



New York Bankers Association

STATEMENT OF
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BEFORE THE
NEW YORK STATE
SENATE BANKS COMMITTEE

MAY 12, 2008
ALBANY, NEW YORK

Good morning. My name is Michael P. Smith and I am President and CEO of the New York Bankers Association (NYBA). Thank you for the opportunity to address mortgage foreclosures and subprime lending practices in New York State on behalf of the more than 160 banks and thrift members of NYBA and their 300,000 employees across the State of New York. I am joined today by Mr. John M. Scarchilli, President and CEO of Pioneer Savings Bank, headquartered in Troy, New York. Mr Scarchilli is also the Chairman of NYBA. We will provide testimony on the impact of the Governor's Program Bill #44 (now introduced as A.10817(Towns)/ S.8143(Farley)).

Since the issue of predatory lending first came into public view about six years ago, NYBA has played a leading role in developing solutions to the problem, even though many of our banks do not make subprime loans, and, (according to a study by Warren Traiger, attached as Appendix A) less than 20% of the subprime loans, which have generated much of the recent concern, were originated by banks or their affiliates at all. Nevertheless, our members have consistently supported strong legislation which would establish meaningful and workable uniform national standards (which regrettably still have not been adopted) in the subprime market designed to eradicate predatory practices, while not creating unnecessary impediments to the dream of home-ownership, particularly for moderate- and low-income Americans.

NYBA respectfully submits, however, that S.8123, in its current form, would not achieve these goals. We believe, instead that the proposed legislation would create unnecessary new legal and regulatory challenges for the entire mortgage market, which would have the unintended consequence of limiting home lending credit to worthy New Yorkers. At a time when further impairments to marketplace liquidity could have a devastating impact on our State's economy, this is an outcome we should all work together to avoid.

With the current headlines about foreclosures, it may seem like progress has been slow, but despite this year's increase in the numbers of homes in New York in foreclosure, we remain in a far stronger position than many other states in combating predatory lending and reducing foreclosures. And that, we believe, is due to the foresight of our State's leaders and our State Senate's sensitivity to the importance of maintaining for its citizens access to appropriate credit through a vibrant banking system. Maintaining a public dialogue like this is one way to continue that progress – and we applaud you for continuing to focus on this important issue. It is in this spirit that we now highlight a few of the most troublesome provisions contained in S.8123.

The bill, for example, establishes a brand new category of loans, defined as “non-conventional loans”, which would be subject to new restrictions, prohibitions, and liabilities which are nearly identical in most respects to

those imposed today on those already defined as “high cost home loans.” Most lenders today do not offer “high cost” home loans because of the added restrictions and potentially onerous legal liabilities which can be created for them and their assignees. We therefore believe that many reputable and highly regulated financial institutions may choose to exit the “non-conventional” lending market rather than face increased loan initiation and compliance costs, uncertain legal risks, and harm to reputation. This will have the unintended effect of making it significantly more difficult for worthy borrowers with less than perfect credit to get home loans in the future from traditional, highly regulated financial institutions. These could include New Yorkers who have had credit trouble in the past but who have worked hard to overcome those obstacles in order to repair their credit records so that they could one day buy a home or send their children to college. At a time when recent surveys show that the housing markets in upstate areas such as Buffalo, Syracuse and Rochester are starting to bounce back, this could be a death blow.

We are particularly concerned about the impact of this proposal, should the current definitional thresholds for non-traditional loans set forth in the bill (loans whose annual percentage rate at consummation exceed by more than 3% the yield on treasury securities with a comparable maturity period for a first lien loan, or 5% for a subordinate lien loan) become law. Currently, the 10 year Treasury rate is 3.89%. The proposed threshold, we believe, is an

inappropriately low threshold to be fixed by statute - particularly when consideration is given to the vagaries of market conditions, such as the inverted yield curve we experienced in the recent past, as well as the wide swings we have recently seen in interest rates. In fact, we have been told anecdotally by a number of bankers, that given the recent dramatic cuts in interest rates by the Federal Reserve and the current threshold in the bill for non-traditional loans, most if not all of the prime loans that were “locked-in” in November 2007, for example, would, if closed, in the current rate environment, be deemed to be “non-conventional.”

