

CONSUMER GROUPS: FIX BANKRUPTCY LAWS SO HUNDREDS OF THOUSANDS OF AMERICANS CAN AVOID HOME FORECLOSURES IN SUBPRIME MORTGAGE CRISIS

81 Percent of Bankruptcy Attorneys Say It's Now Tougher for Clients to Keep Homes Under 2005 Bankruptcy Law Changes; Adding Insult to Injury: Rich Americans Get Break to Save 2nd and 3rd Homes.

WASHINGTON, D.C.//April 12, 2007//Bankruptcy law changes are needed if hundreds of thousands of American families struggling with abusive subprime mortgages are going to escape foreclosure and the loss of up to \$164 billion in home-based wealth, according to a joint call for Congressional action issued today by the National Association of Consumer Bankruptcy Attorneys (NACBA), the Consumer Federation of America (CFA) and the Center for Responsible Lending (CRL). NACBA also released the findings of a national survey of nearly 650 bankruptcy attorneys showing a sharp rise in subprime mortgage-related problems concurrent with controversial 2005 changes to federal bankruptcy laws.

The three consumer groups warned that -- while primarily low-income subprime mortgage borrowers face often insurmountable bankruptcy hurdles to hold onto their homes -- high-income individuals in bankruptcy court get preferential treatment when they seek to save second and third homes.

As the joint statement notes: "The only chance many of these (subprime) borrowers have is through declaring bankruptcy. The problem is that as currently enacted, the Bankruptcy Code favors home mortgage lenders over virtually all other secured and unsecured creditors. The amendment disfavoring protection of the debtor's principal residence was added at a time -- 1978 -- when home mortgages were nearly all fixed-interest rate instruments with low loan-to-value ratios and were rarely themselves the source of a family's financial distress. As a result, bankruptcy law singled out the home mortgage loan as the major debt for which the bankruptcy court is powerless to provide relief. Since that time, the mortgage market has shifted considerably. Subprime lending practices of the last six years, which have relied on property appreciation, and in many cases appraisal fraud, have left many borrowers with mortgages larger than the value of their homes. If the borrowers cannot restructure these debts, then they cannot get back on their feet financially."

Commenting on the findings, Philadelphia bankruptcy attorney and NACBA President Henry Sommer said: "Help is urgently needed for hundreds of thousands of American families at risk of losing their homes due to abusive home loans. For most of these families, bankruptcy is the only viable option to save their home, and this option will be available only if the Bankruptcy Code is revised to eliminate or limit the provisions that exclude home loans from bankruptcy protection. This current exclusion is contrary to sound policy, and operates to disadvantage low wealth and middle income borrowers as compared to debtors with the wealth to own more than one home."

Allen Fishbein, director of housing and credit policy of the Consumer Federation of America, said: "Two million or more homeowners face foreclosure over the next few years, with many of these resulting from negligent and reckless lending practices by mortgage originators. A sizable number of borrowers find themselves in this situation because their mortgages are larger than the current

value of their homes. Modifying the bankruptcy laws to permit the write down of certain toxic mortgages would provide a critical life-line for these at-risk families to hang on to their homes. We urge the Congress to act.”

Eric Stein, chief operating officer of Self-Help and senior vice president of the Center for Responsible Lending, said: "The purpose of bankruptcy is to give troubled families a chance for a fresh start. Today we have an epidemic of homeowners who are in serious financial trouble, and whose houses are worth less than the balance due on their loans because of the irresponsible lending practices of subprime lenders. To make matters worse, bankruptcy laws will actually prevent these families from recovering. Subprime loans have pushed millions of households under water; unless Congress makes some common-sense changes, our current laws will ensure that they drown."

OVERVIEW OF CALL TO ACTION

As 2006 drew to a close, 2.2 million households in the subprime market had either lost their homes to foreclosure or held subprime mortgages that likely will fail over the next several years absent intervention. These foreclosures will cost these families their homes, along with up to \$164 billion in lost wealth. For increasing numbers of borrowers, foreclosure is the only option available. Lehman Brothers has estimated that 30 percent of subprime loans originated in 2006 will end in foreclosure. The joint statement recommends a wide range of specific bankruptcy law changes, including the following:

- ***End the Bankruptcy Code’s special treatment of home mortgage loans.*** As the joint statement notes: “In order to address problems resulting from the Code’s disempowerment of bankruptcy judges to modify home mortgage debt, Congress should eliminate the exception, putting home mortgage loans in parity with other secured debt.” This step also will put middle class homeowners in parity with wealthy debtors, who currently are able to save second and third homes in bankruptcy because they fall outside the currently restrictive mortgage provisions that apply only to primary residences.
- ***Remove time-consuming credit counseling requirements.*** “As a result of the 2005 amendments to the Bankruptcy Code, there are now several hurdles a debtor must clear in order to file for chapter 13 bankruptcy, as Credit Suisse notes in its analysis of the impact of the 2005 amendments on subprime borrowers and the subprime market. For example, as a result of the 2005 amendments, an individual cannot even meet the definition of a ‘debtor’ (and so cannot file for bankruptcy) without first receiving credit counseling from an approved credit-counseling agency. Requirements like these cost precious time, which a borrower facing foreclosure cannot afford to lose, and were clearly not designed for dealing with an immediate crisis regarding the borrower’s home ... The remedy to the counseling requirement is simply to eliminate it for debtors facing foreclosure.”
- ***Curb excessive fees during bankruptcy.*** “Another necessary change is a provision to control the enormous problem of mortgage companies adding unauthorized or excessive fees to the accounts of debtors who are in chapter 13. Many of these debtors emerge from a chapter 13 case after three to five years of struggling to cure an arrearage only to have the lender assert that

