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Prepared Statement of
Colorado Attorney General John W. Suthers
Before the
Financial Crisis Inquiry Commission
January 14, 2010

Chairman Angelides, Vice Chairman Thomas, and members of the Commission, I am John Suthers, Attorney General of the State of Colorado. I appreciate the opportunity to appear before you today to describe the activities of my Office in the midst of and in response to the recent financial crisis.

I. Background.

I have had the honor and privilege of serving as Colorado's 37th Attorney General since January 2005. That means I came into office just as we were starting to hear rumblings about the problems to come in the Colorado housing market. In my view, which is largely hindsight, the states were ill-prepared to deal with many of the root causes of this financial crisis – and Colorado perhaps exceptionally so.

Like many states, Colorado had passed legislation in 2002 dealing with so-called "predatory loans," modeled in part after the federal Home Ownership and Equity Protection Act of 1994.[1] Unfortunately, like its federal counterpart at the time, Colorado's limits on balloon payments and prepayment penalties, and its prohibition on negatively amortizing mortgage loans, applied to such a small subset of the highest cost loans that it proved to be very little deterrent to

[1] 15 U.S.C. § 1639. Colorado's "Consumer Equity Protection Act" is found at §§ 5-3.5-101 to -303, C.R.S. (2009).

abusive lending practices. Loan originators were able to push ever more exotic loan products whose introductory rates and low minimum payment formulas, with significant costs paid outside closing, took those products beyond the coverage of such laws.

In 2005, Colorado did not regulate mortgage loan originators (one of only two states that did not) and we are still one of the few states that does not regulate most of the mortgage lending activities of non-depository lenders.[2] With respect to the few laws we did have back in 2005,[3] we were largely powerless to enforce those laws against national banks and their lending affiliates and subsidiaries due to the aggressive stance federal regulators took to preempt state law, even with respect to discriminatory lending and deceptive advertising.[4]

An additional challenge facing the states, especially smaller states like Colorado, was a relative lack of resources. State banking supervisors, with more and more of their regulated banks defecting to federal charters, saw a reduction in examiners and other staff. In my Office, we have been able to get funding for a total of three FTE dedicated exclusively to mortgage fraud and foreclosure

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[2] Under the Colorado Uniform Consumer Credit Code, §§ 5-1-101 to 5-9-103, C.R.S. (2009), only certain high-cost second mortgages and home equity lines of credit require a lender to obtain a supervised lender license with the State of Colorado. Non-bank lenders making purchase money acquisition loans, refinances of those loans, and traditional second mortgage loans are not regulated.
[3] As part of the Consumer Equity Protection Act passed in 2002, Colorado also adopted a general prohibition on deceptive advertising by mortgage brokers or mortgage originators, and on unconscionable lending practices. *See* § 38-40-105, C.R.S. (2009).
[4] History of federal bank regulators' preemption of state law is discussed in *Cuomo v. Clearing House Ass'n, L.L.C.*, 129 S.Ct. 2710 (2009) and *Watters v. Wachovia bank, N.A.*, 550 U.S. 1 (2007).

relief scams. Existing personnel, already handling a huge variety of other consumer issues, have provided assistance as they could.[5]

II. Mortgage Fraud/False Advertising.

Given our resource constraints, my Office has had to focus our enforcement efforts on deceptive advertising by local loan originators and on egregious cases of mortgage fraud affecting Colorado consumers. We coordinated our efforts with the state district attorneys and the U.S. Attorneys to ensure various cases were pursued by the most effect means. In late 2005 and early 2006, my Office examined the advertising of dozens of local loan originators for federal Truth in Lending Act violations.[6] Cease and desist letters were sent to those advertisers who either were not disclosing an APR in their print advertising or who were disclosing an inaccurate APR.

By late 2006, our newspapers were full of advertisements from loan originators hawking option payment ARM loans.[7] Most of these advertisements emphasized low teaser rates and failed to disclose the negative amortization that borrowers would experience if they made only the minimum payments. Homeowners were led to believe that they were buying a fixed interest rate loan, when in fact only the first monthly payment was at the advertised rate.

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[5] My Consumer Protection Section currently has a total of 41 FTE (17 attorneys) handling a wide variety of consumer fraud, antitrust, debt collection, payday and small installment lending, debt settlement, credit repair, and consumer utility issues.

[6] Loan originators are required to comply with TILA under § 5-3-101(2), C.R.S. (2009) of our Uniform Consumer Credit Code.

