

New England Community Developments

Emerging Issues in Community Development and Consumer Affairs

Massachusetts Mortgage Summit Issues Recommendations

By Julia Reade

Massachusetts Commissioner of Banks Steven Antonakes convened a mortgage summit in November 2006 in response to rising foreclosures across the state and the nation, increasing evidence of mortgage fraud, and other developments in the mortgage market. The event brought together a wide range of stakeholders including representatives from government agencies and mortgage trade associations as well as community and consumer advocates. Attendees, including representatives of the Federal Reserve Bank of Boston, had the opportunity to share perspectives and to propose action steps.

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Immediately following the summit, the Massachusetts Division of Banks—the state agency responsible for overseeing mortgage lending—facilitated the establishment of two working groups to develop specific recommendations. One group looked at rules and enforcement; the second focused on consumer education and foreclosure assistance. In April 2007, the two working groups issued a final report, *Report of the Mortgage Summit Working Groups: Recom-*



mended Solutions to Prevent Foreclosures and to Ensure Massachusetts Consumers Maintain the Dream of Homeownership.

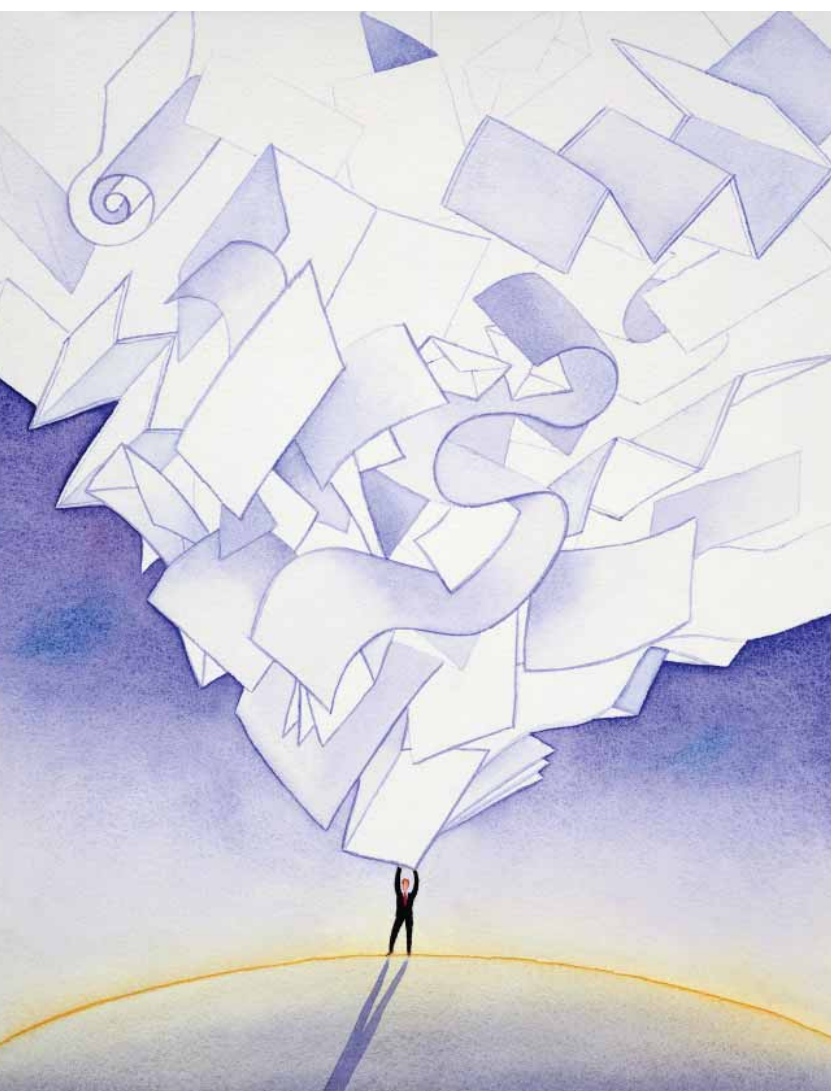
The Massachusetts Mortgage Summit and its working groups are an example of one state's response to the problem of rising foreclosures. The efforts helped organize a broad range of stakeholders, brought partici-

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pants up to speed on the newest information related to foreclosures, and produced a comprehensive list of recommendations. The convening can be considered a first step, and many Summit participants are actively working to implement the strategies laid out in the recommendations.

