State Bar of Michigan

NEWSLETTER

Consumer Law

V. 12, No. 2 State Bar of Michigan Consumer Law Section September 2008

Consumer Law Section Annual Meeting Notice

Thursday, September 18, 2008
2 p.m. Business meeting, program to follow
Hyatt Regency, Dearborn

Responding to Michigan's Foreclosure Crisis
Panelists:

- Joon Sung, University of Detroit Mercy School of Law
- Lorray Brown, Michigan Poverty Law Program
- Greg Sterns, Lighthouse Community Development

Presentation of the Frank J. Kelley Consumer Advocacy Award

Election of section officers and council members

There is no charge for this program and no charge to register for the State Bar Annual Meeting. Please register for the meeting so we can welcome you with a name badge. *www.michbar.org/annualmeeting.cfm*

Contents

State House Passes Predatory Lending Bills

By Fred Miller

With the growing toll of past predatory mortgages on communities and the economy in Michigan and around the country, the Michigan House of Representatives voted overwhelmingly in June to pass a set of bills to strengthen regulation of mortgage lending. However, just before passage, amendments were added to dilute the impact of two key provisions.

The Home Loan Protection Act, (the act) HB 5294 to 5301, seeks to curb mortgage loans that are bound to fail. One approach the act takes echoes the federal Home Ownership Equity Protection Act (HOEPA), by setting special limits and requirements on high-cost and high-interest lending. The thresholds are lower than the federal statute—5 percent in points and fees or an interest rate more than 8 percent over T-bills brings a loan within this category. Prepayment penalties are barred for these loans, as is negative amortization, and outside counseling is required before the homeowner enters into the loan.

The act requires that no mortgage loans be entered into without a reasonable review by the lender showing that the borrower has the ability to repay. While this may seem like basic underwriting that any lender would do anyway, a big part of the foreclosure crisis stems from mortgages given with no such review, including "liars loans" with no documentation required.

Many borrowers were sold multiple refinances of mortgages in recent years to pay off other debt, piling debt onto homes. Some were sold with bait-and-switch sales tactics and misrepresentations of how the loans would affect the borrowers. The act would require all mortgage refinances to have a "net tangible benefit" for the borrower.

Continued on page 3

From the Chair

By Larry Lacey, Chairperson

The Consumer Law Section will hold its annual meeting and election of officers at the State Bar Annual Meeting in Dearborn, Michigan on September 18, 2008, at 2 p.m. We will be holding elections for two open seats on the council for three-year terms. Those on the ballot at this time are Librado (Larry) Gayton, Scott Mussin, Caleb Marker, and Alyson Oliver. Nominations will also be taken from the floor. We encourage as many section members to participate as possible. We will also be having a panel discussion on possible solutions for our clients to the mortgage crisis.

I would like to extend my thanks and the section's thanks to Carolyn Bernstein and Steven Goren for their many years of service on the council. Both have served as chair and in other offices of the council for many years, and we will miss not having their direct input. I would also like to thank the section for the opportunity to serve as chair of the section this past year. It has been a great year with a lot going on. We have partnered with so many groups in so many areas, giving me the opportunity to meet so many people who have the same objective as we do: to protect the consumers of Michigan.

Certain members of this section have been working many extra hours with the legislators of the state to pass bills on predatory lending, foreclosures, and a fix for the Michigan Consumer Protection Act. We have been partnering with groups inside and outside the State Bar, such as ACORN, AARP, CEDAM, MTLA, AFL-CIO, Michigan Catholic Conference, Neighborworks, MPLP, MTLA, and the NAACP. We have also partnered with other sections of the Bar such as the Real Property, Elder Law, and Probate and Estate Planning Sections. Each one of these groups brings a different perspective to the table as each represents a different population, all who are consumers. Even with such diverse groups, our efforts at getting legislation through that is really meaningful to the consumer is very difficult.

Our section has about 1,700 members to whom we offer a listserv for easy communications between members and a newsletter twice a year for the nominal fee of $15. In the past year, the section council has spent monies on a National Consumer Law Center study of the Michigan Consumer Protection Act, soon to be released; partnered with Elder Law of Michigan to sponsor the movie *Maxed Out* at the Lansing Fine Arts Film Festival, along with members of the section appearing on a panel after the show; and presented an all-day seminar on electronic discovery.

I encourage you to become more active in the section. The job of protecting the Michigan consumer is a big one, and we can use all the help we can get.

Want to submit an article?
Want to suggest a topic for an article?

Contact the editors at

ktjapkes@legalaidwestmich.net

House Banking and Financial Services Committee June 10, 2008 Hearing ▪ Home Loan Protection Act

Testimony of Frederick Miller, Campaign to Protect Michigan Consumers

Good morning. I appreciate the opportunity to address you about the most important consumer protection issue this country has faced in decades.

