ReedSmith

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Revised Cook County, Ill., Predatory Lending Pilot Program

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On March 21, 2007, Illinois Governor Rod R. Blagojevich proposed revised rules intended to increase protections to homebuyers against "predatory lending" through the Illinois Predatory Lending Database Pilot Program, HB 4050 (the "Program").

Background

The initial Program, which took effect Sept. 1, 2006, required individuals with low credit scores living in certain neighborhoods in the South and Southwest areas of Cook County, to get financial counseling before obtaining a home loan. However, the Program came under fire from community organizations and civic leaders, who raised serious concerns that certain individuals were being wrongly targeted, based solely on race. In addition, the initial implementation of HB 4050 resulted in fewer mortgage loans being made in certain zip codes targeted by the Program. A report from the University of Illinois demonstrated that housing sales in the targeted zip codes dropped nearly 50 percent, while those in non-targeted zip codes declined only 20 percent. As a result, Governor Blagojevich suspended the initial Program Jan. 19, 2007.

Proposed Counseling – Expanded Scope

The revised Program as proposed would increase the pilot area from certain targeted Chicago neighborhoods to all of Cook County, Ill., which encompasses the city of Chicago and some surrounding suburbs. Additionally, rather than requiring credit counseling only for certain buyers based upon a buyer's credit score, as the initial Program did, the revised Program would require credit counseling for all first-time home buyers, and home-owners refinancing a loan secured by their primary residence if the purchase money loan or refinance involves certain loan features, such as:

- An adjustable rate mortgage ("ARM") (regardless of whether the ARM provides for the potential for negative amortization) that allows adjustments of the interest rate during the first five years of the loan's terms;
- A mortgage that may result in negative amortization;
- An interest-only mortgage;
- A mortgage where points and fees exceed 5 percent;
- A "stated income" loan (with no or limited income verification);
- A mortgage that includes a simultaneous 100 percent second-lien loan; or
- A mortgage including a pre-payment penalty.[1]

There are no exclusions for borrowers based on race, economic status, geographic area inside of Cook County, or prior mortgage histories.[2]

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To be a qualified "credit counselor" under the Program, the statute requires that the counselor be associated with a HUD-certified counseling agency.[3] During the required counseling, the counselor must, at a minimum, obtain certain information about the borrower and provide certain recommendations about the loan, which must then be reported to the predatory lending database.[4] Among the information the counselor must obtain is the borrower's monthly expenses, and the counselor must provide a recommendation regarding such items as the loan terms, the rate of the loan vis-à-vis the "market rate," whether the borrower should seek a competitive bid from another broker or originator, and whether the borrower is "precipitously close" to not being able to afford the loan.[5]

Information Gathering: Proposed Expansion

In addition, the revised Program expands the massive amount of information that a mortgage broker or loan originator must submit to the predatory lending database. The initial Program required that the broker or lender submit extensive information for each loan in the targeted zip codes, including complete information about the borrower, the collateral, the type of loan, the borrower's credit score, the originator's fees, yield spread premium and other charges; information about all brokers, insurers, closing agents, realtors and appraisers; dates on which all required notices were given to the borrower; and whether a sale and leaseback is contemplated. The revised Program would require that all of this information be submitted for all loans in Cook County, and requires additional information as well, such as interest rate, term, closing costs, and whether the loan is an ARM, contains a prepayment penalty, relies on stated income, results in negative amortization, or permits interest-only payments.[6] Unless the title insurer or closing agent simultaneously files with the recorder a certificate of compliance with the Program along with the mortgage, the mortgage is not recordable.[7] In addition, failure to comply subjects a party to liability under Illinois' Consumer Fraud and Deceptive Business Practices Act.[8]

Ramifications If Enacted Without Change

While laudable in its intention as to certain borrowers, the revised Program, if enacted, will place an increased burden on many homeowners by requiring credit counseling, regardless of economic status, number of prior mortgages or refinances, or familiarity with the mortgage process, with the result that many who don't need counseling will nonetheless be required to obtain it.

The revised Program, if enacted, will also place a heavy monetary and resource burden upon brokers and lenders. The Program would require that either the broker or the lender pay the "reasonable and customary costs not to exceed $300 for a counseling session associated with credit counseling."[9] Moreover, brokers and lenders will undoubtedly spend great time and expense furnishing the required information to the database.

Time to Comment

An initial 45-day comment period on the proposed Program began April 6, 2007 and will end May 21, 2007, after which time a hearing will be held. After that, the proposed Program will go to the Illinois Legislature's Joint Committee on Administrative Rules for a 45-day Second Notice Period, after which time the Program will be modified, adopted or withdrawn within 90 days. Accordingly, brokers and lenders may want to participate in both the initial comment process and the hearing on the proposed Program.

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With the merger of Reed Smith and Chicago-based Sachnoff & Weaver in March 2007, the firm is positioned to further serve its clients in the key financial markets of Chicago and the Midwest. Our Chicago office and our Financial Services Regulatory Group is ready to assist clients with the preparation of comments.

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[1] Sections 346.21, 346.22.

[2] An exemption does exist for borrowers applying for a reverse mortgage loan under programs regulated by the Federal Housing Authority that require HUD-certified counseling. Section 346.40.

[3] 765 ILCS 77/70(d).

[4] 765 ILCS 77/74.

[5] 765 ILCS 77/74.

[6] Section 346.15.

[7] 765 ILCS 77/70(g).

[8] 765 ILCS 77/70(j).

[9] Section 346.30.