This article is a description of the problems in the Massachusetts mortgage market and the proposed solutions. For those who may be looking to promote a similar partnership, it provides a description of the collaborative process used in the Mortgage Summit and working groups. The recommendations presented illustrate a number of possible remedies to limit foreclosures and their impact on consumers and communities. We begin by providing some background on the foreclosure problem in Massachusetts. Next, we describe the process of collaboration among stakeholders participating in the Mortgage Summit working groups. Finally, we present the major recommendations of the working groups. Sidebars throughout the article identify where working group recommendations have since been implemented.



Background

In Massachusetts, problems with residential mortgages became obvious when housing price increases began to cool in 2006. Many borrowers had anticipated a continued rapid appreciation in residential real estate values but the market began to slow. For homeowners who were having trouble making their mortgage payments, the traditional remedies of selling their home or refinancing their loan offered no solution if the house was now worth less than the loan. When payments could not be made, foreclosures began to occur.

The multidimensional nature of the foreclosure problem posed a challenge to organizing a coordinated response. There was growing evidence that mortgage fraud and aggressive underwriting were exacerbating the situation. In addition, the mortgage market itself was now quite complex, reflecting changes including growth in lending by entities other than banks and thrifts, the increasing importance of brokers, and the expansion of the securitization process. Different types of mortgage lenders are subject to different sets of laws and regulated by different agencies. Depository institutions (such as banks and credit unions), their holding companies, and their subsidiaries are regulated by federal financial regulatory agencies.¹ Other entities making mortgages in Massachusetts, such as mortgage lenders and mortgage brokers, are regulated by the Division of Banks.

Collaboration

The Division of Banks believed that collaboration by a wide range of stakeholders would be the most effective means of addressing the complex problems surrounding the rise in foreclosures. Increasing their own regulatory enforcements would reduce fraud, but sweeping changes would require much broader support and a broader range of actors. As such, under the leadership of the Commissioner of Banks, the Division of Banks decided to convene the Mortgage Summit and facilitate the working groups.

Supportive Setting

Below are some of the factors that contributed to the fruitful collaborations of the working groups:

1. Strong leadership— The Mortgage Summit and working groups were initiated and facilitated by the Division of Banks, which has both strong credibility and convening powers.
2. Supportive setting— While initiated by the prior administration, the working groups had

the support of Governor Deval Patrick and his administration. Attorney General Martha Coakley and Boston Mayor Thomas Menino were also proponents. At the time, the City of Boston had already begun implementing its own emergency foreclosure prevention program.²

3. Members with diverse interests and resources— The Division of Banks welcomed a wide range of business, government, and not-for-profit organizations to participate in the working groups. Mortgage Summit attendees and working group members represented 15 different banks and credit unions, 14 community and consumer advocacy groups, 5 trade associations, and numerous state and federal agencies.
4. Kick-off meeting— The Division of Banks used the November 2006 Mortgage Summit to create momentum that was then leveraged in a series of quickly scheduled working group meetings.

Many times, members of the working groups had conflicting opinions over proposed recommendations. Most splits centered on a few core points. There were often strong reactions to recommendations that could unreasonably restrict access to credit or harm businesses making sound and fair lending decisions. After discussion and probing, however, committee members worked to find shared tenets, such as “too much access to credit has had negative effects” and “some degree of regulation is necessary.” Often groups continued to disagree on the appropriate levels of regulation necessary for a fair balance. Groups also frequently disagreed about how general or specific a regulation should be, but were able to define that regulations should be “specific enough to be enforceable, but broad enough to be effective.” Ultimately, participants agreed on a statement that expresses the overall theme of their discussions:

“As an overarching theme of the working groups, it was agreed that it should be a fundamental goal of all parties in a mortgage transaction that borrowers only obtain loans they can reasonably be expected to repay based on all information available at the time the loan is made and that all borrowers understand the terms of the loan.”

After receiving the working groups’ recommendations, staff from the Division of Banks drafted and published the *Report of the Mortgage Summit Working Groups*, and publicized it widely to state government,

businesses, and the public. The report contains the recommendations that received the strongest support in the working groups, and it describes a number of issues that were debated without resolution. Major recommendations that received significant support in the working groups are described below.

