



# Update: Legal Issues in Mortgage Technology

May 1, 2008



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# Perception IS Reality: How Compliant Do You Have To Be?



## Predatory Lending: What Does Wall Street Have to Do with It?

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In the United States, owning one's home is at the core of the American Dream. Owning means investing for the long term and an end to rent payments. It also means painting a wall bright purple without needing to answer to anyone, except perhaps one's spouse.

Unfortunately for millions of Americans in the past few years, home ownership has also meant doing business with Countrywide Financial Corporation.

Misleadingly wooed by Countrywide's too-good-to-be-true financing schemes, thousands are now defaulting on their home mortgage loans. This mortgage meltdown has spurred what could become the largest home foreclosure crisis in U.S. history, leaving Countrywide's shareholders and thousands of lower-income and minority customers holding the bag.

Meanwhile, Countrywide executives raked in millions, having sheltered themselves from their corporation's collapse.

**Predatory lending and greed at the top**  
Countrywide Financial Corp., was founded in 1969 and is based in Calabasas, California. The nation's number one mortgage lender, Countrywide services about 17 percent of all mortgages in the U.S.[1]

SEC filings show that CEO Angelo R. Mozilo made a cool \$13 million in a single month last summer as Countrywide's financial situation worsened.[2] Mozilo reaped about \$150 million during 2007 by exercising his stock options and selling off his own Countrywide shares.[3]

The Center for Responsible Lending (CRL) has exhaustively catalogued Countrywide's pillaging of its customers and shareholders. CRL reports the following abuses:

**Predatory lending.** Borrowers and regulators have accused the company of bait-and-switch sales tactics, fraud, racial discrimination, fee-gouging and elder abuse.

**Dangerous products.** Countrywide has been a leader in pushing unsound products, such as adjustable rate mortgages, to borrowers.

The New York Times

## If Everyone's Finger-Pointing, Who's to Blame?



who is to blame for the losses paining Wall

The answer, it seems, is someone else.

A wave of lawsuits is beginning to wash over the troubled mortgage market and the rest of the financial world. Homeowners are suing mortgage lenders. Mortgage lenders are suing Wall Street

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One of many recent home foreclosures. REUTERS/Mark Avery

## THE WALL STREET JOURNAL

OPINION

### The Anti-Mortgage Lending Act

By STUART M. SAFT  
November 10, 2007

The Mortgage Reform and Anti-Predatory Lending Act was approved by the House Financial Services Committee last week and has been sent to the floor for a vote. This piece of legislation is intended to overhaul mortgage lending

ark Times

## Who is to Speak for Borrowers in Trouble

By Mark  
July 17, 2008

Through her client's mortgage papers, the housing loan shark shook her head.

The numbers and interest rates and payment schedules formed such a familiar, dispiriting picture. The 32-year-old man who was sitting across the desk from her said he had been taken out an adjustable rate mortgage called an option ARM. He bought his home, the first he has owned. The terms of the loan put him in the line of millions of people dragged under by the mortgage crisis that has washed across the country.



## Congress to grill Mozilo, O'Neal, Prince over pay

High-profile execs head to Capitol Hill to defend pay packages amid mortgage crisis.

By David Ellis, CNNMoney.com staff writer  
Last Updated: March 7, 2008: 9:15 AM EST

NEW YORK (CNNMoney.com) -- Two high-profile former Wall Street CEOs and the head of the nation's largest home lender will testify Friday before a congressional committee examining the link between executive pay and the mortgage crisis.

A total of 10 witnesses are due to appear before the House Committee on Oversight and Government Reform, including Countrywide Financial's (CFC, Fortune 500) founder and CEO Angelo Mozilo, former Merrill Lynch (MER, Fortune 500) Chairman and CEO Stanley O'Neal and ex-Citigroup (C, Fortune 500) chief Charles Prince.

The hearing was originally scheduled for Feb. 7, but was postponed due to scheduling conflicts.



Lawmakers will be taking a close look at how the compensation and severance packages of Mozilo, O'Neal and Prince were set and approved.

### Casualties of the mortgage mess

## The New York Times

### Foreclosure crisis 'still deepening'

Today on... indicating the... to grow in

reports... ure crisis is... d... a record... default issued... e of 14% from... ough not all... closure, the... to a record flood of foreclosures hitting the market later this year.



## Predatory Lending Sucks

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## WELCOME TO

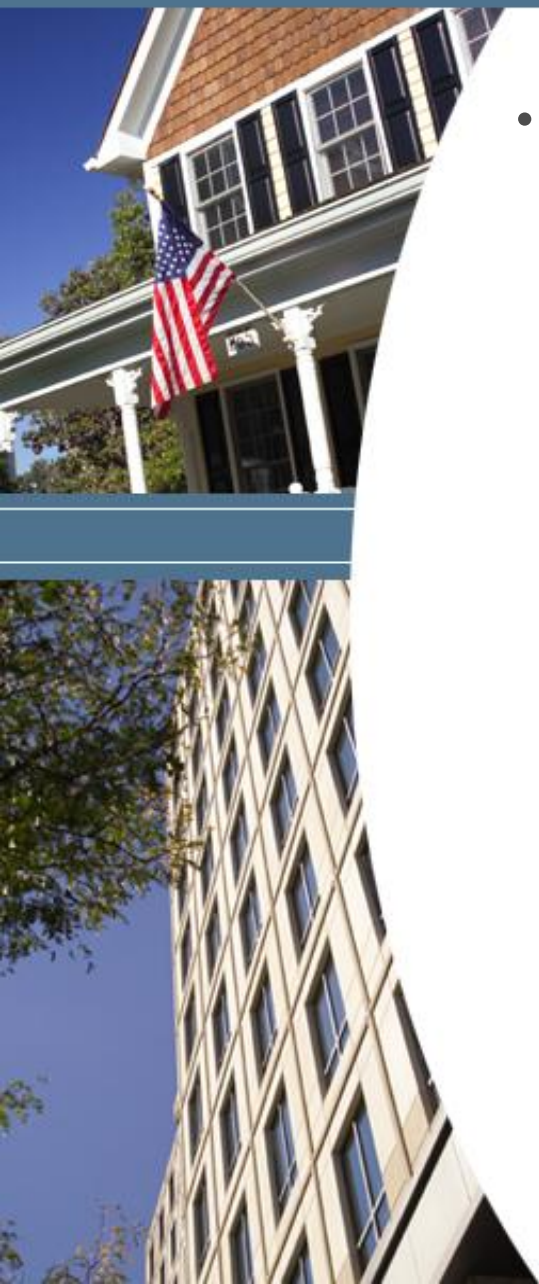
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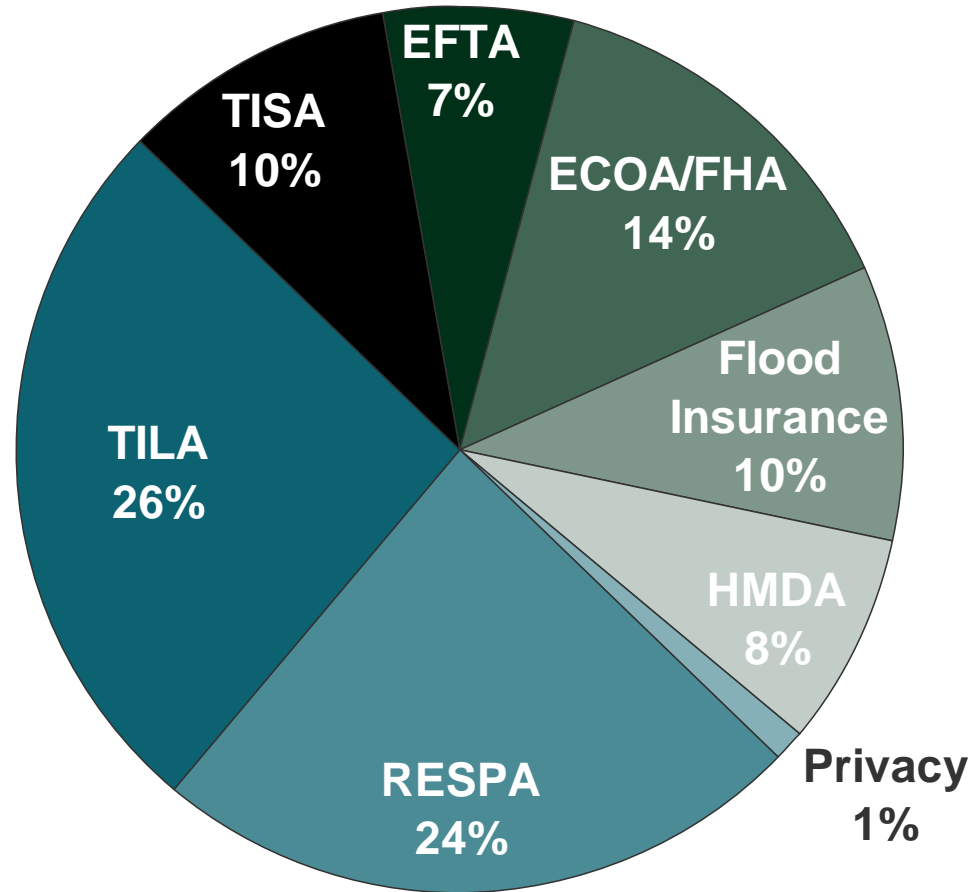


