

# Brooklyn Daily Eagle

## **Brooklyn Law School Professor Predicts Lawsuits Will Follow Collapse of Subprime Market**

### **Government Help for Borrowers Won't Reach the Whole Problem, Scholar Says**

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JORALEMON STREET — Brooklyn Law School Professor David Reiss was recently interviewed by a national Canadian television station, the Business News Network, about the possible explosion of lawsuits following the collapse of the subprime lending market this summer. Reiss predicted the collapse of the subprime market last year in an award-winning academic article.

Lawsuits will likely be filed against entities including the ratings agencies, lenders and investment banks, Reiss told television viewers.

“You name a player,” the professor said, “and I think you will see a lawsuit coming from that direction.” He discussed sources of various protections and legal remedies that might be available to borrowers and investors, including consumer protection laws and suits for fraud, as well as securities laws.

In a law journal article published last year, Reiss identified predatory mortgage lending as “today’s most pressing consumer protection issue, costing American families an estimated nine billion dollars a year.” He attributed the magnitude of the problem to the convergence of three trends: record-breaking rates of homeownership, ever-increasing housing prices and “the development of a credit market, known as the ‘sub-prime market,’ for those with no credit histories and poor credit histories.”

“Predatory lending in the subprime market is particularly rampant,” Reiss wrote, because unsophisticated borrowers are seeking to cash in on their home equity in record numbers. Predatory lenders steer homeowners into loans that are profitable for brokers and lenders but ultimately unaffordable for borrowers.

In spite of the efforts of public interest lawyers like those at the Brooklyn Bar’s Volunteer Lawyers Project and South Brooklyn Legal Services, “traditional litigation has

not been sufficient to tackle the problems that have arisen in the rapidly changing and growing subprime market,” Reiss wrote.

Two Brooklyn neighborhoods, Bushwick and Bedford-Stuyvesant, have been among the most targeted for abusive and discriminatory lending and real estate practices, according to Mark Winston Griffith, of the Neighborhood Economic Development Advocacy Project (NEDAP). Several speakers at a July public hearing in Bedford-Stuyvesant argued that subprime loans are predatory by nature, because they have significantly higher foreclosure rates and African-Americans and Latinos are both four times more likely to receive one.

Sen. Hilary Clinton, D-New York, called on President Bush last month to provide leadership in addressing the crisis in the housing market and its effect on the financial markets. Despite previous optimistic forecasts by the President and the Federal Reserve chairman, Clinton wrote, “It appears from the significant market losses of the past week that there indeed has been spillover from the subprime market to other components of the financial system... [I]t is important to remember that this is not simply a market correction, but a real issue with the financial well-being of millions of American families at stake.”

Gov. Eliot Spitzer announced a \$100 million-dollar “Keep the Dream” refinancing program to give some low- and moderate income homeowners with risky mortgages an opportunity to refinance and avoid possible foreclosure. The program is administered through the state Division of Housing and Community Renewal.

At a White House press conference last Thursday, President Bush allowed that many “hardworking Americans, you know, sign up for loans, and the truth of the matter is they probably didn’t fully understand what they were signing up for.” On Friday, Bush announced several initiatives to help distressed homeowners, without promising a bailout. Sen. Chuck Schumer, D-New York, reportedly said the President made some constructive suggestions, but urged stronger regulation of mortgage brokers. Brooklyn Law Professor Reiss said government intervention is probably appropriate but he still predicts an explosion of lawsuits.

“I do think that at some point it is appropriate for the government to intervene, even though borrowers have some of the blame. It’s appropriate in a large-scale crisis like this to have government intervene to assist people,” Reiss said. But he does not think public assistance for borrowers will significantly reduce the number of lawsuits.

“Some parties that might be harmed, the harm will be reduced by this FHA [Federal Housing Administration] policy,” he allowed. “It might mitigate damages in the future, but it’s not going to change the underlying liability, which is something that has occurred in the past.” Many lawsuits will involve lending banks suing mortgage brokers and investors suing investment banks – not necessarily borrowers, Reiss said. Government assistance for borrowers will be irrelevant to those cases.

Reiss' article in the 2006 Florida State University Law Review recognized a growing momentum to standardize the subprime lending market. However, Reiss questioned the effectiveness and desirability of standardization efforts being made by three major market forces: federal banking regulators; Fannie Mae and Freddie Mac, the largest purchasers of residential mortgages in this market; and the major bond and securities rating agencies, Standard & Poor's, Moody's Investors Services and Fitch Ratings — identified as "Privileged Raters."

The author examined the methods used by each of these three entities and concluded that the rating agencies "have an effective veto over state predatory lending laws." The absence of consumer protection laws drove people to predatory products.

Reiss' article "Subprime Standardization: How Rating Agencies Allow Predatory Lending to Flourish in the Secondary Mortgage Market" received an award from the American College of Consumer Financial Services Lawyers, as the best article of 2006 on a topic dealing with consumer financial services law.

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