The Working Groups’ Recommendations

The two working groups focused their discussions on recommendations that could be implemented quickly, given that foreclosure rates were rising rapidly. While participants were frustrated with the lack of remedies available to consumers with imminent foreclosures, most agreed that it was easier to stop bad loans from being made than to try to fix them after the fact.

At the start of their discussions, the working groups decided to develop recommendations for seven issue areas:

1. Barriers to entry
2. Data and research
3. The foreclosure process
4. Legislative issues
5. Products and practices
6. Education and counseling, and
7. Foreclosure intervention products and services.

Working group members divided themselves into smaller subgroups to develop recommendations for each issue area and then brought their proposals back to the larger working groups for discussion and debate. Where possible, the working groups identified the specific entities that should enact the recommendations. However, the report explains that many of the recommendations would require concerted efforts by regulators, law enforcement officials, financial institutions, regulated entities, community and not-for-profit groups, as well as consumers themselves. The major recommendations of the working groups— those that would have the largest repercussions— are described below.

Make mortgage fraud a crime and increase the ability to prosecute.

The working groups recommend the criminalization of mortgage fraud with the associated penalties of imprisonment and sizable fines. Mortgage fraud is one of the fastest growing white collar crimes and can impact borrowers, communities, the lending industry, and the wider economy. Currently, persons

committing mortgage fraud face civil penalties for unfair or deceptive acts and can lose their business license. The working groups want mortgage fraud to become a criminal offense and recommend that the penalty for the crime be up to 10 years' imprisonment and/or a \$50,000 fine. In cases where multiple cases of fraud are committed, the recommendation is imprisonment for up to 20 years and fines of up to \$500,000.

Update:

On June 11, 2007, Governor Deval Patrick filed legislation to criminalize mortgage fraud. Penalties can include imprisonment for up to 5 years and fines of up to \$100,000. For cases of repeated fraud, punishment can include imprisonment for up to 15 years and fines of up to \$500,000.

The working groups also recommend clarification of the actions that constitute mortgage fraud. They recommend that any purposeful misrepresentation of facts related to the mortgage process be specifically designated as mortgage fraud – including exaggerating property appraisals, inflating borrower income, or lying about the terms of a mortgage. They add that any law should apply to any

party committing fraud, including mortgage lenders, mortgage brokers, appraisers, and the mortgage applicants.

The criminalization of mortgage fraud requires legislative action, although, in Massachusetts, emergency regulations can be passed by the Office of the Attorney General. If mortgage fraud becomes a criminal offense, the district attorneys and the Attorney General would have the authority to investigate and prosecute mortgage fraud cases.

Increase mortgage licensing requirements.

In their deliberations, the working groups participants expressed concern that individuals caught acting fraudulently need only move to a new state to pick up their practice again. As such, the working groups recommend several remedies to deal with “rogue” brokers and lenders. First, the working groups voice support for Massachusetts' participation in the development of a national mortgage licensing system coordinated by the Conference of State Bank Supervisors. The system would track individuals across state lines and identify any public enforcement action taken against a broker or lender. Second, the working groups recommend expanding licensing requirements to include all mortgage originators. Currently, in Massachusetts, only entities operating as a mortgage broker or mortgage lender are required to be licensed. There is

no licensing requirement for individual loan originators working for a mortgage lender or broker or for staff at federally regulated institutions. Licensing of all mortgage originators is currently required in over 20 other states.

Third, the working groups deem current capitalization and net worth requirements to be inadequate and recommend stricter requirements for licensing. For mortgage lenders, the current requirement is \$100,000 minimum net worth. But up to \$75,000 of this can be substituted by a surety bond so, in effect, the minimum net worth requirement is \$25,000. For mortgage brokers, licensing requires only a positive adjusted net worth. The call to increase net worth requirements is intended to ensure that mortgage lenders and mortgage brokers have a significant financial stake in their own companies. Increased bonding or surety requirements would not only increase the financial stake of companies, but would also potentially make more funds available to provide restitution to consumers who have been defrauded. In addition, the working groups unanimously support that licensing require a minimum industry experience of 5 years for mortgage lenders and 3 years for mortgage brokers.