Don't get devoured. Get your FREE report on the Top 10 ways mortgage beasts try to take your home.



- FDIC's Office of Inspector General report regarding compliance with 8 federal consumer protection laws during the 2005 audit cycle
  - » 83% of the institutions examined were cited for "significant" compliance violations
  - » 43% of those institutions were "repeat" offenders
  - » 85% of those repeat offenders were highly rated by the FDIC for their in-place compliance processes

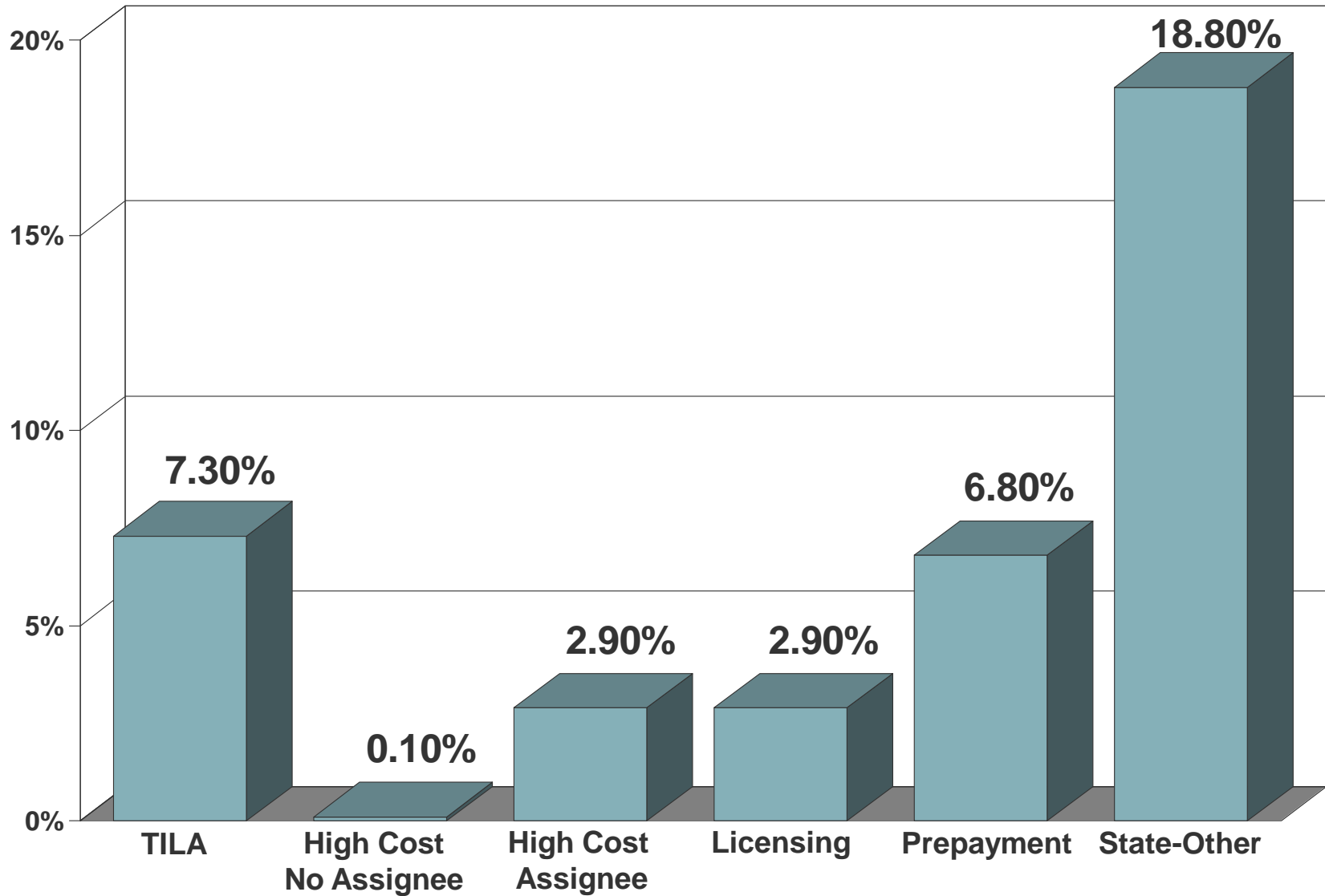
# BREAKDOWN OF “SIGNIFICANT COMPLIANCE VIOLATIONS”



*Total Significant Compliance Violations For Sampled Federally Regulated Institutions*