Thus, we respectfully suggest that any definitional threshold for deeming a loan to be “non-traditional” not be lower than 5% above the yield on treasury securities with a comparable maturity period for a first lien loan, or 7% for a subordinate lien. I would note, on this point, that Virginia adopted the 5% standard as an appropriate threshold in its high-risk mortgage legislation enacted in April 2008, when according to RealtyTrac data, a nationally recognized foreclosure data provider, it ranks 15th in the nation in number of foreclosures. It would seem wholly inappropriate to impose a significantly lower threshold in New York, which has weathered the current mortgage crisis significantly better (consistently ranking 30th in the nation). We also suggest that loan originators be given an additional alternative measuring threshold, which, we believe, may be more reflective of actual current mortgage rates – specifically, a threshold of 3% above the Federal Reserve

H.15 rate (currently at 6.06% for a 30 year conventional mortgage) for a first lien loan, and 5% above the H.15 rate for subordinate lien loans.

The bill also would apply an ability to repay standard to all home loans. As the determination of a borrower's ability to repay varies from lender to lender, and even from program to program, fixed statutory requirements and presumptions such as those set forth in the proposal, may undermine the successful loan underwriting guidelines implemented by many financial institutions today. Additionally, this mandate might have the unintended consequence of deterring lenders from extending home loans in New York. This is so, not only because of the scope of the mandate, but also because the proposal's liability provisions will undoubtedly result in courts' second-guessing lenders' decisions in many foreclosure actions. This in turn will substantially increase lenders' risks and costs. Should an ability to repay standard nevertheless be deemed essential for all home loans, we suggest that it be made applicable only pursuant to a "pattern and practice" standard. Such a standard - which would shift the focus from a transactions-specific analysis, into a "practices" analysis - would be effective in keeping predatory lenders from engaging in widespread abusive practices while protecting lenders from inappropriate lawsuits for isolated small errors or technical mistakes.

We further believe that any final “ability to repay” requirement permit each lender to use its own underwriting guidelines to make such determinations. This would be consistent with the way this issue has been addressed in several other states. For example, in North Carolina the law explicitly allows the lender to utilize “reasonable commercially recognized underwriting standards and methodologies” to analyze a borrower’s ability to repay. Such a standard would recognize – as California has also done – that a method of addressing the ability to repay that “allows lenders to exercise reasonable discretion in conjunction with a list of specific factors that must be considered, is far preferable to a rigid, one size fits all model of credit granting, that will definitely deny credit to many qualified borrowers.” In this regard, it should be noted that, among other things, the “ability to repay” provision would establish a 50% debt-to-income standard, as a benchmark as to when a loan can be assumed to have been made with due regard to the borrower’s ability to repay. Yet, such a presumption could deprive many creditworthy New Yorkers – who live in a state where real estate values are extremely high – of the privilege of home ownership.

The bill also would now require lenders and loan servicers to send a notice to defaulting borrowers at least 60 days before commencing a legal action against the borrower. The bill would further require a court, in a residential foreclosure action, to schedule a settlement conference within 60 days of when the defendant must answer or move. As New York’s judicial

foreclosure process is already among the longest in the nation, we believe that the bill's additional notice requirements and further mandated delays are not only unnecessary, but will significantly impair the efficient processes that have already been developed and are being utilized today in New York to assist troubled borrowers, including the many described earlier in this testimony.

We are also concerned that the additional delay in the foreclosure processes mandated in this bill would have several more unintended consequences.

First, during this extended timeframe, lenders may be forced to pay insurance and taxes on the property, further eroding borrower equity.

