The Maryland Consumer Rights Coalition
October 2006

PROTECTING HOMEOWNERSHIP:

The Challenge Of Preventing Abusive Lending And Foreclosure Practices

A Study Of Maryland Predatory
Lending & Foreclosure Laws

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The statements and recommendations contained in this report are those of the Maryland Consumer Rights Coalition and do not necessarily reflect the views of our funders or those individuals and organizations that we interviewed as part of the preparation of this report.

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The Maryland Consumer Rights Coalition is a nonprofit consumer education and advocacy organization that promotes fairness and safety in the consumer marketplace.

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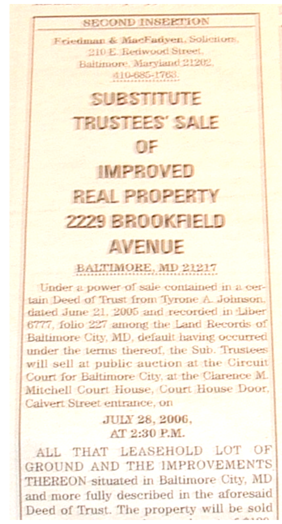

SECOND INSERTION

Friedman & MacFadyen, Solicitors,
210 E. Redwood Street,
Baltimore, Maryland 21202,
410-685-1763.

SUBSTITUTE TRUSTEES' SALE OF IMPROVED REAL PROPERTY 2229 BROOKFIELD AVENUE

BALTIMORE, MD 21217

Under a power of sale contained in a certain Deed of Trust from Tyrone A. Johnson, dated June 21, 2005 and recorded in Liber 6777, folio 227 among the Land Records of Baltimore City, MD, default having occurred under the terms thereof, the Sub. Trustees will sell at public auction at the Circuit Court for Baltimore City, at the Clarence M. Mitchell Court House, Court House Door, Calvert Street entrance, on

JULY 28, 2006,
AT 2:30 P.M.

ALL THAT LEASEHOLD LOT OF GROUND AND THE IMPROVEMENTS THEREON situated in Baltimore City, MD and more fully described in the aforesaid Deed of Trust. The property will be sold

For many years public policy makers and advocates have pushed the idea of homeownership as the "American Dream." Numerous resources have been devoted at the federal, state and local level to helping individuals become homeowners. Unfortunately, not nearly as much effort and energy has been devoted to helping people maintain homeownership. In fact, the attitude has been much the opposite – many feel that if someone loses their home, it must be their own fault. In many states, foreclosure laws are designed to make it quick, easy and relatively inexpensive for a lender to sell a person's home, while making it difficult and costly for a homeowner to challenge a foreclosure proceeding.

This report finds that predatory mortgage loan practices continue to be a problem for homeowners in Maryland and that subprime loans account for a disproportionate share of the foreclosures in the state. We conclude that Maryland's anti-predatory lending law, enacted in 2002, is one of the weaker state laws passed in the wake of widespread lending abuses in the 1990's. We found that Maryland's foreclosure law does not provide homeowners with adequate notice or other protections needed to prevent the unnecessary loss of their homes. We also found that there is little help for homeowners facing foreclosure, even for those who are unable to pay their mortgage through no fault of their own.

In order to help preserve homeownership in Maryland we make the following recommendations:

- Maryland needs to enact a stronger predatory lending law that, among other things, will cover more high cost loans, limit the financing of points & fees and extend liability to assignees.
- Maryland should improve the foreclosure process by providing better notice to homeowners and a meaningful opportunity to raise challenges to foreclosure sales.
- Maryland should require early referral of a delinquent homeowner for counseling and help provide adequate counseling resources. In addition, we should provide financial help for those homeowners who are unable to pay their mortgage through no fault of their own.

These steps would preserve homeownership by reducing predatory lending, improving Maryland's arcane foreclosure system and providing resources for families faced with foreclosure. Preserving homeownership deserves at least as much time, attention, and money as helping families become homeowners.

Maryland should act now to address the problem of predatory lending and mortgage foreclosures before the situation becomes critical. Mortgage delinquencies are predicted to increase by 10 to 15 percent in 2006 among high cost loans.[1] Homeowners are likely to face financial difficulties caused by higher interest rates and higher energy costs.[2] 2007 is likely to bring an even higher increase in delinquencies, as many subprime adjustable rate loans will change rates.[3] Federal regulators have warned banks that non-traditional mortgages such as interest-only loans may lead to a rash of defaults when the principal must be paid or interest rates increase. [4] It is crucial to address these issues now, before we face a large increase in foreclosures and the resulting loss of homeownership.

Introduction

Why should we as a society care about predatory lending practices and high foreclosure rates? Predatory lending is unfair. The lack of strong regulation in this area allows unscrupulous businesses to take advantage of unsophisticated homeowners, resulting in devastating effects on individuals and families. In addition, predatory lending and foreclosures destabilize neighborhoods and undermine public and private efforts to increase homeownership and revitalize neighborhoods.[5] For example, in Baltimore in the late 1990's a wave of predatory property flipping caused serious negative consequences for targeted neighborhoods[6].

More resources need to be devoted to preserving homeownership -- keeping homeowners in their homes. For far too many Marylanders, we are selling them a pipe dream of homeownership, instead of the proverbial "American Dream." We are encouraging homeownership without providing individuals and families with the knowledge and support they need to sustain homeownership. There is little help for homeowners who find themselves unable to pay their mortgage, even if it is due to circumstances beyond their control such as a death, health crisis, divorce or layoff. For the many families that risk losing their homes because of predatory practices or who face financial crisis and have no where to turn for help -- we need to do more.

To compound the problem, there are people who prey on unsophisticated homeowners and convince them to refinance an affordable mortgage with an unaffordable one, often stripping the equity from their home and in some cases pushing the homeowner into foreclosure. In addition, many unsophisticated consumers enter into purchase money mortgages that are unaffordable at the outset and their homes end up in foreclosure, leaving a family with no home and damaged credit. Many sellers make use of buy downs to make the payments affordable for a limited period of time. The myriad of new mortgage products offering variable rates, some changing every month, to interest only loans, lead many to spend more than they can actually afford.

In addition to origination issues, there are also businesses that service loans in a predatory way. There are homeowners who make all of their scheduled mortgage payments but find that bogus or inflated charges have been added making their payments short. All future "short" payments are placed in suspense, late fees are added, and soon the homeowner is in default.

This report looks at Maryland laws related to predatory lending and foreclosures, compares Maryland laws to other state laws and model laws. It also looks at federal preemption, which limits the ability of states to regulate certain lenders and types of mortgage loans. As part of this report, we interviewed experts in foreclosure and predatory lending and advocates from around the state who help homeowners who have been the victims of predatory lending and/or who are facing foreclosure. We also looked at the resources available to help consumers who are facing foreclosure or are trying to deal with a predatory loan.

Predatory Mortgage Lending

What is Predatory Mortgage Lending?

The term "predatory lending" has been used to describe a broad range of loan features and practices that are not common in the prime lending market and that provide no benefit to the borrower. While there is no precise definition of predatory lending, there is wide agreement on what practices are considered predatory. The most common predatory practices, which will be discussed in more detail below, are:

- Excessive fees and points
- Prepayment penalties
- Kickbacks to mortgage brokers
- Loan "flipping"
- Single premium insurance
- Mandatory arbitration clauses
- Ignoring borrower's ability to repay
- Concealing the true nature and cost of the loan
- Balloon payments
- Excessive interest rates [7]

Predatory loans are a subset of the subprime lending market. For those used to dealing with the prime mortgage market, the abuses that occur in the subprime market can be quite eye opening. Most middle and upper-income individuals receive competitive interest rates and low fees when they purchase a home or refinance a mortgage.[8] For those who have less than perfect credit or who are steered to a subprime lender although they have acceptable credit, the experience can be much different. [9]

Subprime mortgages, by definition, cost more than prime mortgages and the price difference can be substantial.[10] In theory, subprime lenders price their products to cover the perceived higher risk of the borrower. However, many question whether the pricing reflects the real risk to the lender. In fact, almost 50 percent of borrowers who have subprime loans qualify for conventional (prime) financing.[11]

Subprime lending has grown exponentially in recent years, from $35 billion in 1994 to $529 billion in 2004.[12] According to a study done by HUD, subprime loans are three times more likely in low-income neighborhoods than in high-income neighborhoods.[13] The study also found that subprime loans are five times more likely in black neighborhoods than in white neighborhoods. Homeowners in high income black neighborhoods are twice as likely as homeowners in low-income white neighborhoods to have subprime loans.[14] The targeting of minorities by predatory subprime lenders has been widely documented.[15]

A substantial increase in foreclosure rates over the last 20 years has been linked directly to the subprime mortgage market.[16] Over the past twenty years homeownership has increased by 3.6%, while foreclosures have increased 335.6%.[17] The rate of foreclosures in the subprime market is substantially greater than the rate in the prime market. In the prime market, foreclosures have remained at less than 1% of loans for over 20 years. During the same time period subprime loans have had foreclosure rates ranging from over 3% to as high as 9%.[18] In the fourth quarter of 2005, the number of subprime loans in foreclosure in Maryland was 9.7 times higher than prime loans in foreclosure.[19] The number of seriously delinquent subprime loans in Maryland was almost 11 times higher than prime loans during the fourth quarter of 2005.[20]

According to HUD, subprime loans account for a disproportionate share of the foreclosures in low-income and predominantly black neighborhoods in Baltimore City.[21] Subprime loans make up a larger share of foreclosures than their share of originations.[22] In addition, HUD found that foreclosures on subprime loans occurred on average 1.8 years after loan origination, compared to 3.2 years for FHA and prime loans.[23]

Predatory Lending Practices in Maryland

In preparing this report, we spoke with housing counselors, attorneys, consumer advocates, and government officials from various parts of the state about the types of loan abuses that are occurring in Maryland. The commonly observed problems include:

- **Refinancing low cost mortgages** – Homeowners who want to obtain a small loan for home improvements or other expenses are pushed into refinancing the entire balance of an existing low cost mortgage with a much more expensive loan.