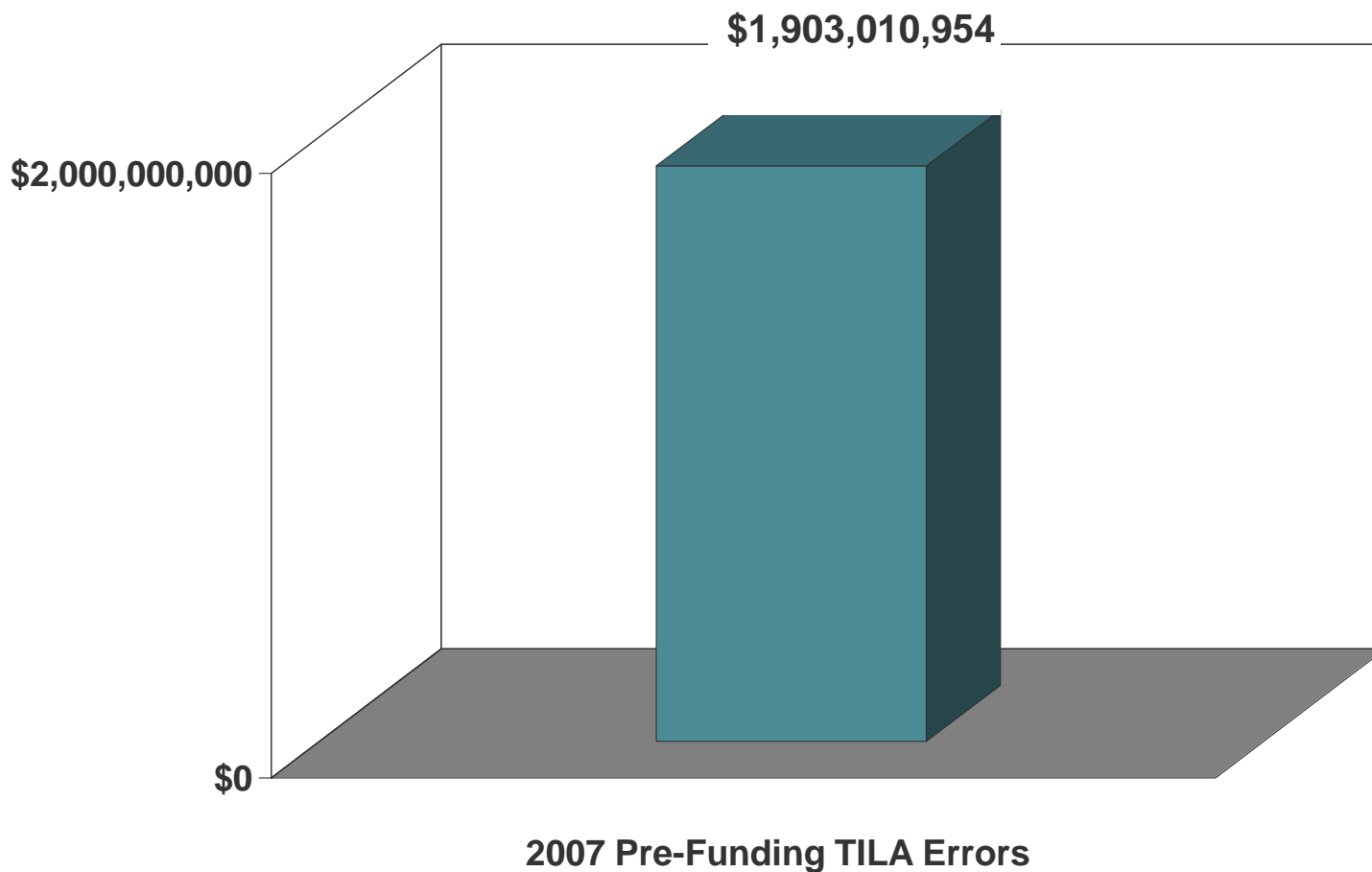
# MAVENT COMPLIANCE AUDIT SUMMARY

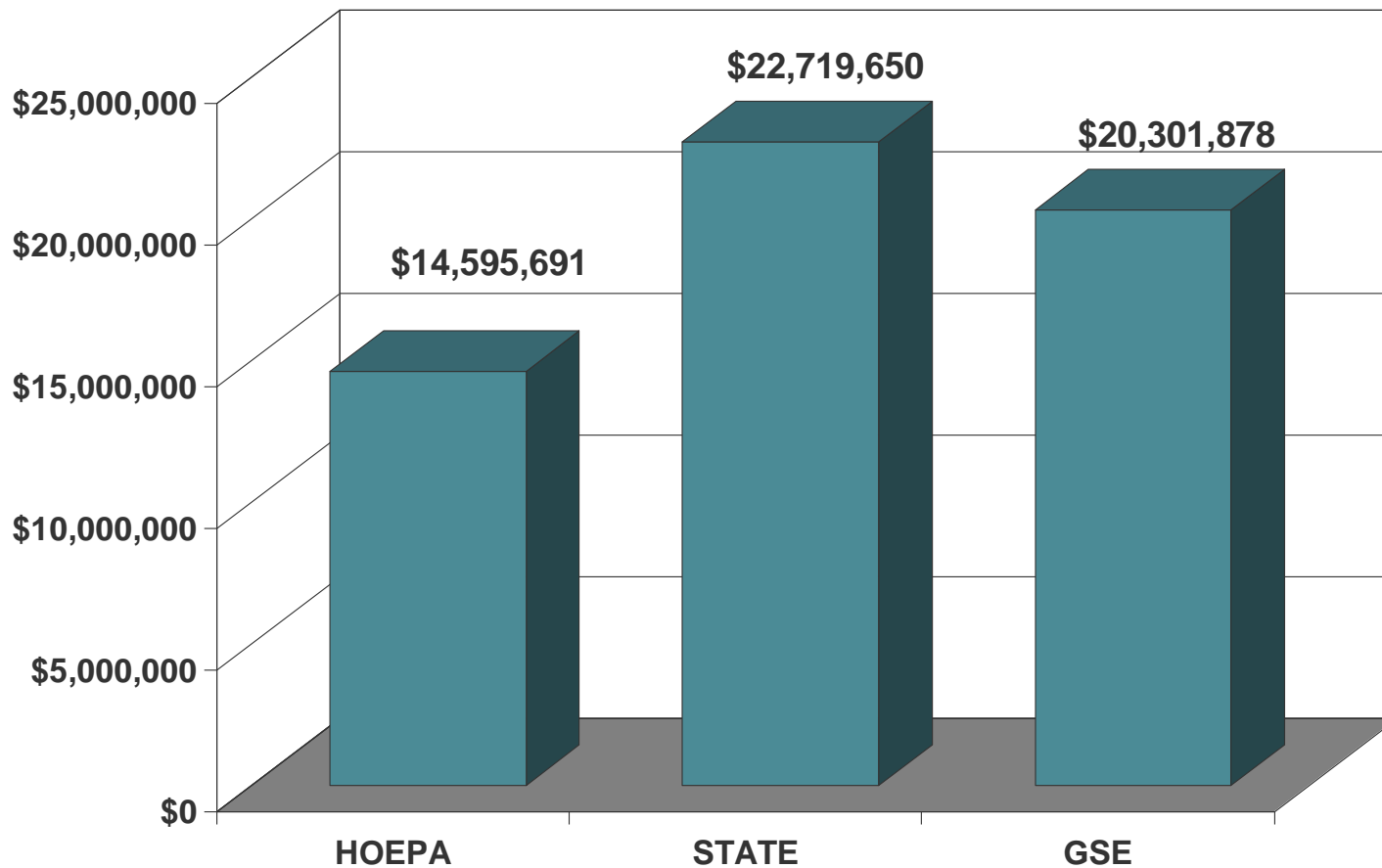
916 LOANS OUT OF 3,244 TOTAL (28%) VIOLATED ONE OR MORE LAWS



# INTERTHINX COMPLIANCE AUDIT

## 41,916 APPS FAILED INITIAL TILA TEST





2007 Pre-Funding TILA Errors

Expected Net Profit  
**\$385,000,000 (est.)**

“At-Risk” Applications  
**\$14,595,000—\$2,000,000,000**

\*All were corrected prior to funding!