[7] Samples of some of the print advertisements we saw and investigated are included with this Prepared Statement as Attachment I.

We issued subpoenas to all of these advertisers and conducted numerous depositions of loan originators. The brokers told us that these ads "made the phones ring." It's clear that thousands of Colorado borrowers got into these loans without knowing the true nature of the teaser rates, the significant negative amortization that they were adding to their principal balances, and the prepayment penalties that came with these loans.

A number of these loan originators ultimately went out of business and we eventually reached a settlement with seven companies that prohibited them from running these advertisements. Several companies refused to settle and were successfully sued for deceptive advertising.

We have also brought civil and criminal actions against lenders and loan originators engaged in deceptive or fraudulent transactions and against individuals engaged in fraudulent real estate schemes. For example:

- In 2007 we settled with Ameriquest Mortgage Company as a result of a multi-state investigation into allegations that it misrepresented and did not adequately disclose the terms of home loans, such as whether a loan carried a fixed or an adjustable rate; charged excessive loan origination fees and prepayment penalties; refinanced borrowers into improper or inappropriate loans; and improperly inflated appraisals;
- In 2008 we brought suit against two large loan originators for advertising and marketing option payment ARM loans in a deceptive

and fraudulent manner. Both cases are still pending and are set for trial in 2010;

- In February 2009 we settled with Countrywide Financial Corporation over the marketing of subprime and other high-risk mortgage products in Colorado. This settlement was part of a multi-state effort led by California and Illinois;
- In July 2009 we obtained criminal convictions against the ringleader of a multimillion-dollar mortgage fraud operation involving nearly three-dozen real estate transactions. An indictment alleged that this ringleader and his colleagues fraudulently obtained $10.9 million in mortgages to buy 34 properties in Denver and surrounding counties and then skimmed $1.1 million from the real estate transactions, which they said paid for repairs never actually performed on the properties; and
- In October 2009 we brought suit against a large loan originator operating primarily in southern Colorado for engaging in deceptive and fraudulent loan originations. That case is still pending.

III. Current Trends.

Over the past two years, my Office has seen a dramatic shift in consumer complaints arising out of mortgage originations. Where we once saw complaints alleging fraud by loan originators, we now see voluminous complaints about mortgage servicing and foreclosure relief scams.

A. Mortgage servicers.

Complaints about mortgage servicers include failure to timely post scheduled payments, the impossibility of connecting with a loss mitigation representative in prolonged efforts to avoid foreclosure, and questions about which entity was the actual holder of the evidence of debt entitled to institute foreclosure proceedings.[8]

In addition to working with loan servicers on individual complaints on behalf of Colorado consumers, my Office is also participating in a multi-state effort to work with loan servicers to encourage loan modifications and other sustainable long-term solutions. The State Foreclosure Prevention Working Group (SFPWG) is comprised of fifteen state attorneys general and the Conference of State Bank Supervisors. Formed in the summer of 2007, the SFPWG met early on with representatives of the 20 largest loan servicers in the United States.[9] Since that time, the SFPWG has been collecting data from 13 of these companies in an effort to verify the performance of their foreclosure avoidance programs.[10]

This data collection effort has led to the publication of three reports by the SFPWG during 2008, with a fourth report covering 2009 to be released shortly.

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[8] It is not unusual for consumers to be negotiating a loan modification with entity while another entity is proceeding with a foreclosure action on the same loan.

[9] Collectively, these companies service approximately 93 percent of the nation's subprime loans.

[10] The remaining companies have declined to participate in this data collection effort for a variety of reasons, including concerns over confidentiality, participation in the HOPE NOW alliance data collection efforts an, in a couple of instances, upon the advice of the US Office of the Comptroller of the Currency.

Unfortunately, each of the first three reports revealed a wide gulf between the level of serious delinquent subprime borrowers and effective loss mitigation efforts – with as many as 7 or even 8 out of 10 seriously delinquent borrowers that were not in any loss mitigation process.[11] While those numbers are believed to have improved over the last year, there are still far too few delinquent and seriously delinquent borrowers who either are not aware of loss mitigation alternatives to foreclosure or who are frustrated by never-ending delays in working out a non-foreclosure solution.