- **Overreaching and "bird-dogging" by mortgage brokers** – Brokers often use aggressive marketing, including going door-to-door to find prospects for loans, and convince homeowners to take out loans that are not in the homeowner's best interest.

- **High cost loans that avoid federal and state predatory lending laws** – Lenders avoid having to comply with state and federal predatory lending laws by pricing their very high cost loans just under the triggers set by Congress and state law.

- **Failure to escrow for taxes and insurance** – When loans are refinanced there is often no escrow account established for taxes and insurance. The homeowner does not realize that the taxes and insurance are not included in their monthly payments and has difficulty paying a large bill in one lump sum and often results in the lender purchasing expensive insurance for the homeowner.

- **Unaffordable loans** – A significant percentage of individuals seen by counselors and advocates (up to 25%) are in loans that they could not afford in the first place. The family does not have enough income to afford the loan payment and other necessary expenses such as food, utilities and basic maintenance for their home.

- **Misrepresentation of loan terms** – When consumers arrive at settlement they find out the loan terms are not what they were promised by the broker or lender. Consumers feel pressured to continue with settlement or risk losing a down payment. Many have been encouraged to stop paying their existing mortgage pending the refinancing. If they refuse to refinance once they learn the true loan terms, it leaves them in default on their existing loan.

- **High risk loans products sold inappropriately** – Brokers often push high risk loan products such as interest only loans, negative amortization loans, loans with adjustable rates or balloon payments, to consumers without the financial wherewithal to deal with substantial changes in payment amounts. Balloon payments appear to be a particular problem on Maryland's eastern shore.

- **"80-20" loan products** – Consumers are encouraged to enter into two loans, one for 80% of loan amount and a second for 20%. This is ostensibly to avoid PMI insurance. The second loans contain high interest rates and balloon payments.

Maryland Lending Laws

In order to evaluate and understand Maryland laws related to predatory lending, it is important to have an understanding of how credit is regulated in Maryland. Maryland, like many other states, has a number of different statutes that govern extensions of credit. In this report, we will discuss those credit statutes that govern consumer loans secured by real property.[24] Which statute governs a particular real estate loan depends on a number of factors including, the type of creditor making the loan, whether the loan is "open-end"[25] or "closed-end,"[26] whether the loan is secured by a first or junior mortgage, and whether the lender elected to make the loan under certain laws. Maryland also requires that lenders be licensed unless they are exempt from licensing. The licensing provisions are also discussed below.

The importance of determining which law applies cannot be understated, because it is impossible to know what interest rates, fees and loan terms are permitted until you determine what law governs the loan in question. For example, balloon payments are restricted in Maryland for certain loans, but not others. Also crucial to determining what loan provisions are allowed under Maryland law is determining whether state law is preempted by federal law or regulations. The preemption issue is discussed below at page 17.

Maryland Credit Statutes

Maryland's credit laws are set out in Title 12 of the Commercial Law Article ("CL") of the Annotated Code of Maryland. Each statute sets limits on interest rates and fees, contains restrictions on certain loan terms, requires certain disclosures and sets out penalties for violations of the law. All real estate loans made in Maryland are subject to the requirements of one of these laws and possibly more than one, although some specific provisions of these statutes may be preempted by federal law. [27] In most cases, the creditor can choose which law it wants to apply to the credit transaction. The credit laws that are applicable to loans secured by real estate are:

- **Interest & Usury, CL §§12-101, *et seq.* ("Usury Law") –** The Usury Law provisions generally apply to loans that are not governed by one of the other credit laws or where a creditor does not elect to make the loan under Subtitle 9 or 10. Both open-end and closed-end loans can fall under this statute.
- **Consumer Loans – Credit Provisions, CL §§12-301, *et seq.* ("Consumer Small Loan Law") –** The Consumer Small Loan Law is limited to loans of $6,000 or less. Since most loans secured by real estate are for more than $6,000, its applicability to real estate lending is limited.
- **Secondary Mortgage Loans – Credit Provisions, CL §§12-401, *et seq.* ("Second Mortgage Law") –** The Second Mortgage Law applies to loans secured by second or other junior liens on real estate, except if the lender elects to make the loan under Subtitle 9 or 10.[28] Because the provisions of the Second Mortgage Law are much stricter than Subtitle 9 or 10, most lenders elect out of this statute. In addition, since both federal and state law favors lenders who hold first liens on real property, the number of second or junior liens originated has declined dramatically in the past twenty years, further limiting the number of loans that fall under this subsection. Some refinancings of first mortgages may come under this law.[29]
- **Credit Grantor Revolving Credit, CL §§12-901, *et seq.* ("Subtitle 9") –** "Subtitle 9" and "Subtitle10" were enacted in 1983 as part of an attempt to modernize Maryland credit laws.[30] "Subtitle 9" applies to open-end transactions, such as home equity loans. Creditors must make a specific written election in the loan contract to come under this statute.
- **Credit Grantor Closed-End Credit, CL §§12-1001, *et seq.* ("Subtitle 10") –** "Subtitle 10" applies to closed-end transactions including traditional purchase money real estate loans and loans secured by first and second mortgages. Creditors must make a specific written election in the loan contract to come under this statute.

Lender Licensing Statutes

In Maryland, lenders who make residential real estate loans are required to be licensed by the state, unless they are exempt from licensing.[31] Generally, banks, savings & loans, credit unions, savings banks and trust companies are exempt. [32] The licensing provisions require lenders to obtain a license and a surety bond. The Commissioner of Financial Regulation has the authority to inspect the books and records of licensed lenders and can take action against lenders for violations of the law, including revoking licenses.[33] Maryland law gives the Commissioner's office jurisdiction over "loan servicers" as well as lenders.[34]

Mortgage Broker Restrictions

According to the advocates and counselors we spoke with, mortgage brokers are involved in a high percentage of predatory loans. While consumers rightfully believe that the broker is acting in the consumer's best interest, brokers often have a financial incentive to place a consumer in a higher cost loan in order to make additional commissions.[35]

In 1979, Maryland enacted a law that places restrictions on mortgage brokers. The "Finder's Fee Act" is intended to protect consumers from abuses by brokers.[36] The statute requires the broker to provide the borrower with a written agreement that states the amount of the broker's fee.[37] The statute allows brokers to charge a fee of up to 8% of the loan amount.[38] A broker who refinances a loan on the same property within two years can only charge a fee for the amount by which the second loan exceeds the prior loan. [39] The Act also prohibits a broker from charging a fee if the broker or an employee of the broker has any ownership interest in the lender.[40] The Maryland Court of Appeals has found that the Finder's Fee Act is not preempted by federal law.[41]

As of October 1, 2005, individual mortgage brokers are required to be licensed in Maryland, unless exempt from licensing.[42] The Commissioner of Financial Regulation may investigate licensees, including examining books and records, examining witnesses and subpoenaing documents.[43] The Commissioner has the power to deny or revoke licenses if a broker is convicted of certain crimes or commits fraud in connection with any loan transaction, among other reasons.[44] As of Jan. 1, 2007, licensees will be required to have 3 years experience in the mortgage lending business, 40 hours of classroom education, pass a written exam, and be of good moral character to obtain or renew a license.[45]

Federal Predatory Lending Law

Necessary to evaluating Maryland's predatory lending laws is a basic understanding of the federal Home Ownership and Equity Protection Act (HOPEA).[46] HOEPA was enacted in 1994 to address predatory lending practices that targeted primarily low-income, minority and elderly consumers.[47] HOEPA governs only closed-end loans that are non-purchase money mortgage loans. It does not cover purchase money loans or open-end loans such as home equity loans. HOEPA covers only high cost loans which are defined in the statute as loans that meet one of following triggers:

- The loan has an APR which is 10% above the rate for Treasury securities of a comparable term. For loans made after Oct. 1, 2002, the trigger is 8% for first lien mortgages and 10% for second or junior liens.
- The loan has upfront fees and charges of 8% of the total loan amount (which is not the gross loan amount) or $400, whichever is greater.