they are several months behind on their payments due to fees for such items as attorney's fees, broker price opinions, and other charges allegedly incurred during the chapter 13 case, and which they were never informed of before. Many bankruptcy courts have decried these abuses, but usually they go unremedied because the bankruptcy case is over and the debtor has no money to litigate about them. Sometimes, the fees are not even revealed to the debtor until the debtor pays off the mortgage balance upon selling the home or refinancing. A provision to remedy the problem of excessive fees could provide that all fees and charges based upon occurrences during the pendency of a chapter 13 case must be approved by the court ...”

- ***End mandatory arbitration in bankruptcy.*** “Mandatory arbitration clauses are found in many consumer contracts, including home mortgages. These clauses force consumers to submit their claims to an arbitrator who issues a final, binding ruling on the merits, with virtually no opportunity for judicial review. The enforcement of these arbitration agreements under the Federal Arbitration Act is often in direct conflict with the goal of bankruptcy jurisdiction to have one centralized forum for the prompt resolution of disputes affecting the bankruptcy estate.”
- ***Create a minimum homestead exemption for the elderly.*** “A significant number of debtors facing foreclosure are elderly and have nonexempt equity in their properties because of low homestead exemptions in some states, either due to recent appreciation or the fact that their predatory mortgages were for less than the value of their properties. These debtors cannot save their homes by refinancing because they cannot afford the monthly payments that would be required, and cannot file chapter 13 cases to save their homes because current law would require paying the value of their nonexempt equity to unsecured creditors. They cannot even get chapter 7 relief because chapter 7 would cause them to lose their homes. The solution to this problem is a homestead floor for the elderly.”
- ***Amend chapter 7 of the Bankruptcy Code.*** “One problem facing debtors who are trapped in high cost loans is the inability to refinance out of those loans. So, for example, a debtor who owes 125 percent loan to value (LTV) on a home must come up with a lender who will finance a 125 percent LTV mortgage -- leaving the debtor in much the same difficulty. The inability to strip down a high loan to value mortgage gives the first lender a stranglehold over the debtor, as payments and fees rise and the debtor's only option is to give up the home.” Holders of personal property can “redeem” their property by paying the creditor the current value of the property; owners or homes should get the same right.

For the full list of needed steps by Congress, review the complete joint statement at <http://www.nacba.org> on the Web.

BANKRUPTCY ATTORNEY SURVEY FINDINGS

Conducted from April 2-9, 2007, the NACBA survey of its Association members was responded to by 640 attorneys (26 percent of total membership). The key survey findings are as follows:

- 83 percent of bankruptcy attorneys with clients experiencing mortgage problems say that subprime mortgages are a “much bigger problem” (53 percent) or “somewhat bigger problem”

(29.8 percent) today than five years ago. Only 6.6 percent say that they have seen no change or a decline in such cases.

- Over four out of five bankruptcy attorneys (81 percent) say it is “somewhat more difficult” (52.6 percent) or “much more difficult” (27.5 percent) “for people facing foreclosure to file to save their homes than before bankruptcy law changes were enacted in 2005”.
- Four out of five bankruptcy attorneys say that “exotic mortgages” – such as nothing-down loans and ARM loans with short-term “teaser” rates are “a big problem” (47 percent) or “somewhat of a big problem” (32.5 percent) for their clients.
- Over half of bankruptcy attorneys (51 percent) say that 50 percent or more of their clients with homes “have come to you at least partially because of mortgage-related problems.” More than a fifth of bankruptcy attorneys (20.6 percent) said that over 75 percent of their clients with homes had mortgage-related problems.
- Among those who report having clients with mortgage-related problems, nearly three out of five bankruptcy attorneys (58 percent) said that half or more of the clients had subprime mortgages, including 50-75 percent with subprime mortgages (35.5 percent) and over 75 percent with subprime mortgages (21.8 percent).
- More than a third of bankruptcy attorneys (34 percent) say that 50-75 percent of their clients (20.4 percent) or over 75 percent (13.8 percent) “could have avoided foreclosure problems if they had sought bankruptcy relief earlier.”

For complete NACBA survey findings, go to <http://www.nacba.org> on the Web.

ABOUT THE GROUPS

The National Association of Consumer Bankruptcy Attorneys (<http://www.nacba.org>) is the only national organization dedicated to serving the needs of consumer bankruptcy attorneys and protecting the rights of consumer debtors in bankruptcy. Formed in 1992, NACBA now has more than 2500 members located in all 50 states and Puerto Rico.

The Consumer Federation of America (<http://www.consumerfed.org>) is a non-profit association of 300 organizations that, since 1968, has sought to advance the consumer interest through research, advocacy and education.

The Center for Responsible Lending (<http://www.responsiblelending.org>) is a national nonprofit, nonpartisan research and policy organization dedicated to protecting home ownership and family wealth by working to eliminate abusive financial practices. CRL is affiliated with Self-Help, one of the nation’s largest community development financial institutions.

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EDITOR'S NOTE: A streaming audio replay of a related news event will be available as of 6 p.m. EDT on April 12, 2007 at <http://www.nacba.org>.