B. Foreclosure Relief Scams.

Shortly after I came into office, I was approached by a number of our local county officials handling foreclosures – called "public trustees" in Colorado – about a rapid increase in the number of individuals who were soliciting homeowners in foreclosure for a variety of foreclosure "relief" services, ranging from refinances and loan modifications to investment schemes designed to save a home from foreclosure. I put together a task force of public and private parties to look at this problem and, in 2006, this task force was instrumental in drafting and then securing passage of the Colorado Foreclosure Protection Act.[12]

The CFPA prohibits foreclosure consultants from collecting up-front fees, from taking a financial interest in a homeowner's property, and requires that foreclosure consulting contracts contain language designed to protect consumers.

[11] Copies of these first three Reports are included with this Prepared Statement as Attachments II, III, and IV.
[12] §§ 6-1-1101 to -1120, C.R.S. (2009).

Investors – referred to as "equity purchasers" under the Act – are subject to strict contracting procedures, a three-day cooling off period during which no documents encumbering the property can be recorded, and special unconscionability provisions relating to sale-leaseback transactions.[13]

Not surprisingly, over the last two years, complaints about foreclosure relief scams have outstripped all other mortgage-related complaints into my Office. Delinquent homeowners are besieged with solicitations arriving at their door, in their mail box, over the telephone, and on the Internet. My Office has now taken action against at total of 33 foreclosure rescue and loan modification firms. We also have investigations under way against dozens of additional companies that are aggressively advertising to Colorado homeowners facing foreclosure. Many of the companies already investigated, and many of those currently being investigated, are located outside of Colorado

Seventeen of these actions were announced as part of two separate sweeps that approximately 25 other state attorney general offices have coordinated with the Federal Trade Commission. The first sweep, Operation Loan Lies, was announced on July 15, 2009 in Los Angeles, California. The second sweep, Operation Stolen Hope, was announced on November 24, 2009 in Las Vegas, Nevada, one of the regions hit hardest by the foreclosure crisis.

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[13] As originally enacted, the CFPA applied only to residences actually in foreclosure. When it became clear that many unscrupulous companies were circumventing its protections by contacting distressed homeowners before a foreclosure was commenced, the coverage of the Act was extended in 2009 to any homeowner at least 30 days delinquent or in default on their mortgage. *See* 2009 Colo. Sess. Laws, ch. 39, § 1 at 154.

IV. Other Initiatives.

In order to leverage our minimal resources, we have also undertaken or participated in a number of other initiatives involving mortgage or foreclosure related issues. Among these are:

Legislation. In addition to the Colorado Foreclosure Protection Act discussed above, my office has been involved in a number of legislative initiatives affecting mortgage lending in Colorado since 2006. Some of these efforts included:

- HB 06-1161, a bill requiring mortgage brokers in Colorado to be registered with the state;
- HB 06-1323, a bill imposing a minimum fine of the amount of pecuniary harm and mandatory restitution for victims where theft by deception involves the mortgage lending process;
- HB 07-1322/SB 07-203/SB 07-216/SB07-249: a series of bills designed (once reconciled with each other) to create a full licensing regime for mortgage brokers originating loans in Colorado;
- SB 07-085, a bill designed to deal with the coercion or intimidation of a real estate appraiser, creating both civil and administrative penalties;
- HB 08-1402, a bill that requires lenders to provide written notice to homeowners regarding the Colorado Foreclosure Hotline;

- HB 09-1085, a bill amending Colorado's nascent mortgage licensing regime to comply with the requirements of the federal "Secure and Fair Enforcement for Mortgage Licensing Act of 2008" (SAFE Act); and
- HB 09-1276, a bill establishing procedures for a borrower facing a foreclosure to seek a temporary deferment of that foreclosure to work with a housing counselor on a loan modification.

Foreclosure brochure. My Office, working with a number of our county public trustees, designed and distributed a brochure educating consumers about foreclosures in Colorado and warning against common foreclosure relief scams. This brochure is used by public trustees across Colorado as part of their initial notices sent to homeowners facing foreclosure.

Colorado Foreclosure Hotline. This Hotline began in October 2006 in response to recommendations from the Colorado Blue Ribbon Panel on Housing and the Colorado Foreclosure Prevention Task Force. It offers toll-free (1-877-601-HOPE) access to HUD-approved housing counselors across Colorado. My Office has been a sponsor of the Hotline since its inception and, in 2009, provided a $500,000 grant to the Hotline out of proceeds from our settlement with Countrywide so that the Hotline could undertake greater efforts to reach out to borrowers, in particular to minority borrowers. Through October 2009, the Hotline has handled more than 88,000 calls, has generated nearly 18,000 face-to-face counseling sessions, and has documented more than 16,000 positive outcomes from those sessions.