If a loan meets the triggers and therefore is a covered loan under HOEPA, lenders are prohibited from including certain provisions in loan documents. [48] HOEPA prohibits the following terms in covered loans:

- Prepayment penalties (with some exceptions)
- Interest rate increases upon default
- Negative amortizations
- Balloon payments (unless loan has a term of 5 years or more)
- Prepaid payments (unless no more than 2 months and money is escrowed)
- Due on demand clauses (with some exceptions, applies to loans made after 10/1/02).[49]

HOEPA also prohibits the proceeds of the loan from being made payable solely to a home improvement contractor and requires the lender consider the borrower's ability to repay the loan.[50] HOPEA requires an additional disclosure be given to consumers 3 business days before the loan is closed advising the borrower that they do not have to complete the loan transaction and listing specified loan terms.[51] One of the more important provisions of HOEPA is that it extends liability to assignees of covered loans, allowing borrowers to raise any claims and defenses they may have against whoever is holding the loan.[52] Additional HOPEA prohibitions that became effective on Oct. 1, 2002 include refinancing by the same creditor within one year and making an open-ended loan to avoid HOEPA.[53]

HOEPA has been widely criticized by consumer advocates and others as being ineffective.[54] In part, because the triggers that subject a loan to HOEPA are high, very few subprime loans exceed the interest and points threshold. While it is difficult to determine how many loans are covered under HOEPA, a recent study estimated that 1.94% of loans would be covered under the new 2002 HOEPA triggers.[55] Lenders can easily avoid the requirements of HOEPA by pricing loans just below the thresholds. In addition, a large number of real estate related loans are not covered by HOEPA at all including open-end loans such as home equity lines, purchase money mortgages or reverse mortgages.

Maryland's Predatory Lending Law

In 2002, the Maryland legislature enacted House Bill 649 which addressed the problem of predatory lending. The Maryland law is widely considered one of the weaker state laws passed in the wake of widespread attention to predatory lending issues around the country and the passage of comprehensive predatory legislation in North Carolina.[56] In fact, a number of consumer and housing organizations in Maryland were so unhappy with final version of HB 649 that they requested the Governor veto the bill.[57]

A look at the legislative history of the Maryland law sheds some light on why Maryland did not take more decisive action to deal with predatory lending. House Bill 649, as originally drafted preempted local governments from enacting laws to address predatory lending. There were no consumer protections in the bill initially. At the time HB 649 was introduced, Baltimore City and Prince George's County were considering enacting strong anti-predatory lending legislation.[58] Banking and lending institutions pushed for HB 649 in order to prevent local jurisdictions from addressing the issue.

At the urging of housing and consumer advocates, HB 649 was amended to include provisions to protect consumers from predatory practices. Amendments were offered to the bill that mirrored some of the provisions of the model Home Loan Protection Act published by the AARP Public Policy Institute.[59] The proposed amendments would have expanded the definition of high cost loans beyond the federal Home Ownership and Equity Protection Act (HOEPA) in order to cover a larger percentage of high cost loans and would have required those loans to comply with the HOEPA limits on balloon payments, negative amortization, advance payments, and increased interest rates after default.

After contentious negotiations among advocacy groups, legislators, and industry lobbyists[60] what emerged was a bill that gave the industry groups what they wanted – preemption of local laws dealing with predatory lending. The bill also provided some modest protections for consumers for certain "covered loans." "Covered Loans" are defined as mortgage loans that meet the criteria of loans subject to HOEPA, except that the comparison percentages for loans are one percentage point less than those specified in HOEPA.[61] The provisions of the 2002 law, which are discussed in more detail in the next section:

- **Prohibit Financing of Single Premium Insurance** – The financing of single premium insurance for credit life, health, and involuntary unemployment insurance is prohibited in covered loans.[62]
- **Require Recommendation to Seek Counseling** – At the time the borrower completes a loan application for a covered loan, the lender must give the borrower a written recommendation that the borrower seek home buyer education or housing counseling and provide the borrower with a list of "county approved" housing counseling agencies.[63]
- **Require Consideration of Ability to Repay** – Prohibits lenders from making a covered loan without "giving due regard to the borrower's ability to repay the loan…"[64] The borrower is presumed to be able to pay if the total of the borrower' scheduled monthly payments do not exceed 45% of the borrower's gross monthly income.[65] The ability to repay section does not apply to a borrower whose gross monthly income is greater than 120% of the median family income for the metropolitan statistical area in which the property is located.[66]

Montgomery County's Anti-Discrimination in Lending Law

After an independent consultant found racial and ethnic disparities in Montgomery County, Maryland, the county enacted a local law addressing discriminatory lending practices in 2005. The law expands the definition of discriminatory housing practices under the county's human relations law. Specifically, the law prohibits lenders from "restricting or attempting to restrict a person's choices" when seeking a mortgage loan because of race, color, religious creed, ancestry, national origin, sex, marital status, disability, presence of children, family responsibilities, source of income, sexual orientation, or age.[67] The law prohibits discouraging a person from a particular loan, product, program or service with more favorable terms, and prohibits offering less favorable mortgage loan terms than would otherwise be offered. In addition, the law prohibits the financing of single premium credit life insurance, excessive upfront points and fees, excessive prepayment penalties or "compensation paid directly or indirectly to a person from any source."[68] The law, which was to take effect on March 8, 2006, has been stayed by a county court after a lawsuit was filed by the American Financial Services Association and others.[69]

Comparison of Maryland's Predatory Lending Law To Other States

Following the lead of North Carolina, which passed a strong predatory lending law in 1999, at least 23 states have enacted some predatory lending restrictions. Most laws have used the HOEPA statute as a starting point and have either expanded the coverage of HOEPA or increased the restrictions for loans otherwise covered by HOEPA or both.

Coverage

A number of states have passed laws that go beyond HOEPA to include open-end loans and/or purchase money loans.[70] States have also expanded the coverage of HOEPA by lowering the APR and the points and fees triggers. A model state predatory loan statute also proposes expanding the coverage to include open-end loans and home purchase loans and lowering the triggers for covered loans.[71] In 2002, when Maryland enacted its predatory lending law, it made the law applicable to loans that have APR's and/or points and fees 1% lower than the HOEPA triggers. For loans made after Oct. 1, 2002, that translates to 7% for first liens and 9% for second liens OVER the rate for U.S. Treasury Securities. Since the interest rate that triggers the Maryland law is tied to the Treasury rate, the interest rate threshold changes with changes in the Treasury rate. The points and fees trigger in Maryland is 7%. For an example of the interest rate that would trigger the Maryland predatory lending law, for a 30 year first mortgage, as of March 15, 2006, see Table 1 below.

Treasury Rate	Maryland Trigger	Loans Covered by MD Predatory Lending Law
4.75%[72]	7%	11.75% and over

Table 1. Interest Rate Trigger for Maryland Predatory Lending Law for 30 Year First Mortgage

While Maryland law may cover slightly more loans than HOEPA, it does not expand the coverage enough to cover the bulk of predatory loans. A number of other states have expanded coverage by lowering the threshold farther (6% for first liens and 8% for second liens is the threshold used by a number of states) and by lowering the points trigger (5% is used in a number of the stronger state laws.)[73]

Substantive Restrictions

The Maryland predatory lending law placed relatively few substantive restrictions on high cost loans. While the law did define high cost loans more broadly than HOEPA, it failed to deal with some of the most pervasive problems in the predatory loan marketplace. The only issues addressed by the 2002 law were ability to repay; single premium credit life insurance; and counseling. We will address each of these issues separately.

Ability to Repay

Maryland's predatory lending law added a requirement, modeled on HOEPA, that for covered loans, the lender must give "due regard to the borrower's ability to repay the loan in accordance with its terms."[74] The law creates a presumption that the borrower is able to repay a loan if the borrower's total scheduled monthly payment obligations, including the payment of the loan being made, do not exceed 45% of the borrower's gross monthly income.[75] The ability to repay requirement does not apply if the borrower's gross income is greater than 120% of the median family income for the metropolitan statistical area in which the residential real property is located.[76] Maryland's provisions regarding ability to repay are similar to HOEPA and to laws passed in a number of other states, although most other states that set a debt to income ratio have set it at 50%.[77] While Maryland law on debt-to-income ratios is relatively strong, because it only applies to covered loans, not many borrowers are protected by this provision.

The Model AARP law recommends that in addition to debt-to-income ratios, states should require lenders to look at the borrower's "residual income." Residual income is the amount of money a family has left after paying mortgage, other debts, utilities and work-related expenses. The Department of Veteran's Affairs (VA) has issued regulations for VA loans which set out guidelines for residual income.[78] These guidelines attempt to ensure that the borrower is left with enough income to pay for food, transportation and other basic needs. Maryland's law regarding ability to repay could be improved by requiring lenders to consider residual income in addition to debt-to-income ratios.

