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**Financial Institutions &  
Insurance Committee**

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**HB 1081**

**Brief Description:** Providing funds to deter, investigate, and prosecute real estate fraud crimes.

**Sponsors:** Representatives Hunter, Benson, Schual-Berke, Newhouse, Cooper, Roach and Simpson.

**Brief Summary of Bill**

- Creates a fund to be administered by the Department of Financial Institutions and the State Treasurer for the purpose of assisting state and local law enforcement authorities in deterring, investigating, and prosecuting fraud on the part of mortgage lenders.
- Requires county auditors to collect money for the mortgage fraud prosecution fund via the imposition of a surcharge upon those recording certain deeds of trust.

**Hearing Date:** 1/22/03

**Staff:** Thamas Osborn (786-7129).

**Background:**

Predatory Lending: Since the late 1990s, there has been increasing controversy nationwide regarding the marketing and lending practices of certain members of the mortgage lending industry, particularly those involved in the *subprime* market. (Subprime loans are those issued to borrowers who do not meet the credit standards required to receive a loan on the *prime* market.) Some unscrupulous lenders engage in a variety of fraudulent and/or deceptive practices resulting in loan agreements that are detrimental to the financial interests of the borrowers and which unfairly benefit the lender. Such *predatory* lending practices tend to diminish the financial benefits of home ownership by retarding the accumulation of equity and substantially increasing the likelihood of default and foreclosure, a phenomenon that some have characterized as a national trend towards "asset depletion." The negative effects of such lending practices have a disproportionate impact on low income persons, minorities, and the elderly.

State Regulation: Under Washington law, there are three acts that are pertinent to the regulation of mortgage lending practices: 1) Consumer Protection Act (Chapter 19.86 RCW); 2) Mortgage Broker Practices Act (Chapter 19.146 RCW); and the 3) Consumer Loan Act (Chapter 19.86 RCW). Although none of these acts directly address some of the specific practices often associated with predatory lending (i.e., excessive fees, prepayment penalties, balloon payments, etc.), they have significant disclosure requirements and generally prohibit practices that involve fraud, deceit, and/or misrepresentation.

Consumer Protection Act (CPA): The CPA is designed to regulate the conduct of any business entity that engages in commercial transactions with consumers, including those businesses involved in the mortgage lending industry. It contains very general language prohibiting "unfair methods of competition and unfair or deceptive acts or practices in the conduct of any trade or commerce." The breadth of this prohibition would seem to encompass many of the deceptive and/or fraudulent practices of unscrupulous mortgage lenders and is, in fact, the legal remedy most often used to redress the grievances of mortgage borrowers.

The CPA allows an injured party to receive treble damages, up to a maximum of \$10,000 dollars.

Mortgage Brokers Practices Act (MBPA): The MBPA provides a general framework for the regulation of the mortgage brokerage industry. Violations of the act constitute an "unfair or deceptive act or practice," which are subject to the remedies provided in the Consumer Protection Act. In addition to providing licensing requirements and defining the parameters of state regulation, the act contains an extensive list of prohibited practices as well as disclosures that brokers must make to potential borrowers.

Consumer Loan Act (CLA): The regulatory scheme of the CLA is patterned after the MBPA and contains very similar requirements regarding disclosures and prohibited practices. The act is specifically designed for the regulation of consumer loan companies that cater to the subprime market. In addition to licensing requirements, the act creates a list of prohibited practices encompassing fraud, deception, failure to disclose specified information, unfair business practices, and other conduct that might adversely affect consumers. Violations of the act that constitute an unfair or deceptive act or practice are deemed to be violations of the Consumer Protection Act.

### **Summary of Bill:**

The bill creates a fund to be administered by the Department of Financial Institutions (DFI) for the purpose of deterring, investigating, and prosecuting consumer fraud on the part of mortgage lenders. The DFI is required to consult with the attorney general and local prosecutors in developing guidelines for the distribution of the funds, which are to be used to enhance law enforcement capabilities at both the state and local level. Only the director of the DFI " or an authorized designee " may authorize expenditures from the fund.

The fund is derived from a two dollar surcharge assessed by the county auditor against individuals recording a residential first mortgage deed of trust. In order to defray the costs of collection, the county auditor may retain up to five percent of the funds collected. Once collected by a county, the funds must be transferred monthly to the State Treasurer who, in

turn, must deposit the funds into an a specially designated "mortgage lending fraud prosecution account."

The DFI has sole authority with respect to the expenditure of funds from the account. Should the funds in the account during any fiscal year exceed \$700,000, the DFI must transfer the excess funds to the Washington Housing Trust Fund.

**Appropriation:** None.

**Fiscal Note:** Received on January 21, 2003.

**Effective Date:** Ninety days after adjournment of session in which bill is passed.