Federal/State Financial Fraud Enforcement Task Force. Established by Executive Order from President Obama On November 17, 2009, Colorado serves as a co-chair of the Mortgage Fraud Working Group.

Public Forums. Members of my staff and I have spoken at public forums across Colorado on issues related to mortgage fraud and foreclosure relief scams. Sessions have been held with distressed homeowners, real estate and mortgage lending industries, housing counselors, and other interested groups.

V. Continuing Concerns.

As more Colorado consumers have fallen behind on their mortgage payments, we have seen an increase in the marketing of other services to those same consumers. In addition to the foreclosure relief solicitations discussed above, we have also seen an increase in payday and other high cost loans, and an increase in debt settlement and credit repair solicitations as well.

A. Payday loans.

Under Colorado law, payday loans are limited in amount (maximum of $500), finance charges ($75 on a $500 loan), and duration (two weeks with one renewal). In 2002, the total loan amount reported by licensed payday lenders in Colorado was $245.9 million. By 2007 that number had increased to $639.5 million – an increase of 160 percent. And, these figures do not take into account unlicensed payday lenders operating primarily, or exclusively, on the Internet.

Since 2005, my Office has undertaken a number of investigations into both licensed and unlicensed payday lending in Colorado, resulting in 62

disciplinary actions and some very contentious litigation in which several payday lenders operating over the Internet claim to be subsidiaries of two Native American tribes and thus entitled to sovereign immunity.[14] We have issued an additional 66 cease and desist notices, primarily to unlicensed Internet lenders. We have assessed in excess of $1.1 million in fines and penalties.

B. Debt management companies.

Since Colorado's version of the Uniform Debt Management Services Act took effect in 2008, my Office has investigated and taken disciplinary action against 26 debt management companies and has issued 22 additional cease and desist notices. Violations include failure to register, failure to make mandatory disclosures, excessive fees, and others. We continue to investigate and prosecute debt management companies that have failed to comply with our Act.

We have required companies to refund more than $1.3 million to Colorado consumers. We have also assessed fines and penalties of $132,250 against debt settlement companies.

C. Credit repair companies.

Companies offering to repair a consumer's credit rating are governed in Colorado by our Credit Services Organization Act[15] and by a similar federal

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[14] Colorado is unique in that payday lending is regulated by the Attorney General's Office.
[15] §§ 12-14.5-101 to -114, C.R.S. (2009).

statute,[16] although the requirements of the two statutes vary somewhat. As a general rule, both act prohibit advance fees for credit repair services, require written contracts, and mandate certain disclosures, including disclosures about cancellation rights. We have begun to see more complaints against credit repair companies and expect to file a significant action against a large credit repair company in the next month or two.

D. Overall consumer credit markets in Colorado.

One significant effect of the current financial crisis is the shrinking of the consumer credit markets in Colorado. We see this directly in our regulation of supervised consumer lenders under our Uniform Consumer Credit Code. These supervised lenders include a variety of finance companies making unsecured loans for personal, family, or household purposes; mortgage companies making high-cost second and home equity line of credit loans; and credit sellers of goods or services intended primarily for personal, family, or household use.

At its peak in 2006, my Office licensed more than 2300 supervised lenders[17] making in excess of $2.8 billion in consumer loans. By mid-2008, we had lost nearly 1300 of these licensees and consumer lending had decreased to just slightly more than $1 billion. The vast majority of these lost licensees came from mortgage lenders who (1) chose to become licensed exclusively under Colorado's loan originator licensing regime; (2) were acquired by a national bank

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[16] Federal Credit Repair Organizations Act, 15 U.S.C. §§ 1679 – 1679j.
[17] This includes licenses issued for each separate retail location operated by a supervised lender.

or chose to convert their state operations to a national bank charter; or (3) simply went out of business.

VI. Conclusion.

The causes and effects of our current financial crisis are no doubt as varied as they are complex. In my Office, we have primarily seen the effects of this crisis through record home foreclosures, spiraling credit card and other high cost debt and, unfortunately, the significant growth of other perhaps less reputable industries to take advantage of the financial struggles of good, honest Coloradans. Thank you for letting me take the time to describe how one relatively small attorney general's office is dealing with some of these effects.