Single Premium Credit Life Insurance

The Maryland law prohibits the financing of single premium credit life, health and involuntary unemployment insurance for covered loans. While this provision was needed and follows the lead of many states,[79] the better course of action would be to prohibit the sale of this type of insurance for all real estate loans.[80] Single premium credit life insurance is an insurance product sold by the lender (who generally receives a sizeable commission for selling it) to the borrower and is paid for in one lump sum at the beginning of the loan. The premium cost is added to the principal of the loan, resulting in the borrower paying interest and points on the credit insurance premium. It's unlikely that purchasing a single premium credit insurance policy would make economic sense for any borrower, and the product is sold primarily to unsophisticated consumers who do not understand the exorbitant cost they are paying. A much less expensive option for a borrower is to purchase non-credit life insurance.

Counseling

The last prong of Maryland's predatory lending law is a requirement that at the time of the loan application, the lender must provide the borrower with a written recommendation that the borrower seek home buyer education or counseling and give a list of agencies approved by the county to provide the education or counseling.[81] One of the problems with this provision is that it requires only a written recommendation for counseling, where some of the stronger laws require mandatory counseling before a creditor can make a high cost loan.[82] Another problem with this provision of the law is that there are no "county approved" housing counseling agencies in Maryland. Housing counseling agencies may obtain HUD certification, but there is no certification or approval process on the county level.

Predatory Practices Not Addressed by Maryland's Law

Other states that have enacted predatory mortgage lending laws have imposed additional restrictions and requirements not included in Maryland's predatory lending law. Some of the restrictions are addressed by other Maryland credit laws and those provisions will be noted below, but many important restrictions were not included in Maryland's law. The abusive lending practices that Maryland failed to address are highlighted below.

Financing of Fees

Several states prohibit the financing of fees for high cost loans.[83] Some states have prohibited the financing of points and fees in excess of a certain percent, ranging from 2% to 8%.[84] These types of provision are very important as they increase the likelihood that the lender will recoup the cost of the loan through regular monthly payments, as opposed to including high up-front costs. Current Maryland law prohibits charging points and fees in excess of 10%, which includes any mortgage broker fee, for loans made under the Second Mortgage Law or Subtitle 10.[85] There is no limit on points and fees under the Usury law, however the limit of 8% on broker's fees applies. These limits are very high and should be reduced.

Loan Flipping

Loan flipping is when a loan is refinanced, often several times, with little or no new benefit to the borrower. Each time the loan is refinanced, the borrower pays additional up-front fees, which strips the equity from the borrower's home because the amount owed increases with each refinancing. As long as there is equity in the home the lender benefits every time the borrower refinances. If the borrower, defaults the lender can make a new loan, resulting in additional points and fees (more profit) for the lender. Even if there is no default, predatory lenders often convince borrowers to refinance their loans in order to receive a small amount of additional cash. The lender then obtains a large prepayment penalty in addition to the points and fees for refinancing.[86]

The table below illustrates how multiple refinancings can result in a dramatic loss of equity for a homeowner.[87] In this example, the borrower takes out a $70,000 loan. Three years later, the borrower falls behind and refinances. The refinanced loan effectively costs the borrower another 10% of the loan amount in points, fees and closing costs. Even though the borrower has paid almost $30,000 toward his mortgage in three years, once he refinances, his home equity is dramatically reduced. A subsequent refinancing reduces the homeowner's equity even further.[88]

	ORIGINAL LOAN	REFI #1 @ 3 YEARS	REFI #2 @ 6 YEARS
Value to homeowner	$70,000	$0	$0
Pay off of prior loan		$76,495	$83,107
Loan with 10% points and fees financed	$77,450	$84,145	$91,300
Home Equity lost at loan closing	($7,450)	($14,145)	($21,300)
Total amount paid by homeowner to "achieve" this lost equity		($28,680)	($59,839)

Table 2. Equity Lost In Multiple Refinancings.

North Carolina, New York and Massachusetts have placed limits on refinancings.[89] New York and Massachusetts prohibit points and fees from being charged if a loan is refinanced within 24 months. In North Carolina, a refinanced loan must provide a tangible net benefit.

Maryland law addresses this issue in a very limited way. The Second Mortgage loan law prohibits refinancing more than once during any 12 month period or twice during a 5 year period.[90] Subtitle 10 prohibits the imposition of refinancing charges for second liens more often than once in any 12 month period, if the loan is more than 30 days in default.[91] In addition, the Finder's Fee Act states that a broker who refinances a loan on the same property within two years can only charge a fee for the amount by which the second loan exceeds the prior loan.[92] These limits are not as strong as other state laws or the model law and should be improved.

Assignee Liability

One of the obstacles to helping consumers who have predatory loans is raising violations of the law against subsequent assignees of the loan. Often, the predatory practices are committed by a mortgage originator who may be long gone by the time the consumer realizes the problem. HOEPA extends liability to the assignee of high cost loans for all claims and defenses that the borrower could raise against the originator, while placing limits on the damages that can be awarded against an assignee. [93] A number of states have followed HOEPA's lead and extended liability for assignees.[94] Maryland should follow the example of HOEPA and other states and extend assignee liability for high cost loans.

Prepayment Penalties

Prepayment penalties are provisions in loan contracts that require a significant payment if the loan is paid before maturity. If the borrower wants to refinance the loan or pay off the loan, they will be stuck paying a high fee. Prepayment penalties are virtually non-existent in the prime market, but exist in approximately 80% of subprime loans.[95] Many of the recently enacted state predatory lending laws place limits on prepayment penalties. Maryland law prohibits prepayment penalties for loans made under the Consumer Small Loan Law, the Second Mortgage Law and Subtitle 10.[96] For loans made under the Usury Law, prepayment penalties are prohibited for loans with interest rates in excess of 8%.[97] If the interest rate is less than 8%, prepayment penalties are allowed with certain limits.[98] Maryland law is relatively strong on prepayment penalties – prohibiting them for most loans, not just high cost loans, but this prohibition should be expanded to cover all loans. Unfortunately, some lenders do not have to comply with the Maryland law on prepayment penalties because of federal preemption.[99] Preemption is discussed in detail below at page 17.

Balloon Payments

Balloon payments are a common feature of predatory loans. Some loans are structured so that the monthly payments cover less than the full principal due -- paying interest only or just a small amount toward the principal, leaving a large lump sum payment (the balloon) due at the end of the loan term. Often borrowers are unaware of the balloon at the time they enter into the loan and are then forced into refinancing when the balloon comes due. A number of states have limited balloon payments, particularly early in the loan. The District of Columbia, Connecticut, and New York prohibit balloon payments until 7 years after the loan is made.[100] Illinois and New York prohibit balloon payments until 15 years after loan origination.[101] North Carolina, New Jersey, New Mexico, Kentucky, Massachusetts and Georgia prohibit balloon payments.[102]

Maryland places some limits on balloon payments. The Second Mortgage Loan law prohibits balloon payments except under certain circumstances.[103] Unfortunately, the Court of Appeals has interpreted this section to allow most balloon payments and has held that the lender does not have to give the consumer notice that they may postpone the balloon payment for six months.[104] Subtitle 10 allows balloon payments on loans secured by real property; however, if the loan is a consumer loan secured by a second lien on residential real estate, the borrower is permitted to postpone payment on the balloon for six months.[105] The Consumer Small Loan law prohibits balloon payments on loans unless the loan is payable in full in less than one year.[106] The other credit statutes do not prohibit balloon payments. Maryland law on balloon payments is not very strong relative to other states and should be improved.

Other Provisions

Other states have enacted provisions that restrict mandatory arbitration clauses;[107] prohibit lenders from encouraging borrowers to default on existing loans;[108] require timely delivery of payoff information; prohibit negative amortization;[109] prohibit increasing interest rates after default; prohibit taking payments in advance and prohibit acceleration clauses.[110] These are important provisions that should be considered in order to protect Maryland homeowners.

Federal Preemption of State Laws

No discussion of state lending laws is complete without an examination of federal preemption of state laws. While at first blush it may appear that the federal government has tied the hands of the states to address predatory lending, there is still much states can do to regulate abusive mortgage loans. Traditionally, credit laws including limits on interest rates, points, fees and loan terms were controlled by state law, except for federally chartered institutions. Beginning in 1980, Congress began preempting certain state lending laws in an attempt to make more mortgage money available for home borrowers. [111] Federal preemption is authorized by at least eight different statutes. Whether federal preemption applies to a particular loan depends largely upon the type of lender and/or the type of loan.[112] For the purposes of this report, we provide a brief overview of the statutes that have the greatest impact on a state's ability to address predatory lending and identify areas were states can act to reduce predatory lending. It is important to note that recent surveys in Ohio and Tennessee have found that a large percentage of subprime lenders do not meet federal preemption requirements, so are governed by state predatory lending laws.[113]

Preemption for Federally Chartered Institutions

The National Bank Act ("NBA") allows a national bank to charge either the maximum rate allowed under state law or an alternative federal rate. In 2004, the Office of the Comptroller of the Currency adopted regulations that claim broad preemption of state laws as to national banks. Basically, the regulations preempt all state laws unless the law is only "incidental" to the banking industry. [114] The preemption only applies to national banks and their operating subsidiaries for credit that is initiated by the bank or subsidiary – not to loans assigned to it.[115] Preemption does not apply to state unfair and deceptive practices acts, the uniform commercial code or state anti-discrimination laws.[116] Unfortunately, the OCC has largely preempted state and local regulators from enforcing those state laws that do apply to national banks. [117]