# CURRENT TRENDS

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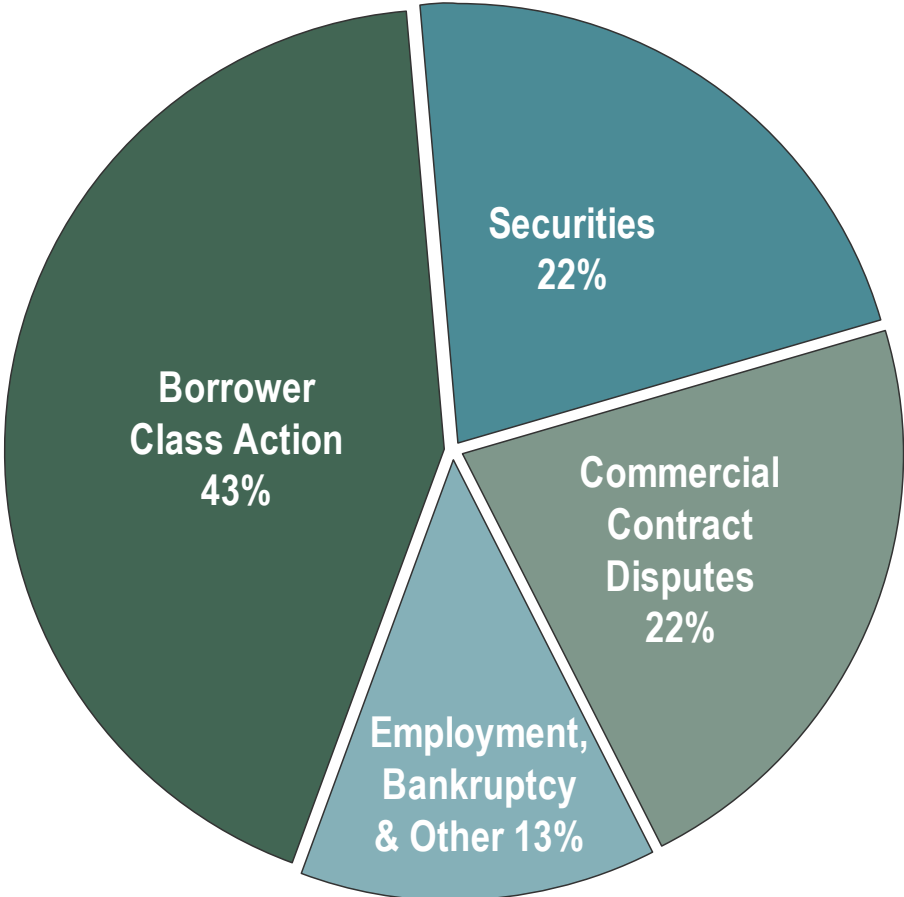
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- Regulatory Response
    - » State interventions into foreclosures
    - » Increasing costs from cures and penalties
    - » New laws and regulations
  - Litigation
    - » Borrower class action
    - » Borrowers seeking defense to foreclosure
  - Secondary Market
    - » Investors putting back loans to sellers
    - » Rating agencies enhancing criteria
  - Budget Cuts
    - » Staffing reductions impacting ability to monitor loans

# LITIGATION RISK

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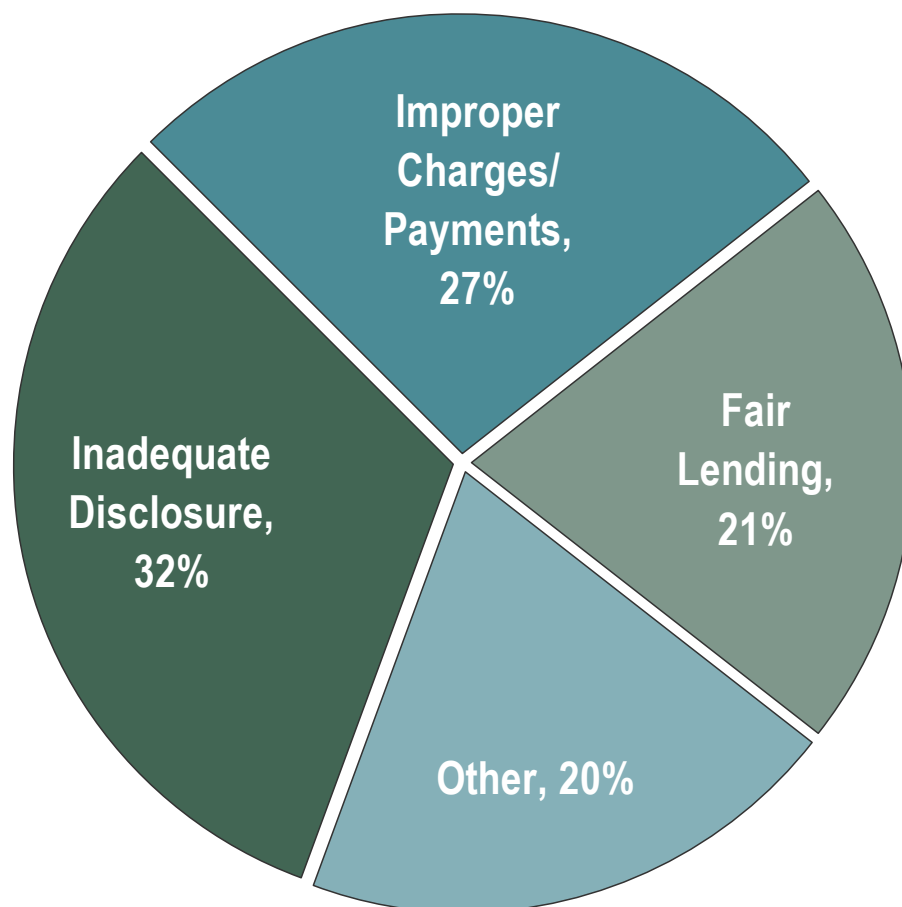
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*Subprime mortgage litigation outpacing savings-and-loan crisis of the early 1990s*



***H2:2007 Types Of Cases Filed***

*All of 2006's top 10 subprime mortgage originators have been named in a class action*