Update:

On May 13, 2007, the Division of Banks issued proposed revisions to regulations on minimum experience requirements for licensing of mortgage lenders and mortgage brokers. The proposed revisions require 5 years' experience for the licensing of a mortgage lender and 3 years' for a mortgage broker.

On June 15, 2007, the Division of Banks issued proposed amendments to regulations on the licensing of mortgage lenders and mortgage brokers. The proposed amendments include a minimum net worth of \$200,000 and a surety bond of at least \$100,000 for mortgage lenders; for mortgage brokers, they recommend a net worth minimum of \$25,000 and a surety bond of \$75,000.

Increase revenues to build capacity at the Division of Banks.

The working groups recommend that the Division of Banks raise additional resources for its enforcement role by increasing the fees charged to mortgage lenders and mortgage brokers. These fees

have not changed since 1992, when licensing was implemented. At that time, the Division of Banks was responsible for licensing about 150 mortgage lenders and mortgage brokers. Currently, they license over 2,000. The working groups also believe that further funding increases are needed if the scope of responsibilities of the Division of Banks expands. Should any new regulations be passed, each would require some form of associated funding for enforcement.

Update:

On June 11, 2007, Governor Deval Patrick filed legislation that would enable the Division of Banks to access greater funding for enforcement.

Adopt federal guidance on certain mortgage loan products.

In October 2006, federal regulators issued guidance on nontraditional mortgage products, which include loans that do not fully amortize, such as interest-only loans and payment option ARMs. In January 2007, the Division of Banks adopted parallel guidance that could be applied to lenders that are not federally regulated. Federal regulators are currently developing guidance on hybrid ARM products, including 2/28 and 3/27 loans. The working groups recommend that once federal agencies have finalized the guidance, the Division of Banks again adopt parallel guidance that can be applied to licensees.

Change foreclosure laws.

The working groups also recommend changing laws to improve the rights of consumers in the foreclosure process. They recommend that lenders or their agents be required to submit a pre-foreclosure notification to both homeowners and the Division of Banks at least 90 days before filing a petition to foreclose. The recommended notification would include information about a wide range of parties involved in the mortgage, including the current mortgage holder and servicer, and the original lender and broker. It would also provide contact information for the lender or lender's agent so that consumers could attempt to cure the default or pursue a workout of the terms of the mortgage. If a home is sold at auction, the borrowers must be provided a full accounting of the sale, including information about money owed to them.

There was unanimous support among partici-

pants for giving consumers the right to cure a default- or catch up on late payments. In Massachusetts, a lender can foreclose on a home where the mortgage is in default even if the borrower is able to catch up on late payments. In addition, the working groups recommend that lenders not be allowed to accrue unreasonable fees against the borrower after the lender files the pre-foreclosure notification.

Create a database to track foreclosures at the Division of Banks.

The working groups participants agreed that lack of data about foreclosures is a significant problem. To address this, they recommend that the Division of Banks develop a database to track the information contained on each pre-foreclosure notification and foreclosure petition. The Division could use this information to analyze foreclosure trends in particular neighborhoods or communities, as well as to identify any mortgage lenders, brokers, or servicers who have unusually high incidences of foreclosures tied to their loans.

Limit foreclosure rescue schemes.

Massachusetts has seen a significant increase in two types of foreclosure rescue schemes. In the first scheme, "consultants" charge homeowners a significant fee to negotiate on their behalf with lenders to avoid foreclosure. Fraudulent consultants do little or no work on the foreclosure, often leaving the homeowner without enough time to pursue a legitimate workout. In the second scheme, homeowners are told that they can stay in their home by selling it to the "rescuer" who will rent the property back to



Update:

On June 11, 2007, Governor Deval Patrick filed legislation requiring pre-foreclosure notification to homeowners and the Division of Banks, and post-foreclosure accounting of costs and proceeds of the home sale.

On June 11, 2007, Governor Deval Patrick filed legislation requiring that the name and license number of the originating mortgage lender and mortgage broker be recorded on all mortgages when filed with a registry of deeds. The legislation also requires that the Division of Banks receive copies of all pre-foreclosure notifications and post-foreclosure accounts of sale, which will be entered and maintained in a foreclosure database.

them. Often, rents are far higher than the original mortgage payments, and in some cases consumers do not realize that they have given up the ownership rights of their property to someone else.