The Home Owners' Loan Act ("HOLA") is similar to the NBA, but applies to federal savings associations.[118] The Office of Thrift Supervision (OTS), which regulates federal thrifts, has interpreted HOLA as preempting all state laws regulating savings associations. [119] OTS has specifically found that state UDAP statutes are *not* preempted. In a small victory for homeowners, the Maryland Court of Appeals found that when a federal savings association stated in its contract that the loan was made under Maryland law, the state law was *not* preempted.[120]

The National Housing Act preempts state laws for FHA and VA Insured loans.[121] The Federal Credit Union Act of 1934 governs federal credit unions and is similar to the NBA and HOLA, however, its preemption of state law is narrower.[122] State laws that do not limit rates, terms of repayment and certain other conditions are not preempted. [123]

Preemption for Federally Insured State Chartered Banks

In 1980, Congress extended the "most favored lender" status granted to national banks to state chartered banks.[124] This action allows state chartered banks to charge the same interest rates as national banks, effectively preempting state interest rate caps. States are still permitted to regulate most substantive provisions of loans made by state chartered banks.[125]

Preemption for Federally Related First Mortgage Loans

The Depository Institutions and Monetary Control Act ("DIDMCA")[126] preempts state usury ceilings on any "federally related" mortgage loan secured by a first lien on residential real property. Because of the broad definition of a federally related loan, virtually all first mortgages are covered, but the scope of preemption is limited. DIDMCA preempts state limits on *interest rates, points, finance charges or "other charges."* DIDMCA applies to purchase money loans and refinanced loans. Some commentators believe that DIDMCA has added to the predatory lending problem by requiring borrowers to refinance existing mortgages in order for the lender to have first lien status and preempt state limits on interest rates. [127]

Preemption for Alternative Mortgage Transactions

Another statute that has a significant impact on the mortgage market is the Alternative Mortgage Transaction Parity Act ("AMTPA").[128] AMTPA, which became effective in 1982, extends federal regulations which previously applied only to federally-chartered lenders to all "housing creditors" that make "alternative mortgage transactions."[129] AMTPA was intended to allow "creative" financing for mortgage loans by preempting state laws limiting variable interest rates, balloon payments and negative amortization.[130] AMTPA does not limit interest rates on mortgages, but instead it deals with the "structure" of mortgage loans.[131] AMTPA only applies to "alternative mortgage transactions," which are generally defined as loans that contain adjustable rates, balloon payments or negative amortization.[132] Commentators point to AMTPA as contributing to the dramatic increase in predatory lending since the early 1980's. [133]

Because of the abuse that occurred after the passage of AMPTA, in 1994, Congress re-regulated to a limited extent high cost loans when it enacted HOEPA. (See discussion of HOEPA at p. 9) If a loan is covered by HOEPA, its provisions and not those of AMTPA will control.[134] In addition, as of 2003, the Office of Thrift Supervision (OTS) removed prepayment penalties and late fees from those items that were preempted under AMTPA, thus allowing states to regulate these items for lenders who are not federally chartered.[135]

State Action in the Wake of Federal Preemption

While federal preemption is broader than many commentators believe is proper, it does not completely limit a state's ability to address predatory lending within its borders.[136] States are largely prohibited from regulating national banks and federally chartered savings associations and credit unions, and their operating subsidiaries, most subprime lenders do not fall into this category. State limits on interest rates, points and fees on first mortgages are largely preempted by DIDMCA, however, this preemption does not apply to junior liens and does not preempt state laws addressing other loan terms and conditions. Also, DIDMCA does not apply to some small lenders, home improvement contractors or brokers.[137]

While AMTPA applies broadly to all "housing creditors," and gives the creditor the option to follow federal regulations instead of state law, its provisions only apply to "alternative mortgage products" and it does not preempt state limits on prepayment penalties or late fees.[138] In addition, state unfair and deceptive practices laws are generally not preempted by federal law, allowing actions against lenders for fraudulent and deceptive conduct.

A large percentage of subprime loans are originated by non-bank lenders or mortgage brokers.[139] Most of the leading subprime lenders are mortgage companies and finance companies.[140] For many of these transactions, states can regulate various terms and conditions of the loans and can place restrictions on the abusive predatory practices described above. In addition, a recent study has found that state predatory lending laws have been effective in reducing predatory lending, particularly in those states with strong laws.[141] The findings of the study support decisive state action to address predatory lending in order to protect homeowners, in spite of preemption.

Foreclosures In Maryland

Foreclosures have skyrocketed over the past 20 years, increasing 335% from 1998 to 2003.[142] This dramatic increase has been linked directly to the increase in subprime lending. Unfortunately, this increase in foreclosures has not led to any significant change in foreclosure law, which remains largely unchanged since the 1800's. In stark contrast to other laws that protect consumers when they are being deprived of property, foreclosure laws in Maryland and many other states allow foreclosure sales of homes with minimal notice and limited conditions upon which a sale can be stayed. [143]

Causes of Foreclosure

According to the advocates and officials we spoke with, the reasons that individuals find themselves facing foreclosure, can be generally classified into certain categories.

- Loss of income due to illness, job loss or divorce
- Unaffordable loan and/or predatory loan terms
- Unexpected expenses such as property repairs, or medical expenses
- Refinancing of prior loan with no escrow for taxes
- Servicing abuses – unreasonable late fees, forced placed insurance, inspection fees, etc. added to amount due which makes it difficult to bring account current

The Foreclosure Process

Foreclosure is the process by which the holder of a mortgage or deed of trust sells the real estate used as collateral for the loan. Foreclosure procedures are a matter of state law and vary state by state. In one-half of the states, foreclosures are by judicial action. [144] The other half are "power of sale" states, in which there is little or no supervision of foreclosures by the courts.[145]

In Maryland, the foreclosure process is summary in nature.[146] Virtually all mortgages are foreclosed pursuant to a "power of sale" or an "assent to decree."[147] A "power of sale" or "assent to decree," are clauses in mortgages or deeds of trust that state that upon default, the borrower agrees to the entry of an *ex parte* order to sell the property.[148] *Ex parte* means there is no service of process on the borrower as required in most judicial proceedings.

In Maryland, with either a "power of sale" or "assent to decree," a foreclosure proceeding must be filed in the circuit court for the county in which the property is located.[149] The foreclosure action is considered an "in rem" proceeding – the court takes jurisdiction over the property, not over the borrower.[150] In the very rare case that a mortgage does not contain either a "power of sale" or an "assent to decree," the holder must proceed by strict foreclosure (also known as judicial foreclosure), which requires that all interested parties be served, a hearing held, and that a judge order the foreclosure sale to take place.

Limited Notice to Homeowner

Under a "power of sale" or "assent to decree" foreclosure, there is no court initiated notice to the borrower or service of process on the borrower. In fact, the foreclosure process is similar to the entry of a confessed judgment, which allows entry of a judgment without notice and a hearing.[151] Confessed judgments have been largely prohibited by law in consumer contracts. In fact, tenants in Maryland enjoy greater protections from eviction than a homeowner has in foreclosure.[152]

Prior to May 26, 2005, the only notice of the foreclosure sale required by state law was sent to the borrower "not earlier than thirty days and not less than 10 days before the date of the sale."[153] The notice is sent by first class mail and certified mail by the attorney for the mortgage holder. No notice of sale is sent to the borrower from the court. Consequently, many borrowers did not realize that their house was being sold until a few days before the sale.[154]

As of May 2005, the mortgage holder is required to send an additional notice to the borrower no later than 2 days after the foreclosure action is filed.[155] While this additional notice provision is an improvement over the prior notice requirements, it still is problematic. A sale can be held as quickly as 15 days after the foreclosure action is filed, leaving little time for a borrower to respond to the notice.[156] This notice is also sent by the lender or its agent, and is not an official court notice, making the borrower less likely to take the notice seriously. Even if a homeowner immediately finds a housing counselor to help him, the loss mitigation process with most lenders takes 30 to 45 days, leaving the counselor with too little time to negotiate a workout agreement.

The limited notice given to borrowers makes it difficult for them to garner the resources necessary to stop a sale – either by paying the debt or by hiring an attorney to challenge the lender's entitlement to proceed with a sale. In addition, under a "power of sale" or "assent to decree", there is no court hearing scheduled to determine if the foreclosure sale is appropriate. The only avenue to challenge the foreclosure sale is to file an injunction prior to the sale (which requires depositing all amounts due with the court), by exceptions filed after the sale or by an objection to the audit.[157] All of these options provide only limited grounds upon which a sale can be challenged. For example, the Court of Appeals has held that usury is not a basis upon which a foreclosure sale can be set aside and neither is the failure to provide the homeowner with an accurate statement of the amount needed to redeem the property.[158] Challenging a foreclosure sale in court is time consuming, expensive and not a realistic option for most homeowners facing foreclosure.