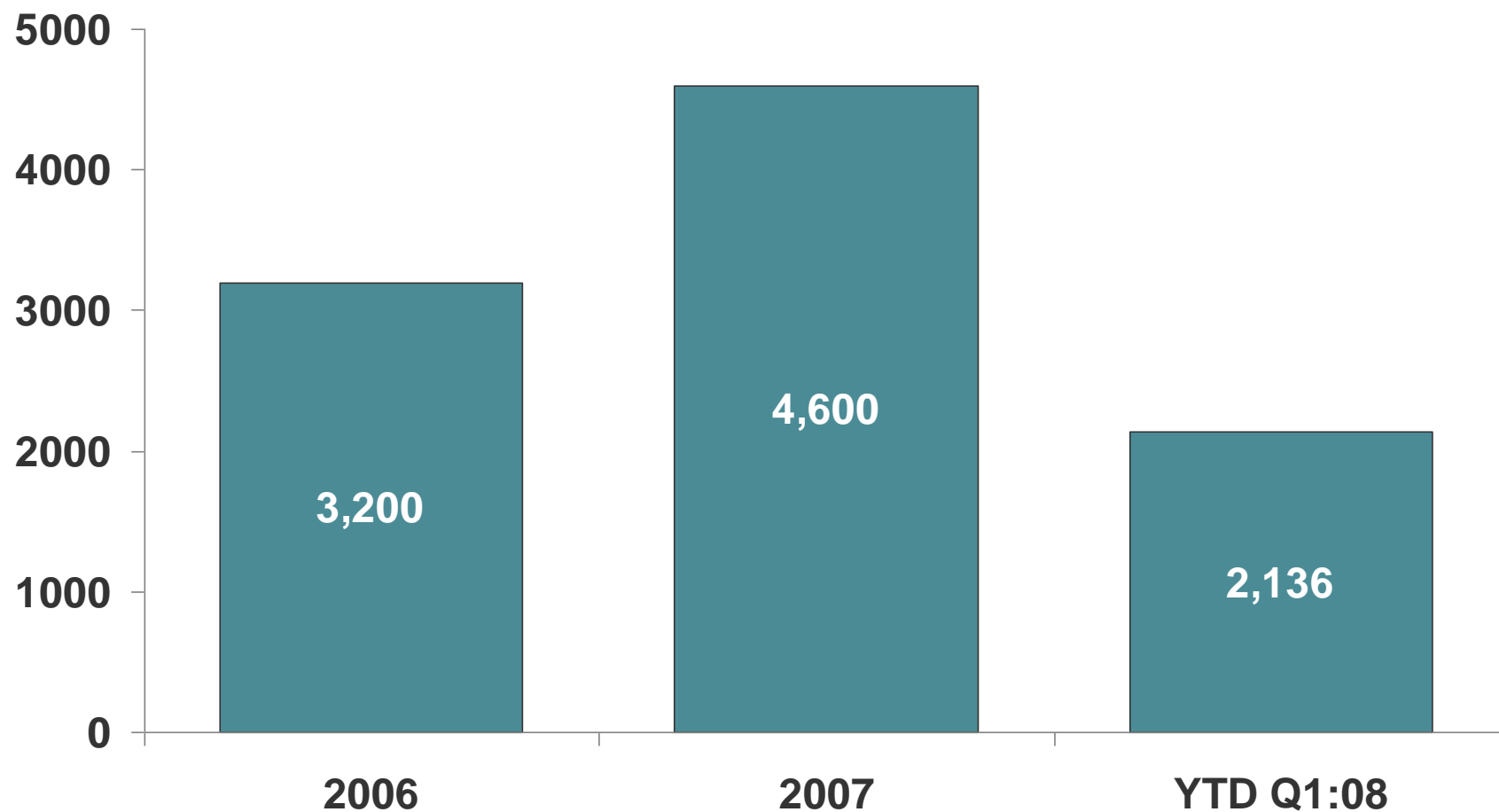
***Subprime-Related Filings by Case Type***

