Brown Sues Countrywide For Mortgage Deception

Contributed by Editor
Sunday, 29 June 2008

LOS ANGELES – California Attorney General Edmund G. Brown Jr. on Wednesday sued Countrywide Financial, its chief executive Angelo Mozilo, and president David Sambol, for engaging in deceptive advertising and unfair competition by pushing homeowners into mass-produced, risky loans for the sole purpose of reselling the mortgages on the secondary market.

“Countrywide exploited the American dream of homeownership and then sold its mortgages for huge profits on the secondary market,” Attorney General Brown said Wednesday. “The company sold ever-increasing numbers of complex and risky home loans, as quickly as possible. Countrywide was, in essence, a mass-production loan factory, producing ever-increasing streams of debt without regard for borrowers. Today’s lawsuit seeks relief for Californians who were ripped off by Countrywide’s deceptive scheme.”

Brown alleges that Countrywide Financial used deceptive tactics to push homeowners into complicated, risky, and expensive loans so that the company could sell as many loans as possible to third-party investors. According to the lawsuit, the company marketed complex and difficult to understand loans with very low initial or “teaser” interest rates or payments.

Countrywide employees, including loan officers, underwriters, and branch managers – who were under intense pressure to process a constantly increasing number of loans – misrepresented or obfuscated the fact that borrowers who obtained certain types of loans would experience dramatic increases in monthly payments.

In the past, lenders like Countrywide sold home loans to customers and held the loans in their own portfolio, an incentive to maintain strong underwriting standards. Countrywide, however, sold its loans to third-parties in the form of securities or whole loans, often earning more profit for riskier loans. The business model generated windfall profits for Countrywide.

The company pushed these loans by emphasizing a low “teaser” or initial rate, often as low as 1 percent for pay option ARMs. Countrywide obscured the negative effects – including rising rates, prepayment penalties and negative amortization – which would inevitably result from making minimum payments or trying to refinance. The company misrepresented or hid the fact that borrowers who obtained its home loans – including exploding adjustable rates and negatively amortizing loans – would experience dramatic increases in monthly payments.

In an effort to rope in as many customers as possible, Countrywide greatly relaxed and liberally granted exceptions to its mortgage lending standards. Traditionally, lenders required borrowers to document income and assets but Countrywide offered reduced or no documentation loan programs to increase its loan sales. Angelo Mozilo and David Sambol actively pushed for easing underwriting standards and granting exceptions to documentation requirements.

In Countrywide’s 2006 annual report, the company touted the massive growth of its loan production from $62 billion in 2000 to $463 billion in 2006 – three times the increase of the U.S. residential loan production market, which tripled from $1.0 trillion in 2000 to $2.9 trillion in 2006. 26 percent of Countywide loans were for California properties. The company sold an ever-increasing number of loans in an effort to gain a 30 percent market share of loan originations and then sell its loans on the secondary market, as mortgage-backed securities or pools of whole loans. Countrywide’s securities trading volume increased from $647 billion in 2000 to $3.8 trillion in 2006.

Countrywide routinely sold loans based upon a borrower’s stated income and without verifying the information. Loan officers memorized scripts that marketed low payments by focusing on the potential customer’s dissatisfaction, saying, for example, “Which would you rather have, a long-term fixed payment, or a short-term one that may allow you to realize several hundred dollars a month in savings?” The loan officer did not state that the payment on this new loan would exceed the payment on the current loan.

Countrywide paid greater compensation to brokers for loans with a higher interest rates, as well as prepayment penalties, because it could sell those loans for higher prices on the secondary market. Countrywide also paid rebates to brokers who originated loans with prepayment penalties, adjustable rates and high margins.

Countrywide operated an extensive telemarketing operation in which it touted its expertise and claimed to find the best financial options for customers. Customer Service representatives at Countrywide call centers were required to complete calls within three minutes, often processing sixty-five to eight-five calls per day. Employees who did not meet quotas were terminated. The company’s deceptive marketing practices, designed to sell costly loans while hiding or misrepresenting the terms and dangers, included:

• Encouraging borrowers to refinance or obtain financing with complicated mortgage instruments like hybrid adjustable rate mortgages or payment option adjustable mortgages • Marketing complex loan products by emphasizing a very low “teaser” rate while misrepresenting the steep monthly payments, increased interest rates and risk of negative amortization • Dramatically easing underwriting standards to qualify more people for loans • Using low or no-documentation loans which allowed no verification of stated income • Hiding total monthly payment obligations by selling homeowners a second mortgage in the form of a home equity line of credit • Making borrowers sign a large stack of documents without provider time to read the paperwork • Misrepresenting or hiding the fact that loans had prepayment penalties

As the secondary market’s appetite for loans increased, Countrywide further relaxed its standards to finance borrowers with ever-decreasing credit scores. Countrywide employees routinely overrode the company’s computerized underwriting system, known as CLUES, which issued loan analysis reports recommending or discouraging loans based on factors such as a consumer’s credit rating. As the pressure to produce loans increased, Countrywide set up an entire department in Plano, Texas, at the direction of Mozilo and Sambol, where employees could submit requests for underwriting exceptions. In 2006, 15,000 to 20,000 loans a month were processed through this exception process.

Countrywide’s deceptive sales practices resulted in a large number of loans ending in default and foreclosure. According to Countrywide’s February 2008 records, a staggering 27 percent of its subprime mortgages were delinquent. Overall, approximately 20,000 Californians lost their homes to foreclosure in May 2008 and 72,000 California homes were in default, roughly 1 out of 183 homes.

Despite receiving numerous complaints from borrowers claiming that they did not understand their loan terms, Countrywide ignored loan officer’s deceptive practices and loose underwriting standards. Countrywide also pushed its borrowers to serially refinance, repeatedly urging borrowers to obtain home loans to pay off their current debt.

The lawsuit, filed Wednesday morning in Los Angeles Superior Court, redacts confidential information Countrywide provided during the attorney general’s investigation. The attorney general is seeking the company’s consent to file an amended complaint that removes the redactions.

During the course of its investigation into Countrywide, state investigators reviewed hundreds of thousands of documents and interviewed scores of witnesses including consumers and former employees.

Consumers who believe they have been victimized by Countrywide Consumers should file a complaint by contact the Attorney General’s Public Inquiry Unit in writing at Attorney General's Office California Department of Justice Attn: Public Inquiry Unit P.O. Box 944255, Sacramento, California or through an online complaint form: http://ag.ca.gov/contact/complaint_form.php?cmplt=CL.

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