The lack of notice until after foreclosure proceedings have been filed means that the amount needed to bring the account current has risen significantly because of attorneys fees and other costs that are added to the amount due. This makes it even more difficult for a homeowner to bring the account current as they must come up with $2,000 to $3,000 in attorney's fees and costs, in addition to the arrears due. There has been discussion of implementing statewide rules limiting trustee's fees and auctioneer fees in foreclosure cases, but as of this date, no rules have been adopted. [159] In addition, there has been concern about auctioneer fees in Baltimore City and whether auctioneers have been routinely over-billing for advertising costs in foreclosure cases.[160] Because of the potential for abuse in the costs charged in foreclosure proceedings and the minimal oversight of this process by the courts, there should be rules that prevent overreaching by the parties involved.

Due Process Challenges

There have been numerous due process challenges to "power of sale" foreclosures around the country, under the theory that the homeowner is being deprived of a significant property right without adequate notice and a meaningful opportunity for a hearing.[161] In 1980, the Maryland Court of Appeals upheld the constitutionality of "power of sale" foreclosures in Maryland.[162] However, this may be an issue ripe for reconsideration, since the Court of Appeals has recently held that an erroneous demand for payment does not provide a grounds to overturn a sale, and the only way to stop a sale is the extraordinary remedy of injunctive relief, which requires a deposit of all amounts due.

The arcane process of foreclosure is not understood by the average homeowner.[163] Many borrowers expect that they will receive a hearing in court where they can raise defenses to the foreclosure. Borrowers do not understand how fast the process is; do not know the sale date until a few days before the sale; and do not understand that they have no right to redeem after the sale.[164]

Common Difficulties in Preventing Foreclosures

In our conversations with housing counselors and other advocates that advise consumers facing foreclosures, several common barriers emerged as making it difficult to prevent foreclosures. Problems cited include:

- **Inadequate notice** – The limited notice of foreclosure that homeowners receive contributes to high foreclosure rates. By the time a homeowner reaches a counselor, it is often too late to negotiate a workout. The late notice also means that significant fees have already been incurred by the time the homeowner receive notice. If homeowners had earlier notice and contacted counselors sooner, they would have a much better chance of preventing foreclosure.
- High foreclosure costs – Overreaching by attorneys, auctioneers, advertisers and others in the foreclosure process results in significant fees, some of which are not justified. These costs make it difficult for homeowners to bring their mortgages current.165
- **Limited judicial review –** The process for challenging a foreclosure sale is expensive and time consuming and the grounds for enjoining a foreclosure sale are very limited. Further, the requirement that all amounts due must be paid into court make it virtually impossible for most homeowners to obtain an injunction.
- **Uncooperative lenders –** Mortgage companies and servicers can be difficult to deal with for homeowners and advocates alike. It can be hard to get adequate payoff information or records of payments made on the account, partly because mortgages tend to change hands frequently. The mortgage companies seem to have little incentive to enter into workout agreements, according to advocates.
- **Failure to comply with servicing requirements** – Federally guaranteed loans require lenders to follow specific procedures upon a borrowers default as a prerequisite to initiating foreclosure yet few lenders follow the procedures.

The Basic Foreclosure Process In Maryland

- Lender sends acceleration letter to borrower
- Lender files Petition to Foreclose or Order to Docket (depending on whether proceeding under an “assent to decree” or “power of sale”)
- Lender sends notice to borrower within 2 days of filing the action (required as of May 2005)
- Sale must be advertised once each week for three weeks
- Notice of sale date sent to borrower not less than 10 days nor more than 30 days before sale
- The sale of the property is held
- The court is notified of the sale
- The court enters an order setting a date for exceptions to be filed
- If no exceptions are filed, a final order of ratification is entered by the court
- Settlement takes place with the buyer
- The trustee reports the sale to a court appointed auditor
- The auditor issues a final accounting
- If there are no objections to the accounting, sale is ratified
- If there is a deficiency, the lender has 3 years to file a notice of deficiency and obtain a deficiency judgment.

Foreclosure Rescue Scams

In a sad commentary on our society, an offshoot of the explosive increase in foreclosures is a new scam aimed at vulnerable homeowners facing foreclosure, commonly referred to as "foreclosure rescue fraud."[166] These frauds generally happen as follows: a "foreclosure consultant" contacts a homeowner facing foreclosure and offers to help stop the foreclosure; the consultant has the homeowner sign documents transferring title to the home to the consultant (generally unbeknownst to the homeowner); the consultant pays the arrears to the mortgage company and the homeowner makes payments to the consultant, not realizing that they no longer have an ownership interest in the property. Eventually, the consultant evicts the homeowner, when the homeowner cannot meet the onerous repayment obligations. There are several variations on the fraud, but they all result in the homeowner losing their home and the equity in it.[167]

Maryland was one of the first states to address this issue by enacting a comprehensive foreclosure rescue fraud statute in 2005.[168] One of the provisions of the bill is a new notice requirement that requires the person foreclosing to send written notice to the owner within 2 days after the foreclosure action is docketed.[169] The notice includes a warning about scam artists and provides the telephone number for the Consumer Protection Division of the Attorney General's office. The division is charged with referring callers to non-profit counseling agencies that assist consumers with foreclosure prevention. The statute provides numerous protections for homeowners, including:

- The right to rescind a foreclosure consulting contract at any time;
- The right to rescind a foreclosure reconveyance within three business days after the transfer or conveyance;
- Requiring that a contract be given to the homeowner that specifies the terms of the foreclosure consulting agreement, gives notice of rescission rights, and contains warnings that the homeowner should consult an attorney before signing;
- Limiting interest on any loan made by the consultant to the homeowner to 8%;
- Prohibiting the consultant from acquiring an interest in the property being foreclosed;
- Prohibiting the consultant from obtaining a power of attorney from a homeowner;
- Requiring a separate notice to the homeowner if the title to the property is being transferred.
- Requiring the homeowner to receive at least 82% of the net proceeds of any resale of the property.170

The foreclosure rescue law does not apply to attorneys, banks or their affiliates, title insurers, licensed mortgage brokers or lenders, real estate brokers or certain non-profit organizations unless the individual is engaging in activities intended to transfer title to that individual.[171] The law provides for enforcement by the Attorney General and allows for a private action for damages by homeowners, including a right to attorney's fees and treble damages.[172]

Recommendations

To effectively reduce foreclosures and keep homeowners in their homes for the long run, we need a multi-prong approach. First, we need to reduce predatory lending and servicing abuses by enacting strong laws that apply broadly to the subprime market and prohibit the abusive terms and features of many predatory loans as well as predatory servicing practices. Second, we need to improve the foreclosure process so consumers have better and earlier notice and the opportunity to redeem prior to significant costs being incurred. Limits on fees charged in connection with foreclosures should be considered. Homeowners also need to have easier access to the court system to raise defenses they may have against the lender. Payment in full of all amounts due under the loan cannot be the admission price for relief from the courts. Third, we need to provide comprehensive help to those facing foreclosure – as early in the process as possible.

Enact A Strong State Predatory Lending Law

The law that Maryland passed in 2002 is one of the weaker of the predatory lending laws that has been enacted around the country. We need to improve our law in the following ways:

- Lower the triggers for coverage under the predatory lending law in order to cover more loans.
- Limit the financing of points and fees.
- Extend assignee liability for high cost loans.
- Expand coverage of the predatory lending law to include open-end loans and purchase money loans.
- Reduce the 8% limit on mortgage brokers' fees.
- Limit fees that can be charged when refinancing loans within three years.
- Require lender to consider residual income when determining ability to pay.
- Limit balloon payments for all mortgage loans.
- Limit pre-payment penalties for all mortgage loans.
- Prohibit single premium credit life insurance for all mortgage loans.
- Require mandatory counseling before certain high cost loans can be made.
- Limit the ability of loan servicers to add charges without notice and an opportunity for the homeowner to contest the charges.

Improve the Foreclosure Process

While a substantial overhaul of the foreclosure process is not likely, a few relatively simple steps could make the process more equitable. Several suggested changes are outlined below:

- Require the lender to refer a homeowner who is 45 days past due to a non-profit counseling agency or a hotline that can help the borrower to negotiate a workout agreement with the lender.[173]
- Require the lender to give notice to the homeowner of the amount past due and the amount needed to redeem, prior to the imposition of fees and costs for foreclosure.
- Require the lender to give the homeowner 30 days from the date of the notice of delinquency to bring the account current.

- Require the court to send notice of foreclosure filings to the homeowner and provide homeowners with a meaningful opportunity to raise challenges to the sale.
- Expand the grounds upon which a sale can be challenged.
- Implement rules limiting trustee's fees, auctioneer's fees and advertising fees in foreclosure cases.
- Require judicial foreclosure for certain high cost loans.

