on Housing and Community Development, and the Appellate Division's reliance upon our submission as amicus curiae in the first appellate division nationwide that examined how predatory lending can violate civil rights laws. See *Associates v. Troup*, 343 N.J. Super. 254 (2001).

I have testified previously and at some length before this Committee during the extensive deliberation and amendment refinement amendment that led to the passage of the NJ HOSA. Rather than repeat that testimony, I want to make three points. First and most importantly, the law is working. The state Department of Banking and Insurance has made this clear, as have the most significant national financial institutions which have effectively endorsed the statute through their recent actions. Fannie Mae and Freddie Mac (the two institutions which purchase the vast majority of all mortgages made in this country) have recently announced that they will continue their existing policies with regard to New Jersey, purchasing all mortgages except for "high-cost" loans that they have never purchased as part of their anti-predatory lending policies and for the same reasons that led to NJ HOSA. Similarly, the three credit rating agencies (Standard & Poors, Fitch, and Moody's) have all stated that they will rate New Jersey mortgages with

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<sup>1</sup> Founded by Alan Lowenstein, NJISJ is chaired by former Attorney General Nicholas Katzenbach and includes among its officers the Honorable Dickinson Debevoise, Douglas Eakeley, and Ted Wells.

the exception of the marginal high-cost loans which, at best, are estimated to be no more than 5% of the existing mortgage market.<sup>2</sup>

Second, it is equally critical to note that there is no basis for the concerns that I have heard raised, such as the completely unfounded rumor that the law will make impossible cash-out refinancings in the state. On numerous occasions recently, I have been informed by members of the press, legislators, and others that they are being told that this law will lead to such outcomes. While I understand that there was some basis for concern before Standard & Poors issued its recent statement on November 25, there is absolutely no basis for that concern now. Unfortunately, there appears to be a widespread campaign to scare both consumers and members of the lending industry who understandably are not all in a position to independently review and assess the legislation and the guidance issued by the DOBI. There is no doubt that these concerns will dissipate once reality, rather than rumor, carries the day, as it will in the coming weeks.

Finally, the proposed amendments are, for the reasons discussed above, simply unnecessary at this point. More importantly, they will effectively gut the statute. In particular, the two proposed amendments related to the threshold for high-cost loans (exclusion of broker compensation and fees paid to unaffiliated third parties) will substantially undermine the statute by significantly expanding the number of high-cost (and presumptively abusive) loans that will be made to New Jersey borrowers without the protections afforded consumers by NJ HOSA. Further, these amendments raise the exceedingly troubling possibility that New Jersey law will now become weaker than the federal Home Ownership Equity Protection Act ("HOEPA"), leading to the possibility that this law will be preempted and leave consumers vulnerable to predatory lending practices.

To provide some additional background, the proposal to exempt mortgage broker fees until such fees exceed 5% of the total loan amount is simply an astonishing proposal that flies in the face of even the more limited, and largely ineffective federal law (HOEPA) and would eviscerate New Jersey's statute. As you know, NJ HOSA provides that a loan is considered high-cost only when certain fees and points add up to more than 5% of the total loan amount. Since the existing definition of points and fees excludes title insurance (typically the largest fee), escrow accounts, two bona fide discount points, and a number of other categories, the actual threshold for high-cost loans will frequently exceed 7 or 8%. This proposal would thus allow charges of more than 12 or 13% to be incurred

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<sup>2</sup>Based on data obtained by the federal government as part of the Home Mortgage Disclosure Act (HMDA), approximately 15% of New Jersey mortgage loans are made by subprime lenders. Lobbyists for subprime lenders state that 40% of subprime loans are affected by NJ HOSA, although no publicly available data has been provided in support of this claim. This would lead to the 5% figure. It is critical to note, however, that any legitimate loans that would fall within this category would be expected to still be made, most (if not all) at lower costs to the consumer. This is the case because, according to Fannie Mae or Freddie Mac, up to one-third to one-half of subprime borrowers actually qualify for conventional loans, and because the subprime market responds to regulation by shifting its practices and costs to just below whatever thresholds are imposed. See, for example, Federal Reserve Board analysis showing that subprime loans made just below high-cost loan thresholds. Memorandum to Board of Governors re Regulatory Analysis of Proposed Revisions to Regulation Z Concerning Predatory Lending Practices, November 28, 2001, 4.

without triggering the consumer protections associated with high cost loans. The federal law does no such thing, including direct broker compensation in its definition of points and fees.

Similarly, the proposal to exclude from the definition of points and fees those fees paid to third parties that are affiliated with the lender is equally troubling. The existing framework in which fees paid to unaffiliated entities are excluded, while fees paid to affiliated entities are included, is that used by HOEPA and thus is one that lending institutions are familiar with. This distinction makes considerable sense, given the risk of predatory abuses when a lender is using its own affiliates for appraisals and other services. These types of abuses, for example, have been associated with Household Finance, Inc., involved in the recent \$484 million settlement with the Federal Trade Commission. The state of New Jersey had the fourth greatest number of claimants against Household of any state in the country, and the Attorney General is currently distributing \$17 million to over 19,000 New Jerseyans.

For these and other reasons, the proposed amendments are both unnecessary and harmful to New Jersey's citizens. Thank you once again for your invitation to testify. I look forward to answering any questions you might have.