Additionally, the further delays can result in unnecessary deterioration of individual properties, and even entire neighborhoods. Third, the extended mortgage foreclosure process can have a significant impact on a financial institution's capital requirements and rankings. This is so, because, under risk-based capital rules, loans that are 90 days or more past due are subject to a 100 percent risk weighting (as compared to loans that are current or below 90 days delinquent, which carry a 50 percent risk weighting). Indeed, we have been told anecdotally, that should the already lengthy mortgage foreclosure process in New York be extended further, it is likely that a bank regulator would require that loan to be written off in its entirety, in which event there would be less, rather than more, incentive for a bank to effectuate a workout. For all these reasons, we are also obviously strongly

opposed to the Assembly passed one-year foreclosure moratorium bill (A.9695-B(Brennan)/S.6724-B(Padavan)).

The provisions of the bill mandating settlement conferences also may have unintended consequences, resulting in reduced access to mortgage credit in New York. It is unclear what this conference requirement entails, and what level of discretion would vest in the presiding judge to modify the terms of the existing mortgage documents - something that runs in contravention to basic Constitutional principles that reject interfering with or impairing the provisions of contracts. In that event, unpredictable new quantities of risk will be injected into the mortgage lending process, resulting in increased financing costs to all New York consumers.

Despite our many concerns with S.8123, NYBA remains committed to working with you to eradicate predatory lending. Even before New York State's comprehensive anti-predatory lending legislation -- one of the toughest such laws in the nation -- was signed into law in 2002, New York's bankers were quick to act on the problem. In 2001, our Association developed "Best Practices for High Cost Home Lending," that includes much of what is contained in this bill. In 2006, the New York State Legislature passed the Home Equity Theft Prevention Act -- another effective measure which NYBA did not oppose, which goes a long way toward protecting a homeowners' equity when facing foreclosure. And another recent law,

requiring mortgage loan originators working for bankers and brokers to register and attain continuing education credits, will further help protect consumers from predators in the marketplace.

New York's tough high cost home lending law is one reason that our State has not suffered the rates of foreclosure of many other States. Chief among the law's protective provisions are prohibitions against, among other things, balloon payments within the first 15 years of the loan, loan flipping, and negative amortization. The law also prohibits lending without a due regard to the borrower's ability to repay, and prohibits lending without the borrower first receiving a comprehensive counseling disclosure, as well as a list of counselors to consult before committing to a loan. Importantly, too, the law - which is enforceable by the Attorney General - also provides a private right of action for borrowers and provides that on a finding of an intentional violation by the lender, the loan will be rendered void. Thus, many of the egregious practices we have heard so much about in recent months relating to high cost home loans, are already prohibited under New York law.

Therefore, since New York, as well as many other states, has already acted in this area, we urge that any new legislative initiatives embrace the best features of existing state solutions but not erect additional unnecessary barriers to the mortgage origination and credit process which will impede the

ability of banks and thrifts to meet the credit needs of the communities they serve, including the important low- and moderate-income segments.

The increase in foreclosures in New York State – although undoubtedly a cause for concern - is far below the national average, and lower than most other states, with New York consistently ranking 30th according to RealtyTrac. One of the reasons for the difference in the State's performance is that New York City has performed very well relative to other large metropolitan areas. In fact, its foreclosure rate in April, 2008 was the lowest of any of the five largest cities in the U.S., and less than half of the national average, according to RealtyTrac. Moreover, in April 2008, more than 70% of the foreclosure filings in New York State were Lis Pendens, which is only the first filing in a foreclosure process that is the longest in the country and can take up to eighteen months – providing ample time for borrowers and lenders to effect a meaningful work-out when at all possible.