The working groups targeted these types of schemes by proposing legislation to limit the actions of consultants and property purchasers. Specifically, they recommend that transactions involving consultants be required to be in writing and that payment not be required until all services have been performed. For arrangements involving property purchasers, they recommend that the written contract be explicit about the fact that the consumer is selling their home and contain all terms of the sale. Property purchasers would also have to ascertain with a reasonable amount of confidence that the consumer can cover rent payments and can buy the home back in the future. For either type of foreclosure rescue program, the working groups recommend that the consumer have a 5-day grace period within which to cancel the contract.

Update:

On June 1, 2007, Attorney General Martha Coakley announced emergency regulations prohibiting unfair and deceptive foreclosure rescue schemes. Distressed property transfers are allowed only if they are not-for-profit, such as between family members or as arranged by a not-for-profit community or housing organization.

Raise consumer awareness and increase support.

As the working groups placed a strong emphasis on helping consumers avoid bad loans, they developed numerous recommendations about how best to increase consumer awareness about foreclosures and how to strengthen the impact of existing financial education resources. The working groups strongly supported both statewide and grassroots approaches to building consumer awareness campaigns and informing communities about the home ownership resources and local support networks available to them. They recommend that resources be focused on communities most affected by foreclosures and that awareness and education materials be written in the languages spoken in the local areas. The working groups' recommendations also stress the importance of making homeowner counseling by trained not-for-profit organizations available to local residents and encourage community-based not-for-profit

organizations to hold workshops that focus on the risks of unsuitable mortgages.

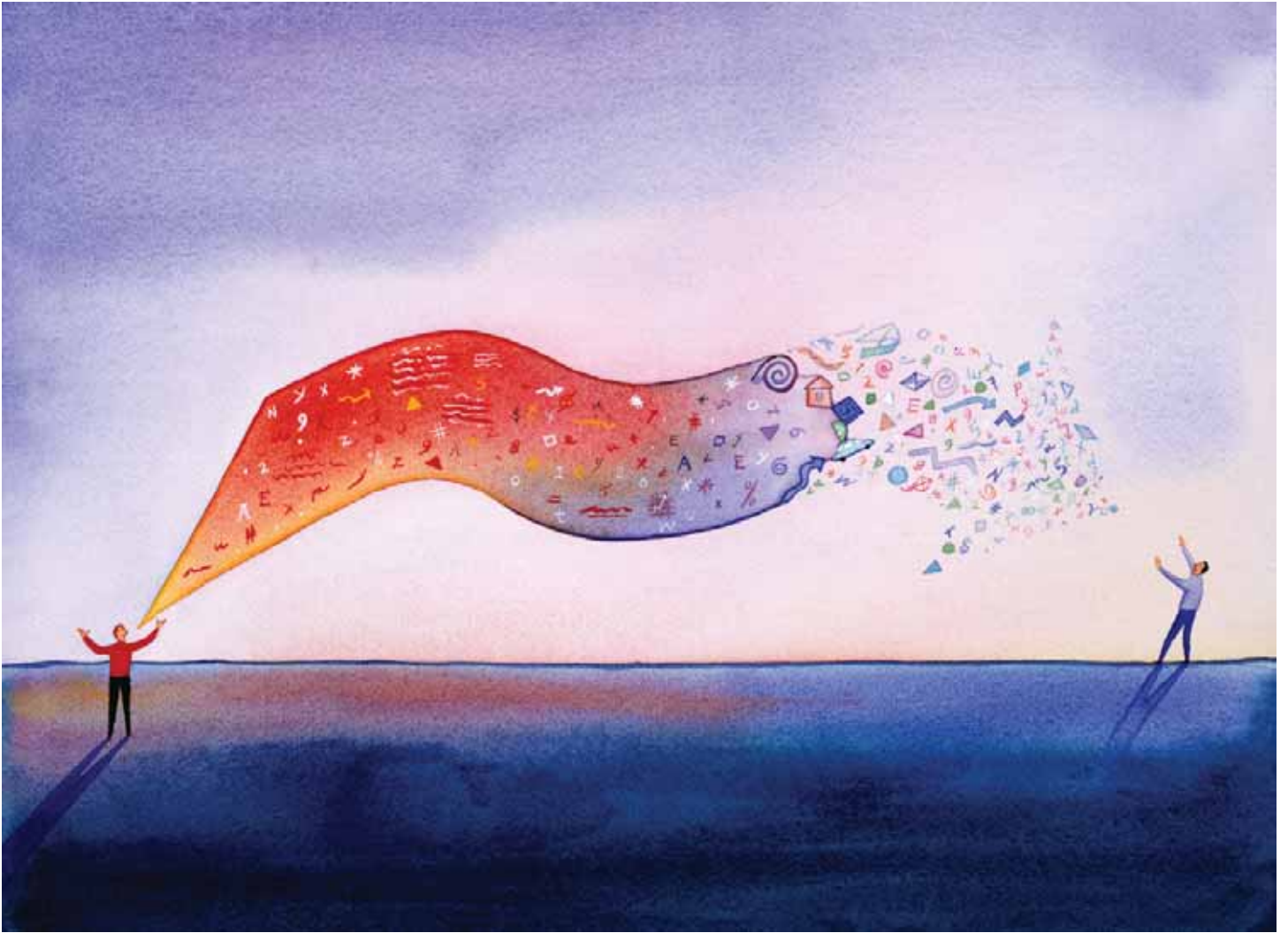
The working groups have several recommendations specifically for the state government related to consumer education. They suggest that the state create a home preservation fund that would be used to provide grants and loans to homeowners who are victims of mortgage fraud or predatory lending. The fund would also be used to support the work of not-for-profit agencies doing outreach, counseling, and refinance assistance. In addition, they suggest that the state should increase its own capacity for financial education and consumer support. Specifically, it should develop a strong financial education website, create a statewide directory of foreclosure counselors, and enhance the Division of Banks' mortgage hotline service.