Provide Comprehensive Help to Those Facing Foreclosure

Resources for homeowners facing foreclosure need to be improved. Individuals whose homes are in foreclosure are often referred from place to place, unable to find help.[174] Existing housing counseling agencies that focus on homeownership need to devote more resources to helping struggling homeowners. Legal services attorneys, the private bar and housing counselors need to work together to find the resources necessary to represent those who are the victims of predatory lending. We need to develop a comprehensive referral network for those facing foreclosure.

We need to improve education and outreach to homeowners, to try to reach individuals who are having difficulty paying their mortgage, before the situation becomes critical. Early intervention will make it easier to help homeowners prevent foreclosure. If a homeowner does not get help until he is three months behind on his mortgage and substantial foreclosure costs have been incurred, it makes it very difficult to save his home.

We should also consider providing financial help to homeowners who get behind on their mortgage through no fault of their own. Over the course of a 30 year mortgage, it is not unusual for homeowners to face financial difficulties, such as a job loss, health crisis, or unexpected emergency repairs to their home, that cause them to fall behind on their mortgage. Homeowners need help overcoming temporary, but difficult, financial situations, however, there are very few resources to help those homeowners.[175] In the 1980's, Maryland's, Homeownership Emergency Mortgage Assistance Program (HEMAP), provided assistance to homeowners who fell behind on their mortgage payments due to no fault of their own. The HEMAP program assisted many homeowners who had nowhere else to turn and Maryland should consider creating a similar program to provide a valuable safety net for homeowners.[176]

NOTES

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[1] Downey, Kristin, *Mortgage Stress Seen for '06*, WahsingtonPost.com (December 7, 2005).

[2] Id.; Herman, Charlie, *Housing Woes: Interest Rate Increases and Foreclosures*, ABCNews.com (March 21, 2006).

[3] Id.

[4] Hill, Patrice, *Regulators Target Mortgage Bankers,* Washington Times (December 21, 2005).

[5] Waldron, *Self -Help, Leading the Charge Against Predatory Lending*, p. 41, Advocasey (Winter 2005); Forrester, Julia, *Still Mortgaging the American Dream: Predatory Lending, Preemption and Federally Supported Lenders*, p. 18, Berkeley Electronic Press (2005).

[6] *Baltimore City Flipping and Predatory Lending Task Force, Final Report 2005*.

[7] Quercia, Stegman & Davis, The Impact of Predatory Loan Terms on Subprime Foreclosures: The Special Case of Prepayment Penalties and Balloon Payments, p. 3-4 (2005).

[8] National Consumer Law Center, *Stop Predatory Lending: A Guide for Legal Advocates*, p. 16 (2002). [Hereinafter, NCLC, *Stop Predatory Lending*.]

[9] Id.

[10] Ho & Pennington-Cross, *The Impact of Local Predatory Lending Laws*, p. 3 (June 2005).

[11] NCLC, *Stop Predatory Lending*, p. 25.

[12] Forrester, Julia, *supra* note 5, p. 43.

[13] HUD, *Unequal Burden: Income and Racial Disparities in Subprime Lending in America* (April 2000)

[14] Id.

[15] Smitherman, Laura, *Ad drive focues on lender ruses,* The Baltimore Sun (Dec. 13, 2005).

[16] Saunders & Cohen, *Federal Regulation of Consumer Credit: The Cause or Cure for Predatory Lending?*, p. 11 (March 2004).

[17] Id.

[18] Id.

[19] Mortgage Bankers Association, *National Delinquency Survey, Fourth Quarter 2005*,

p. 5

[20] Id.

[21] HUD, *Unequal Burden in Baltimore: Income and Racial Disparities in Subprime Lending*. p. 8 (May 2000).

[22] Id.

[23] Id.

[24] For an overview of credit laws in Maryland including those for non-real estate loans see, Corwin, *A Road Map Through Maryland's Consumer Credit Laws*, 35 Maryland Bar Journal 31 (2002).

[25] "Open-end" credit is an agreement to extend credit from time to time with no set number of payments or payment amounts. Bank credit cards and home equity loans are examples of open-end credit.

[26] Closed-end credit is a single extension of credit which is paid off in specified amounts in a fixed period of time. Automobile loans and purchase money real estate loans are usually closed-end transactions.

[27] Corwin, *supra* note 23, p. 32.

[28] Maryland Annotated Code, Commercial Law Article (CL) §§12-913, 12-913.1, 12-1013, 12-1013.1.

[29] CL §12-103(3).

[30] Corwin, *supra* note 23, p. 32.

[31] Annotated Code of Maryland, Financial Institutions Article (FI), §11-504.

[32] FI §11-502.

[33] FI §11-515, §11-517.

[34] Loan servicers act on behalf of the lender by accepting payments on the loan, handling escrow accounts and otherwise performing the duties of the lender, but the servicer is not the owner of the loan. FI §11-501.

[35] Childs, Christopher R., *So You've Been Preempted – What Are You Going To Do Now?: Solutions for States Following Federal Preemption of State Predatory Lending Statutes,* 2004 Bringham Young Univ. Law Review 701 (2004).

[36] CL §§12-801 – 12-808.

[37] CL §12-805(d).

[38] CL §8-12-804(a).

[39] CL §12-804(c).

[40] CL §12-804(e).

[41] *Sweeny v. Savings First Mortgage*, 388 Md. 319, 879 A.2d 1037 (2005).

[42] House Bill 1040, 2005 General Assembly Session; codified at Financial Institutions Article, §§11-601, et seq.

[43] FI §11-613.

[44] FI §11-607; §11-615.

[45] FI §11-605.

[46] 15 U.S.C. §1639.

[47] National Consumer Law Center, Foreclosures, p. 106 (1st ed. 2005). [Hereinafter, NCLC, *Foreclosures.*]

[48] NCLC, *Stop Predatory Lending*, p. 45

[49] Id.

[50] Id. at 46.

[51] Id. at 47.

[52] Id. at 48.

[53] Id. at 46-47.

[54] Forrester, *supra* note 5, page 21 – 22.

[55] Ho & Pennington-Cross, *supra* note 10, p. 11.

[56] Waldron, *supra* note 5, p.41; Conference of State Bank Regulators, *State Initiatives to Battle Predatory Lending*, p. 12 (2000); National Consumer Law Center, *The Cost of Credit: Regulation and Legal Challenges,* p. 641 (2005) [Hereinafter, NCLC, *Cost of Credit*]; Peterson, Christopher L., *Federalism and Predatory Lending: Unmasking the Deregulation Agenda*, 78 Temple University Law Review 1, p.66 (2005).

[57] AARP, ACORN, Maryland Center for Community Development and the Maryland Consumer Rights Coalition all requested that then Governor Parris Glendening veto the bill. The Governor signed the bill on May16, 2002.

[58] Craig, Tim, *Protesters upset about bill on loan oversight,* The Baltimore Sun (Feb. 15, 2002).

[59] AARP, Home Loan Protection Act: A Model State Statute (November 2001).

[60] Craig, Tim, *supra* note 58.

[61] CL §12-124.1, §12-311, §12-409.1, §12-1007. As explained in the previous section, Maryland's regulation of mortgage related loans is covered by several different subtitles of the Commercial Law Article, so each of the applicable subtitles was amended by HB 649.

[62] CL §12-124.1, §12-312, §12-410, §12-1007.

[63] CL §12-124.1, §12-311, §12-409.1, §12-1029.

[64] CL §12-127, §12-311, §12-409.1, §12-1029.

[65] Id.

[66] Id.

[67] Montgomery County Code, §27-12(c).

[68] Id.

[69] Jarboe, Kathleen Johnston, *Montgomery lending law on hold* , The Daily Record (March 8, 2006).

[70] See, Ho & Pennington-Cross, supra note 10, Appx. A, for a comprehensive comparison of Predatory Lending Laws. States and localities that have expanded the coverage beyond refinanced closed end loans include: Arkansas, California, Chicago, Cleveland, Connecticut, Georgia, Massachusetts, New Jersey, New Mexico, New York, and the District of Columbia.

[71] AARP, Home Loan Protection Act, *supra* note 59, p. 8, 11 (November 2001).

[72] On of March 15, 2006 the applicable Treasury Rate was 4.75%. See www.federalreserve.gov for a listing of Treasury Security rates.

[73] Several states and localities have APR triggers of 6% for first liens and 8% for junior liens. See, Illinois, Chicago. Some jurisdictions have set the points and fees trigger at 5%. See, Georgia, Indiana, Connecticut, Massachusetts, New York, North Carolina, South Carolina, District of Columbia. Ho & Pennington-Cross, supra note 10, Appx. A.

[74] CL §12-127; §12-311; §12-409.1; §12-1029.

[75] Id.

[76] Id.

[77] North Carolina, Massachusetts, Illinois, New York, Georgia, New Jersey have similar ability to repay tests, except that their debt to income ratio is 50%. Ho & Pennington-Cross, supra note 10, Appx. A.

[78] AARP, Home Loan Protection Act, *supra* note 59, p. 24.

[79] Arkansas, California, Colorado, Illinois, Indiana, Kentucky, Nevada, New Jersey, New Mexico, New York, Ohio, Utah, District of Columbia, and Wisconsin all prohibit the financing of single premium credit insurance for covered loans. Ho & Pennington-Cross, supra note 10, Appx. A.