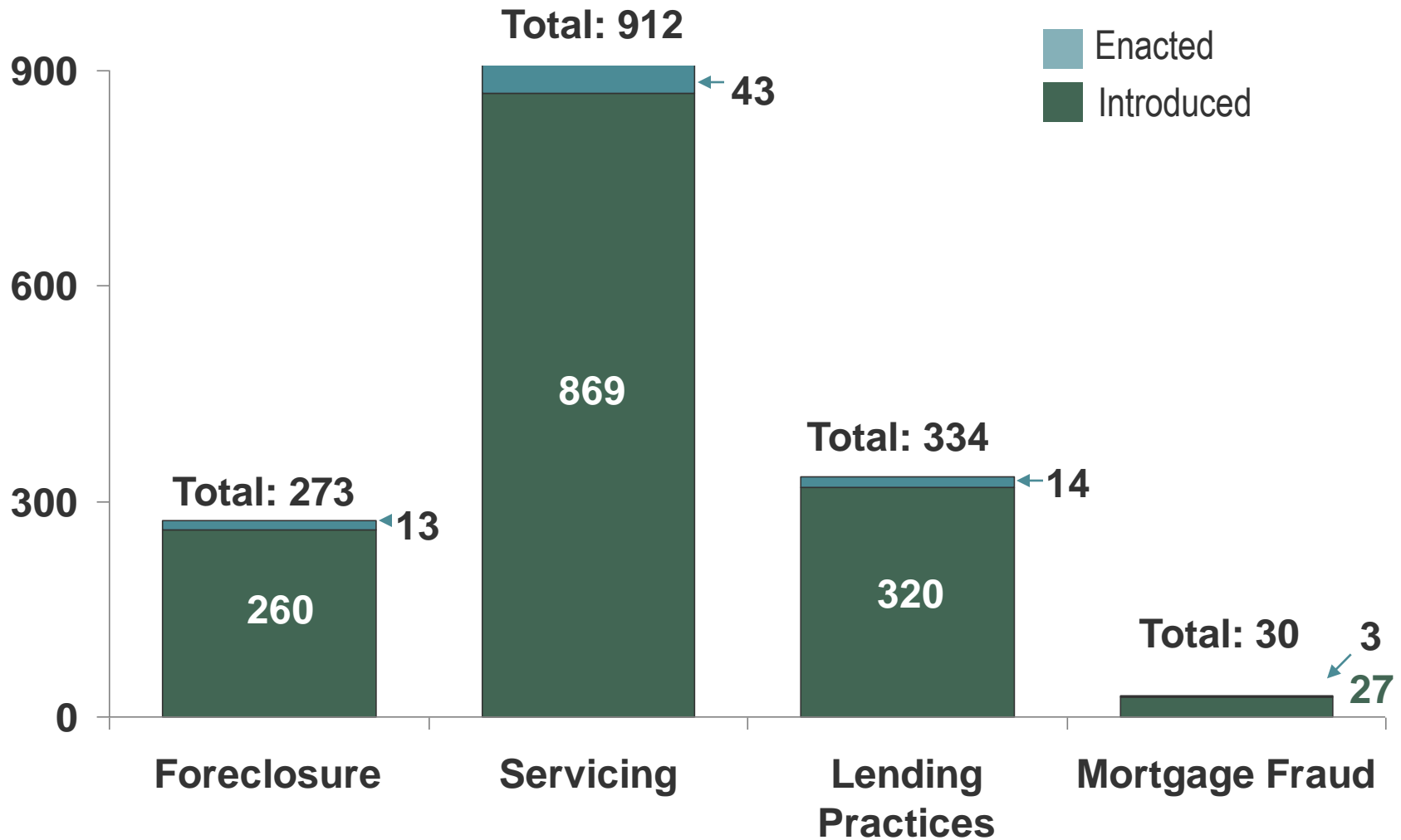
# REGULATORY RESPONSE

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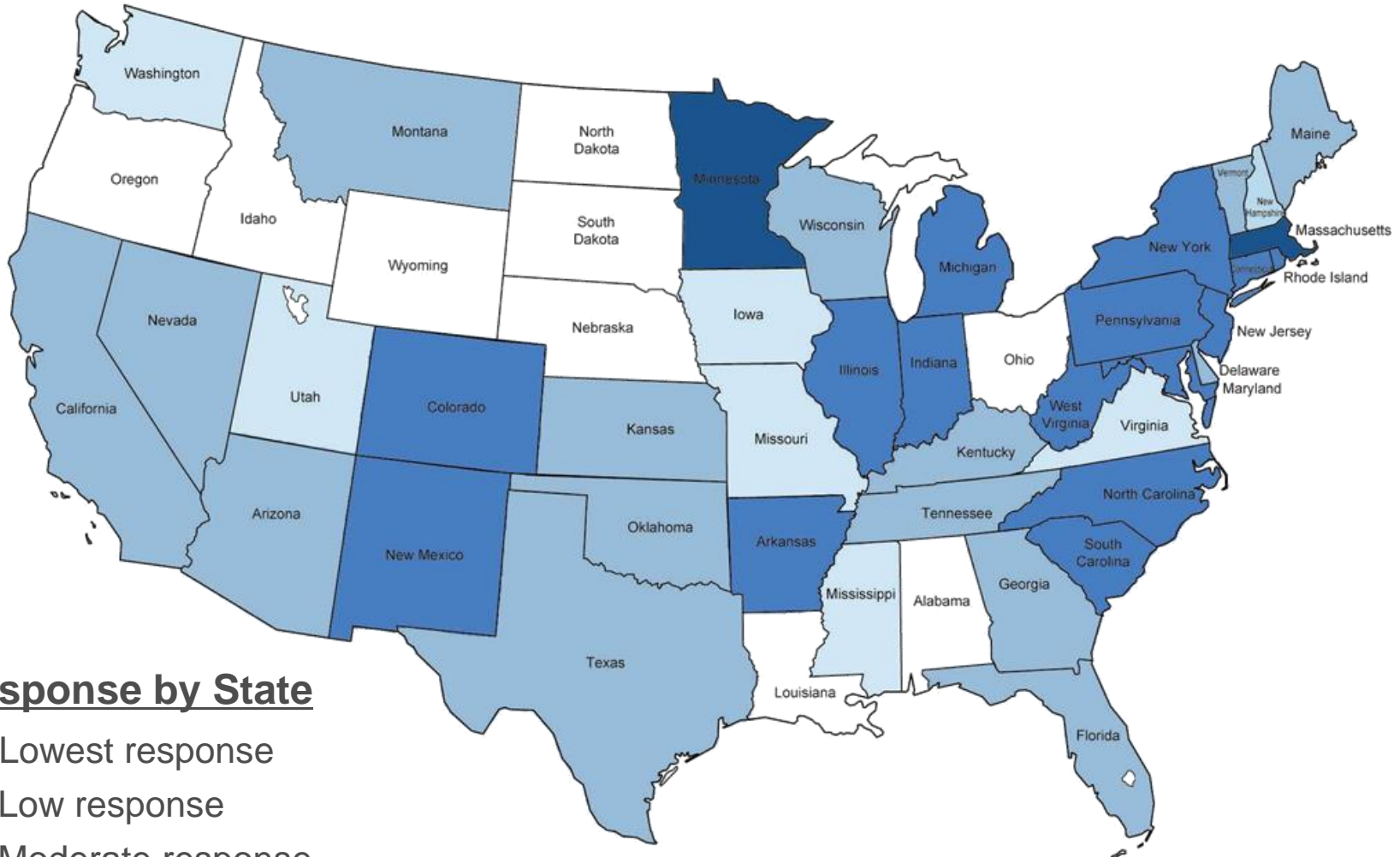
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*Total bills introduced that affect mortgage lending*





# CURRENT TREND: STATE RESPONSIVENESS



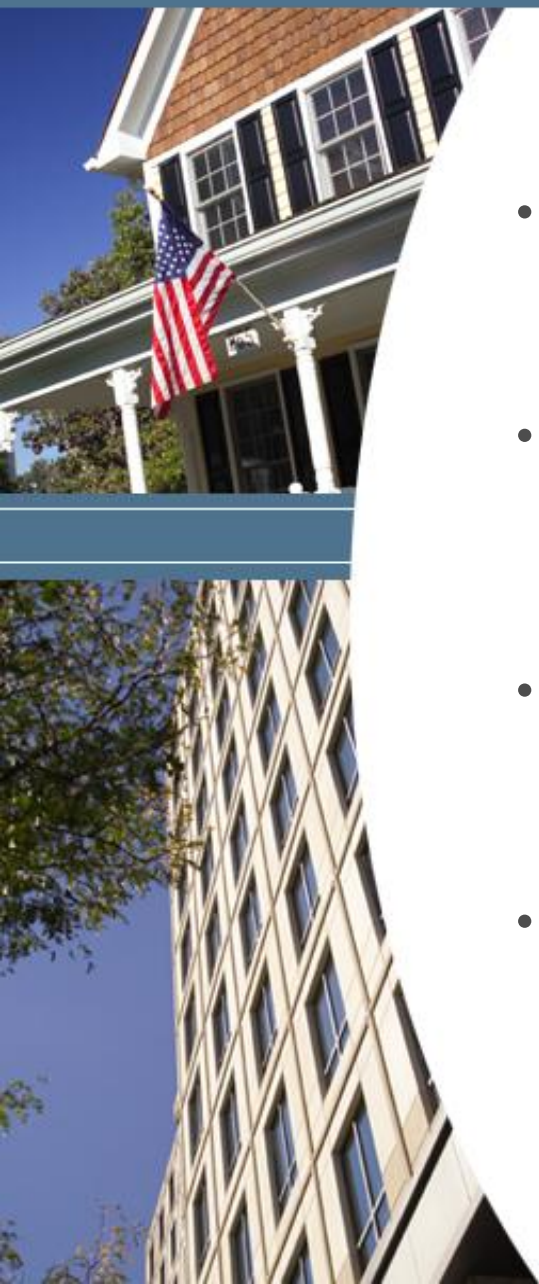
## Response by State

- Lowest response
- Low response
- Moderate response
- High response
- Highest response