Create foreclosure intervention products.

The working groups recommend the creation of specialized mortgage "rescue" products to help homeowners refinance out of unsustainable loans. There was a strong desire among the participants to keep homeowners in their homes because of the potentially destabilizing effect that a high number of foreclosures can have on a particular community. The foreclosure intervention mortgage would need to be designed for consumers that do not qualify for standard products because of poor credit, too-high loan-to-value ratios, or their inability to pay for closing costs. The working groups suggest that government sponsored enterprises such as the Federal Home Loan Banks provide credit enhancements and funding for these intervention products. Finally, the working groups emphasize the need for lenders that originated a high numbers of the loans experiencing difficulty to help create these intervention products.

Conclusion

Many parties are moving to implement the working groups' recommendations. Less than eight months after the initial Mortgage Summit, Governor Deval Patrick, Attorney General Martha Coakley, and the Division of Banks have all moved to enact various recommendations made by the working groups. Lenders and industry groups have formally endorsed many of the recommendations. And new collaborations have sprung out of the working groups' recommendations, such as a working group to develop a foreclosure intervention mortgage product.



The strength of the Mortgage Summit and its working groups emerged from the Division of Banks' ability to pull together the participation of over 75 people representing nearly 50 organizations and to get these participants to agree on executable recommendations. It helped that the participants were drawn from groups committed to reducing foreclosures and limiting their impact on Massachusetts homeowners and communities. The collaborative process that ensued enhanced the depth, breadth, and creativity of thinking that went into development of the recommendations, and the support of such a wide range of stakeholders has helped implementation progress rapidly. It is hoped that some of the lessons learned in Massachusetts will prove helpful to other communities building collaborations to address foreclosure problems in their local areas.

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Resources

Division of Banks Report of the Mortgage Summit Working Groups
<http://www.mass.gov/dob>

Governor Deval Patrick's Proposed Mortgage Fraud Legislation
<http://www.mass.gov>

Foreclosure Data Analysis for New England
<http://www.bos.frb.org/commdev/foreclosures>

Endnotes

¹ Federal regulators consist of the Federal Reserve, Federal Deposit Insurance Corporation, National Credit Union Administration, Office of the Comptroller of the Currency, and Office of Thrift Supervision.

² In October 2006, Boston Mayor Thomas Menino announced expansion of the city's foreclosure prevention program. New initiatives included a refinancing consortium consisting of "First Choice Lenders" that would try to help homeowners refinance into a more secure mortgage and a \$500,000 Boston Homeownership Preservation Fund to support foreclosure-prevention counseling and outreach.