

Prepared Text

**Statement of
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**“Building Sustainable Homeownership:
Responsible Lending and Informed Customer Choice”**

Federal Reserve Bank of Philadelphia
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Good afternoon. Thank you for inviting me to participate in this important discussion.

I appreciate the Federal Reserve Board of Governor’s decision to convene this public discussion of predatory lending, in general, and “Responsible Lending and Informed Consumer Choice,” in particular. I am Mark Pinsky, President & CEO of Opportunity Finance Network, the national network of community development financial institutions, or CDFIs. The Opportunity Finance Network comprises some 165 private financial intermediaries that have provided more than \$9 billion for quality affordable housing, small businesses, and community facilities and services.

We are part of a larger “opportunity finance” industry that has provided, over the past 35 years, more than \$19 billion in financing in many of our nation’s underserved markets with net charge offs approximately the same as those of banks and other mainstream financial institutions working in conventional, conforming markets.

As the immediate past Chairman of the Federal Reserve’s Consumer Advisory Council, I have seen close-up the Federal Reserve’s dedication to combating predatory lending through effective implementation of HOEPA, Truth in Lending, financial education, and other means. In that role, I also learned from bankers, regulators, consumer advocates, mortgage lenders, legal experts, and others about the complex and overwhelming challenge that predatory lending presents. In my comments today, I do not want to suggest that there is anything simple about fixing this problem. Indeed, my assumption is that laws, rules, and regulations can slow—but not stop—bad people from doing bad things. The best hope of responding effectively to predatory lending is a both-and approach: Both through the law (at the federal, state, and municipal levels, as well as in the courts, where necessary) and in the marketplace.

About Opportunity Finance

The Opportunity Finance industry works just outside the margins of conventional, mainstream finance to help the people and communities there join the economic mainstream and to help the economic mainstream enter emerging opportunity markets. We are permanent players bridging gaps at the margins of the mainstream economy.

In these opportunity markets, where most people seek nothing more than a chance to join the race for the American dream of economic and social mobility, predatory lending is a constantly mutating viral infection. It hides, deceives, and perpetuates itself—before it destroys or disables its unsuspecting host. And like viruses, predatory lending is hard to detect and treat because it masks itself as something neutral—subprime lending.

Subprime lending is a good and necessary component of economic growth and opportunity. Predatory lending is neither good nor necessary. In fact, predatory lending is not just a subprime lending problem—although it is turning some prime credit borrowers into subprime customers.

I came here to make three points today:

First, predatory lending is a real and present danger not only to low-income and low-wealth people and communities but to our nation's economy.

Second, although national policy solutions today are too limited to put the brakes on predatory lending, HOEPA is among the best tools at the federal level for addressing abusive mortgage lending. It is limited by the things that constrain many regulations—most notably, that it can never be as nimble as the problem it is addressing. State and municipal statutes are effective in many instances, as well. At a time when predatory lending is still mutating aggressively, federal pre-emption of those state and municipal rules would almost certainly weaken consumer protections and impair households. Finally, addressing predatory mortgage lending without also addressing predatory consumer lending activity is a tragically incomplete approach.

Other speakers today have made these points more effectively than I could. For that reason, and because my request to appear today asked that I do so, I will focus my comments on my third point:

There is a new generation of responsible mortgage financing strategies in the subprime and predatory markets and on the horizon that are intended specifically to use market forces to mitigate predatory lending in the short term and, we hope, to undermine it in the long term. At the Federal Reserve's request, I am going to focus my comments on these responsible mortgage strategies if only to begin to differentiate "best" practices and "good" practices from "bad" practices that constitute predatory lending.

Responsible Subprime Mortgage Finance

Over the past decade, as predatory lending became a national epidemic, financial institutions in the Opportunity Finance Network have sought ways to harness their relationships, skills, and purpose in support of a meaningful response that is appropriate to what we do and who we are. As Martin Eakes of Self-Help and the Center for Responsible Lending has challenged us time and again, predatory lending strips far more wealth from low-income and low-wealth people in a year than all the CDFIs together can create.

Over time, CDFIs have led or participated in state and municipal anti-predatory lending activities, provided financing to assist homeowners trying to get out from under oppressive predatory loans, partnered with responsible subprime lenders through “refer-up” programs, and worked behind the scenes with credit counselors and other support organizations.

For several years now, Opportunity Finance Network, its Members, and an array of other allied organizations have collaborated on possible credit responses. We are, after all, lenders. Our theory has been that if we could offer a set of responsible mortgage products perhaps we could make it more difficult for predatory lenders to penetrate markets, steer prime credit customers into predatory loans, and corrode the economic fabric of vibrant if modest places.

We are approaching this hazardous arena with caution and concern—probably similar “broad brush” concerns that are scaring responsible mainstream lenders away from emerging markets. We are risking our hard-won reputation for finding, serving, and staying with customers because we believe in their long-term prospects and our track record of helping people gain the resources and realize the opportunities they seek. We know that we may be pursuing the “good”—and not necessarily always the “best”—in pursuit of a change in market behavior that will be difficult for us to achieve—at most we aspire to be a tail wagging a dog.

Our hope has been and remains that there is an effective policy strategy to put predatory lenders out of business. We will continue to support appropriate state and local statutes; to advocate for forceful implementation of HOEPA and other federal tools; and to partner where appropriate with legal aid attorneys, credit counselors, and grassroots advocates on many of the issues you heard about earlier today.

We no longer believe we can sit by and wait for a policy solution, however, as abusive lenders steal billions of dollars from the people we exist to serve. We need to intervene in the marketplace to wield our influence as lenders with a demonstrated track record of commitment to people and places that are under-served and/or ill-served by conventional financial providers.