[80] The following states have prohibited single premium insurance for all home related loans: Georgia, Massachusetts, North Carolina, South Carolina and Texas. Ho & Pennington-Cross, supra note 10, Appx. A

[81] CL §12-127(c); §12-311(e); §12-409.1(c); §12-1029(c).

[82] Arkansas, Georgia, Indiana, Massachusetts, New Jersey, New Mexico, New York, North Carolina, and South Carolina all require counseling before a covered loan can be made. Ho & Pennington-Cross, supra note 10, Appx. A.

[83] North Carolina, Arkansas, Indiana, Pennsylvania. Ho & Pennington-Cross, supra note 10, Appx. A.

[84] California (6%), Illinois (6%), Kentucky (4%), Massachusetts (5%) New Jersey (2%), New Mexico (2%), New York (3%), South Carolina (2.5%), Utah (8%). Ho & Pennington-Cross, supra note 10, Appx. A.

[85] CL §12-405; §12-1005.

[86] Ackelsberg, Irv & Saunders, Margot, *Increase in Predatory Lending and Appropriate Remedial Actions*, Testimony before the Senate Committee on Banking, Housing and Urban Affairs (July 27, 2001).

[87] Id. Table reprinted with permission of the National Consumer Law Center.

[88] The example assumes that the value of the home has stayed the same.

[89] AARP, Home Loan Protection Act, *supra* note 59, p. 19.

[90] CL §12-408.

[91] CL §12-1010.

[92] CL §12-804(c).

[93] National Consumer Law Center, *Truth In Lending*, p.629 (2005).

[94] Arkansas, Colorado, Florida, Georgia, Illinois, Kentucky, Massachusetts, Nevada, New Jersey, New Mexico, New York, North Carolina, and South Carolina provide for assignee liability. Ho & Pennington-Cross, supra note 10, Appx. A.

[95] NCLC, *Foreclosures,* p.7.

[96] CL §12-311(c); §12-407(d); §12-1009(e).

[97] CL §12-103 (b).

[98] CL §12-105(b). Legislation was introduced in the 2006 session of the Maryland General Assembly that would have prohibited prepayment penalties for loans made under the Usury Law. The legislation was defeated in committee. H.B. 216, 2006 Session.

[99] In *National City Bank of Indiana v. Turnbaugh*, 367 F.Supp. 2nd 805 (D.Md. 2005), the court found that Maryland limits on prepayment penalties are preempted by federal law for operating subsidiaries of national banks.

[100] Ho & Pennington-Cross, supra note 10, Appx. A.

[101] Id.

[102] Id.

[103] CL §12-404(c).

[104] *Drew v. First Guaranty Mortg. Corp.*, 379 Md. 318, 842 A2d 1 (2003).

[105] CL §12-1003(c).

[106] CL §12-306.

[107] New York, New Mexico, Kentucky, Arkansas, and Georgia have enacted these provisions. NCLC, *The Cost of Credit,* p.638 - 641.

[108] New York, New Jersey, Kentucky, Arkansas, and Georgia have addressed this issue. NCLC, *The Cost of Credit,* p. 638 - 641.

[109] North Carolina. NCLC, *The Cost of Credit,* p. 638 - 641.

[110] New Jersey. National Consumer Law Center, *The Cost of Credit,* p. 640 (2005).

[111] See, Forrester, Julia, *supra* note 5, p. 7, 46.

[112] See, NCLC, *The Cost of Credit,* p. 41.

[113] Conversation with Uriah King, Center for Responsible Lending, January 25, 2006.

[114] NCLC, *Cost of Credit,* p. 74.

[115] Id. at p. 76.

[116] Id.

[117] Id. at p. 77.

[118] Id. at p. 41.

[119] Id.

[120] *Wells v. Chevy Chase Bank*, 377 Md. 197, 832 A.2d 812 (2003).

[121] NCLC, *The Cost of Credit,* p. 42.

[122] Id. at p. 85-86.

[123] Id. at p. 86.

[124] NCLC, *The Cost of Credit,* p. 88.

[125] Id.

[126] Pub. L. No. 96-211, 94 Stat. 161 (1980) (codified in various sections of Title 12 of the U.S. Code).

[127] Forrester, Julia, *supra* note 5, p. 48.

[128] 12 U.S.C. § 3803.

[129] NCLC, *The Cost of Credit,* p.108-109.

[130] Id.

[131] Id.

[132] Id.

[133] Id. at p.110; Forrester, Julia, *supra* note 5, p. 7, 49.

[134] NCLC, *The Cost of Credit,* note 60, p. 110.

[135] Id.

[136] Forrester, Julia, *supra* note 5; Mierzwinski, Edmund, *Preemption of State Consumer Laws: Federal Interference is a Market Failure,* Government, Law and Policy Journal, New York State Bar Association, Vol. 6, No.1 (2004).

[137] NCLC, *The Cost of Credit,* p.47; *Sweeney v. Savings First Mortgage,* 388 Md. 319, 879 A.2d 1037 (2005).

[138] NCLC, *Cost of Credit,* p. 110.

[139] Childs, Christopher R., *supra* note 35.

[140] Id.

[141] Li & Ernst, *The Best Value in the Subprime Market, State Predatory Lending Reforms,* The Center for Responsible Lending (Feb. 23, 2006) [Available at www.responsiblelending.org.]

[142] Saunders & Cohen, *supra* note 16, p. 11.

[143] NCLC, *Stop Predatory Lending*, p. 66.

[144] NCLC, *Foreclosures,* p. 65.

[145] Id. at p. 66.

[146] Gordon, Alexander, IV, *Gordon on Maryland Foreclosures*, p. 23 (4th Ed. 2004); *G.E. Capitol Mortgage Services, Inc. v. Levenson*, 338 Md. 227, 657 A.2d 1170 (1995).

[147] Gordon, Alexander, IV, *supra* note 146, p.17-18.

[148] Id.

[149] Id.

[150] Id. at p. 5.

[151] Id. at p. 17.

[152] Real Property Article §8-401. Tenants have the right to service of process, a hearing, right of redemption, right to place rents in escrow for certain disputes with landlords, among other protections. Thanks to Scott Borison, Esq. for his written comments on this issue.

[153] Real Property Article §7-105. Certain types of loans may require notice of default be sent to the borrower prior to initiating foreclosure, for example HUD insured mortgages require a notice of default be sent to the borrower. NCLC, *Foreclosures*, p. 52. Borrowers whose loans are held by Federal National Mortgage Association (Fannie Mae) are entitled to 30 days notice prior to acceleration. Gordon, Alexander, IV, *supra* note 146, p. 23.

[154] Conversations with housing counselors and attorneys that represent consumers facing foreclosure confirm that many consumers do not realize that their house will be sold until few days before the foreclosure sale.

[155] Real Property Article § 7-105.

[156] Gordon, Alexander, IV, *supra* note 146, p. 23*; G.E. Capitol Mortgage Services, Inc. v. Levenson*, *supra* note 146.

[157] Gordon, Alexander, IV, *supra* note 146, p. 23-24.

[158] Id. at p. 1133-1134; *Greenbriar Condominium v. Brooks*, 387 Md. 683, 878 A.2d 528 (2005).

[159] Id. at p. 1315.

[160] Id. at p. 1325-1332.

[161] NCLC, *Foreclosures,* p. 77

[162] Gordon, Alexander, IV, *supra* note 146, p. 59.

[163] Id. at p.15; Conversations with advocates.

[164] Gordon, Alexander, IV, *supra* note 146 at p. 23.

[165] A class action lawsuit which alleged over charging for foreclosure related fees by a law firm that handles a high volume of foreclosure cases in Maryland was settled favorable to consumers in 2005. *Dave Shorb, et al. v. Draper & Goldberg*, *PLLC,* Case No. 10- C-04-002942, Circuit Court for Frederick County, Maryland. More information on the settlement can be found at www.dgsettlement.com.

[166] NCLC, *Foreclosures,* p. 91

[167] See, Id. at 91- 95 for a discussion of the various scams.

[168] Id. at 95. Real Property Article, §§ 7-105, 7-301 - 7-315.

[169] Real Property Article §7-105.

[170] Real Property Article §7-303 - §7-315.

[171] Real Property Article §7-302.

[172] Real Property Article §7-319; §7-320

[173] National Consumer Law Center, *Proposal for Predatory Mortgage Reform,* p. 7, (February 23, 2000); Minnesota has mandated notice of a hotline for homeowners. Collins, J. Michael & Gorey, Rochell Nawrocki, *Analyzing Elements of Leading Default Intervention Programs,* PolicyLab, p.11 (2005).

[174] Conversations with advocates and individual homeowners.

[175] The HELP program was created in Baltimore City to help victims of predatory lending refinance their predatory loans, but for various reasons, the number of homeowners it has been able to assist has been limited.

[176] Pennsylvania currently has a successful HEMAP program. The Reinvestment Fund, *Mortgage Foreclosure Filings in Pennsylvania*, p. 79–80 (2002).