# SECONDARY MARKET

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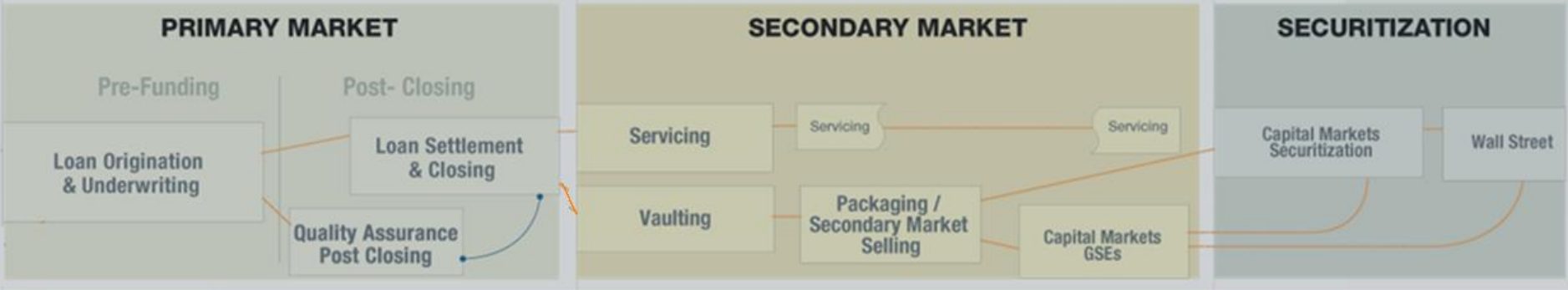
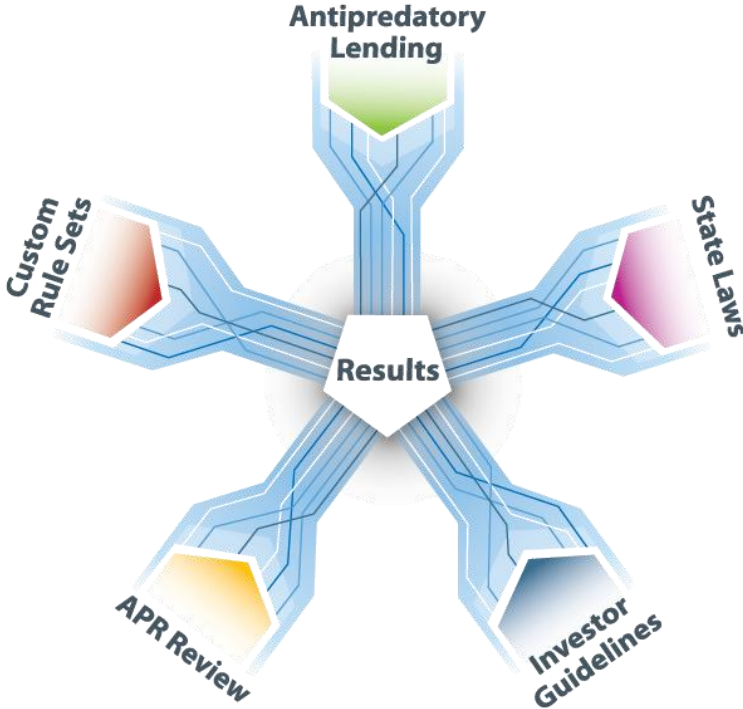


- Repurchases for Rep & Warrant Breaches
  - » “Put” depts are the new whole loan desk
- Foreclosures and deficiency judgments
  - » Pre-screen for non-compliance
- More comprehensive compliance reviews
  - » Usury, fee restrictions, prepay
- Rating agencies enhancing criteria

# AUTOMATING COMPLIANCE

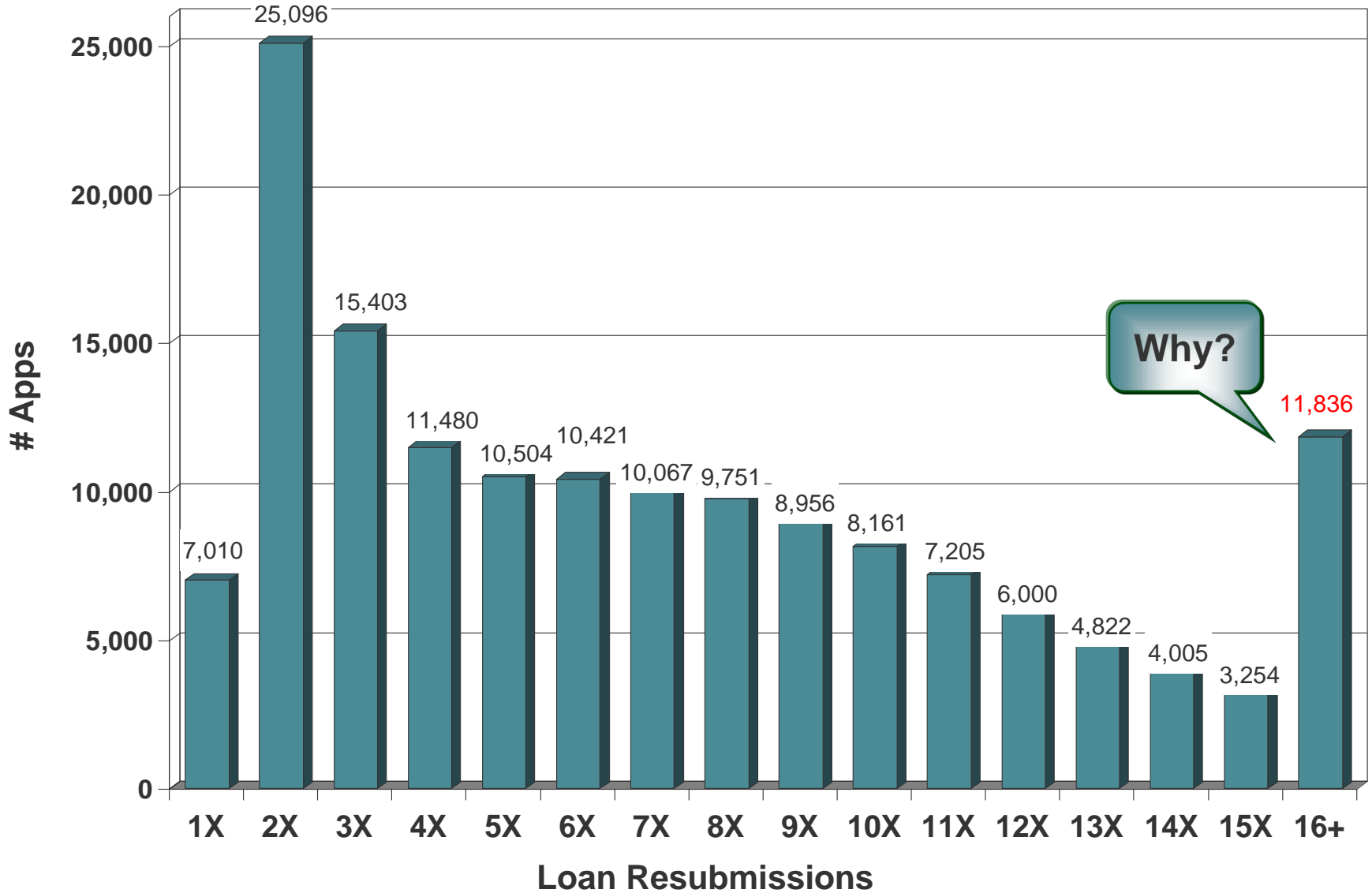
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# INTERTHINX PRE-FUNDING REVIEWS

## MOST APPS WERE REVIEWED 2-5 TIMES PRE-FUNDING



## LOAN CHARACTERISTICS

- » Property Address
- » Event Dates
- » Occupancy
- » Lien Position
- » Loan Amount
- » Borrower Income
- » Purpose
- » Rate
- » Fees
- » Yield Spread
- » Bona Fide Discount

## PRODUCT TYPE

- » Fixed vs. ARM
- » Pay-Option
- » Interest-Only
- » Balloon
- » Construction-Perm
- » Prepay Penalties
- » Neg Am
- » Mortgage Insurance
- » FHA / VA / RDA
- » HELOC



## RESULTS

- » TILA
- » HOEPA
- » Anti-Predatory
- » Licensing
- » State Law
- » Prepay
- » Usury
- » Restricted Fees
- » Internal Policies
- » Investor Guidelines
- » GSEs