Opportunity Finance Network is putting the finishing touches on a mortgage platform—in conjunction with partners—to deliver an array of responsible mortgage products to people who are or may be vulnerable to predatory lenders. The Opportunity Finance

Network's mortgage platform is designed to provide a comprehensive and credible *business* response to predatory lending.

Here's how it will work: Opportunity Finance Network is creating a CDFI-industry owned mortgage company that will contract with a mainstream mortgage company. That mainstream mortgage company, as a subcontractor, will provide services ranging from originations to compliance to servicing through our Member financial institutions and, possibly, their partners. This structure will ensure that the CDFI industry maintains governance control over the entire process. Our mortgage company partner will provide turnkey training and software.

Our industry-owned mortgage company will screen and monitor the mortgage distribution network for compliance with a set of responsible lending criteria—currently modeled on criteria set by the Center for Responsible Lending. That distribution network will drive product and service innovations going forward.

Our lenders will operate either as correspondent originators or brokers—they will be free to choose whichever better suits their business plans. We have prepared a software decision-making tool to help potential correspondents and brokers assess the housing market and economic conditions in their target markets and also to prepare a preliminary assessment of the operating costs and possible revenue scenarios of participating in our mortgage network.

We are developing a marketing campaign that will focus heavily on lead generation. This entire effort will make sense only if it can achieve material scale—our mid-term goal is to exceed \$1 billion in new originations per year within a few years.

We will incorporate financial education as part of a loss-mitigation strategy that is quantifiable and translates into savings for borrowers. We have an agreement in place with a national service provider for this purpose.

In sum, we are organizing a responsible mortgage finance *system* rather than simply offering a responsible mortgage *product*.

Our approach is one of many public purpose credit responses to predatory lending, and we hope there will be more. A guiding principle for us is that there is no single right approach to responsible subprime mortgage lending—more efforts to undercut predatory lending are better than fewer efforts. At the same time, the economies of scale in the mortgage business will push us all to efficient, highly productive models. To work, we believe that any successful responsible subprime mortgage platform needs to embrace the considerable advantages of the mainstream mortgage finance system while re-aligning incentives to reward responsible behavior.

We do not intend or want to be the only responsible subprime mortgage provider in the marketplace—fortunately we are certain there will continue to be others. We are part of a collaborative of lenders and others ranging from the National Federation of Community Development Credit Unions to ACORN to Self-Help to Housing Partnership Network that is coordinating efforts to mount a counter-attack to the predators.

The lead product on our industry-owned mortgage platform will target asset-deficient home buyers because it combines an array of characteristics that we expect will work well in current market conditions. While it will provide homeowner benefits such as 105% loan-to-value financing to support downpayment and pre-closing financial literacy assistance, recognition of “boarder” income, tolerance of low FICO scores, and forbearance of medical debts up to \$5,000, this purchase mortgage will be priced just above prime rates—probably no more than 80 basis points above prime.

There will be three tiers of investment: Opportunity Finance Network will share in the risk by taking the junior-most, first-loss piece; a large socially motivated investor has agreed in principle to purchase the next 25%; our mainstream mortgage company partner will hold the senior 80% *tranche*, although we believe it is a conforming product that secondary markets will purchase readily.

We plan a \$50 million pilot of the product and platform in the first quarter of 2007. Member CDFIs will originate the initial \$50 million. To succeed beyond that, however, we expect to add multiple products to our platform. With the likelihood of a crisis in so-called “exotic” mortgages, for instance, we may add a refinancing product. To influence predatory lending, the platform must support multiple mortgage products and result in a substantial volume of responsible mortgage originations. It is possible that our platform will be able to deliver products from multiple originating sources and through multiple delivery channels—but we are not there yet.

Conclusion

This panel is about “best practices” in serving subprime mortgage markets. We have built our mortgage finance strategy around the best practices we could identify based on a number of factors:

- The worst practices of predatory lenders; those things that we absolutely will not do.
- The CDFI industry’s experiences over the past 30 years serving markets and customers outside the economic mainstream.
- The pioneering work done by analysts, advocates, and practitioners—some of whom you have heard from today, and
- Our research into what it will take to succeed in our ambitious effort to bend and eventually break the predatory lending business model.

To that end, I will conclude my comments by summarizing the practices and policies that we hope will differentiate what we are doing from what predatory lenders do.

First, we will stay with the customer every step of the way from origination through processing, underwriting, and closing and on into servicing and, as needed,

counseling. That is the heart of our brand promise. We have structured our platform so that we will maintain a privity with the customer through the life of the mortgage.

Second, our long-term success depends on ensuring that our customers have unmitigated access to the full spectrum of consumer finance products and services going forward.

Third, we will provide expert, long-term foreclosure mitigation and prevention services to help our customers manage and, if necessary, overcome, post-closing household debt problems.

Fourth, each of our products will provide a fixed-interest rate option at the lowest possible rate.

Fifth, we will provide fair financial incentives to brokers and originators that give them reason to pursue customers aggressively but eliminate unfair incentives that encourage or reward bad, or predatory, actions.

Sixth, we will use a detailed, prescribed settlement fee schedule that will prevent brokers and correspondents from charging excess or unauthorized fees.

Seventh, none of our products will have pre-payment penalties.

Eighth, we will certify our brokers and correspondents according to principles based on the Center for Responsible Lending. Certified brokers/correspondents must comply across their entire business and not just for an isolated product offering.

We believe our strategy is a good response to predatory lending, but it probably is not the best one. It is the best we can provide right now as we seek to engage capital markets incrementally in our decades-long effort to ensure that everyone has the resources and opportunity to act in the best interests of themselves, their communities, and future generations. We believe, in the words of the abolitionist leader Theodore Parker, that "the moral arc of the universe is long, but it bends toward justice."

Thank you for the opportunity to speak today.