Nevertheless, in response to the recent increase in foreclosures in New York and nationwide, many banks have been aggressively reaching out to help. Several of our largest member banks have established refinancing and grant programs in the billions of dollars to help keep troubled borrowers in their homes (See Appendix B.) Additionally, many NYBA members are currently following a strict multipart strategy to reach out to distressed borrowers,

known as the HOPE NOW Alliance, which, to date, has helped approximately 1.2 million homeowners nationwide to stay in their homes. In addition to their many internal work out programs, New York's banking industry and the non-profit groups it supports have also, for many years, had in place a strong and wide-ranging support system to assist troubled borrowers in every state. Programs such as Operation Hope, Neighborhood Housing Services, NeighborWorks, PACE Program, and the Long Island Housing Coalition have long worked in coordination with financial institutions, to offer foreclosure prevention counseling. There is also a network of HUD-certified counselors across the State of New York who stand ready to help borrowers in distress. In 2007, NYBA joined forces with New York's multi-agency Halt Abusive Lending Transactions (HALT) Task Force, and was an active participant in HALT's first New York City event. And in March, 2008 the State of New York Mortgage Agency (SONYMA), announced receipt of an almost \$750,000 Federal grant, as well as an almost \$125,000 supplemental matching grant of its own, to expand foreclosure prevention counseling efforts across New York State. All of this is in addition to the assistance that banks themselves can provide when a borrower is having difficulty. Foreclosure is a last resort for the lender and lenders will go to great lengths to avoid it.

Six years ago, when Congress and the State Legislature began to focus on this issue, NYBA set out to learn more about how the predators operate in

our neighborhoods, and why many consumers become victims. We developed a pilot program with bank mortgage specialists and neighborhood churches. We learned much about the tactics that drive borrowers away from legitimate lenders and toward abusive lenders. In response to what we learned, the banking industry stepped up its activity in two areas: education and access.

Financial education, or financial literacy, is not only the best defense against the predators, it is the best offense for consumers who want a financially secure future. A borrower must have basic knowledge about the mortgage process to navigate such a complex transaction. Financial education resources are plentiful in our communities. Not only do banks and thrifts hold home-buying seminars in their communities, they also provide significant funding for consumer groups and community advocates to help educate borrowers, and many even help borrowers in distress to stave off disaster through loans and grants.

The New York Bankers Association supports a number of financial education programs for all age levels. Notably, our national partner, Operation Hope, recently dedicated a Hope Center in Harlem. The mission of Operation Hope, and organizations like it, is financial empowerment through in-school curricula for children and young adults, as well as workshops, budget and credit counseling, and mortgage and small business lending counseling for

adult consumers. Resources like this are making a difference and will help loosen the grip of the predators on our neighborhoods.

Regarding access, banks in New York are expanding into more and more neighborhoods every day. This has been good for competition and ultimately good for consumers because it means more choices and better alternatives to what the predators are offering. We support the State's Banking District Development program, which has been instrumental in encouraging banks to set up shop in new neighborhoods. Other states are now looking at New York's Banking District Development Program as a model for their laws and regulations.

The banking industry is committed to the cause of eradicating abusive loans and their devastating impact on families and communities in New York. As a result, we have consistently supported strong legislation which would contain the following key elements: (i) include uniform standards for the mortgage brokerage, lending and underwriting process; (ii) not target for further regulation the prime mortgage market, which has been an engine of the national economy - especially since the banking and thrift organizations which serve this market are already heavily regulated; and (iii) not effectively eradicate the subprime market, which plays an important and meaningful role for many New Yorkers in achieving the American dream of home ownership.

Unfortunately, as stated earlier, we believe that S.8134, as currently drafted, does not meet these objectives. We urge, instead, that all concerned parties continue their efforts to work toward a final bill which limits its focus to the subprime market, regulates those firms not currently subject to the rigorous array of state and federal regulations to which banking institutions must adhere, in a manner consistent with those institutions, and avoids undermining consumer access to appropriate credit. In the interim, NYBA's members will continue to (i) support strong enforcement of current laws; (ii) commit resources to financial education for consumers of all ages and means; and (iii) increase access to banking services and legitimate loan products. We have much work to do, but we have made a great start here in New York. We remain committed to being a partner in the solution to this problem.

Thank you.