## FORMULATION

- » Formulation
- » Government Relations
- » Outside Counsel
- » In-house Counsel
- » Compliance Experts

## DEVELOPMENT

- » Requirements Gathering
- » System Enhancements
- » Rule Authoring
- » Quality Assurance
- » Testing

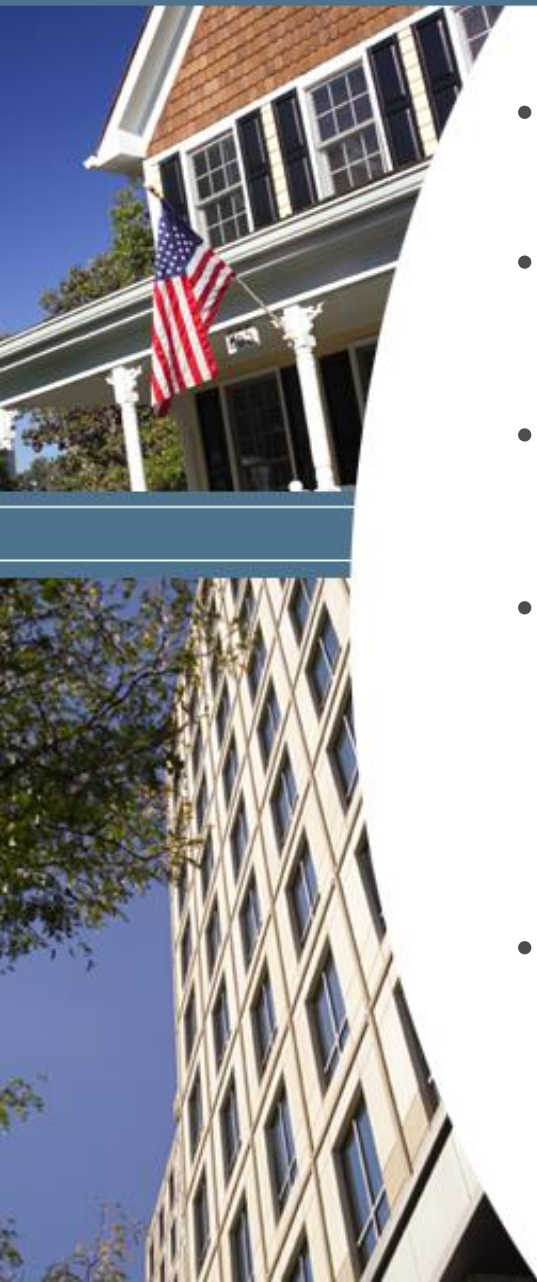
## IMPLEMENTATION

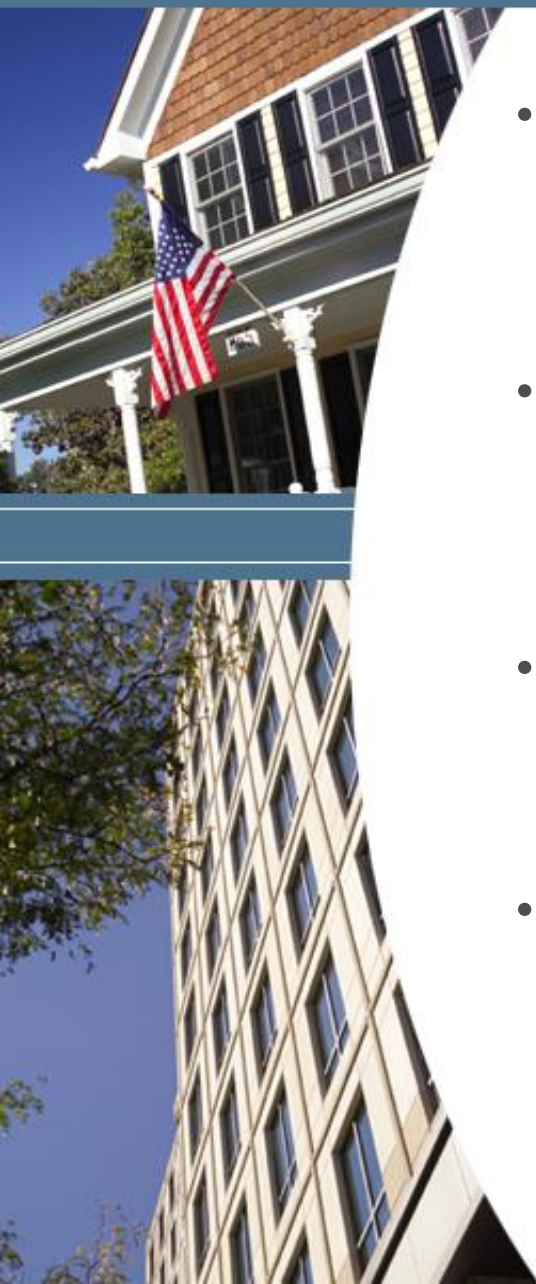
- » Change Control
- » Impact Analysis
- » Deployment
- » Support

# FUTURE TRENDS

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- Class-action and individual lawsuits
  - Executive accountability
  - Enforcement actions
  - Secondary markets
    - » Automated compliance conduits
    - » Stronger reps & warrants
    - » Increased data and transparency
  - Increased complexity with laws and regulations



- Unintended consequences
  - » Stimulus package
  - » HOEPA triggers
- Quick changes
  - » Maine
  - » Kentucky
- Vague regulation
  - » Minnesota
- Evolutionary complexity
  - » “Mezzanine” threshold regulations

	Categories	Ability to Repay	Prepayment Penalty	VOI / Low Doc
<b>HR 3915</b>	<ul style="list-style-type: none"> <li>• Qualified</li> <li>• Not Qualified</li> <li>• High Cost HOEPA</li> </ul>	✓	✓	✓
<b>S 2452</b>	<ul style="list-style-type: none"> <li>• Subprime</li> <li>• Non-Traditional</li> <li>• High Cost HOEPA</li> </ul>	✓	✓	✓
<b>FRB Reg Z</b>	<ul style="list-style-type: none"> <li>• Higher-Priced</li> <li>• High Cost HOEPA</li> </ul>	✓	✓	✓
<b>Maine</b>	<ul style="list-style-type: none"> <li>• Rate Spread</li> <li>• High Cost</li> </ul>	✓		✓
<b>Minn</b>	<ul style="list-style-type: none"> <li>• Subprime</li> </ul>	✓	✓	✓
<b>NC</b>	<ul style="list-style-type: none"> <li>• Rate Spread</li> <li>• High Cost</li> </ul>		✓	✓

## HIGH COST LAWS

State	Triggers	Index	Index Date
Maine	8% / 10%	Comparable Treasury Yield (H-15)	Reg Z
North Carolina	8% / 10%	Comparable Treasury Yield (H-15)	Reg Z

## RATE SPREAD LAWS

State	Triggers	Index	Index Date
Maine	3% / 5%	Applicable Treasury Yield (FFIEC)	HMDA
	OR 8% / 10%	Comparable Treasury Yield (H-15)	Reg Z
North Carolina	3% / 5%	Applicable Treasury Yield (FFIEC)	Reg Z
	AND 1.75% / 3.75%	CMR	HMDA/Prior Week
Minnesota	2% / 3%	Comparable Treasury Yield (H-15)	HMDA