My name is Fred Miller. I am an attorney for UAW Legal Services Plan, also currently the treasurer of the State Bar of Michigan Consumer Law Section, and I represent the Campaign to Protect Michigan Consumers. The Campaign is a coalition of groups concerned about the severely diminished state of consumer protection law and practice in Michigan. Our coalition includes the State Bar Consumer Law Section and many other organizations, including the UAW, AARP, the Area Agencies on Aging, the Community Development Association of Michigan, the Alliance for Justice, ACORN, and others.

Both the State Bar Consumer Law Section and the Campaign to Protect Michigan Consumers strongly support the package of predatory mortgage lending legislation before you, and urge that it not be compromised by deleting any key provisions.

The foreclosure crisis, with its dramatic impact on communities and the nation's economy, was created in part by the failure of consumer protection laws and agencies. Many of the loans now in foreclosure would never have been signed by home buyers and homeowners if large parts of the mortgage sales industry had not succumbed to sales practices frowned on by consumer-friendly businesses throughout the economy, including:

- The use of documents incomprehensible to lay people, and frankly to many lawyers

The foreclosure crisis, with its dramatic impact on communities and the nation's economy, was created in part by the failure of consumer protection laws and agencies.

- Bait-and-switch sales practices, with surprise terms at closing, often hidden in the stacks of documents
- Sales of subprime loans to consumers who qualified for better mortgages, but were not informed, plus hidden kickbacks to brokers for selling even higher-rate loans than the best the subprime lender was willing to provide
- Prepayment penalties, to keep homeowners in bad loans for years by making refinancing more expensive
- Targeting poor neighborhoods for the worst practices

The mortgage wreckage caused by bad sales practices has devastated many who got little or no benefit from their loans, even in the short term, and damaged other homeowners who didn't borrow a dime, by ruining their neighborhoods, housing values, and local businesses.

Continued on next page

State House Passes . . .
Continued from page 1

Intense negotiations involving lenders, brokers, and consumer representatives preceded passage, and many compromises were made. However, just before passage, opponents weakened the bills with two amendments. One added a definition of "net tangible benefit" that would allow the requirement to be met if any one of numerous criteria was found. Under this definition, nearly every loan would meet some definition of "net tangible benefit," no matter how detrimental the loan is to the borrower.

The other major change was the addition of a very large loophole: a complete defense to any liability of any party if the borrower made any material "misstatements, misrepresentations or omissions" in applying for the loan. Reasonable reliance is not required to invoke this defense, so liar loans, which invite inflated figures, may be defensible under this added provision.

The State Bar Consumer Law Section council has joined with many consumer and community groups to support the act while trying to take out the weakening amendments as the bills are considered in the state Senate. ☙

House Banking . . .
Continued from page 3

Throughout the period these practices developed, there was little done in Michigan to combat them. The small band of lawyers who represent homeowners in foreclosure in Michigan struggle to find legal tools to give us the leverage to help our clients. The willingness of mortgage lenders and servicers to adjust mortgage terms to better fit the real value of homes and the circumstances of borrowers is at best erratic, varying from servicer to servicer and literally from day to day.

But leverage and lawsuits are not what this legislation is about. It is about setting standards for an industry that needs clear public standards in order to regain the trust of ordinary people, and it is about giving both government and citizens the power to enforce those standards.

Not selling mortgages that homeowners clearly cannot afford, that will pile debt on homes that will inevitably be lost—this was once the standard every lender automatically upheld, the only standard that made business sense. Not any more. The mortgage market has changed, and is wildly out of kilter. Consumer protections are a big part of righting the market, for both consumers and those who invest in mortgages and securities backed by mortgages.

The mortgage market has contracted sharply, but it will expand again. The changes in the market that led to this crisis have not disappeared. If we want to avoid more problems in the future, we need state and federal laws like the Home Loan Protection Act.

Consumer Education: Part of the Solution or Part of the Problem?

By Josh Ard

Consumer attorneys and consumer advocates typically try to provide some sort of education to consumers. It may be largely brochures, such as those produced by the National Consumer Law Center. Many of us have presented seminars to the public in an attempt to help them protect themselves. We recognize that prevention is much cheaper than a cure. Everybody seemingly buys into these activities. They are funded by governments and foundations. Businesses tout their support of educational efforts. It is now time to step back and decide what the effect has been.

The NASD Investor Educational Foundation conducted a study entitled "Off the Hook Again: Understanding Why the Elderly Are Victimized by Economic Fraud Crimes," with results and analysis prepared for WISE Senior Services by The Consumer Fraud Research Group (2006). One hypothesis was that financial education was a key part of the solution. That hypothesis was not supported by the data. In fact, the opposite occurred:

> How financial literacy relates to investor fraud is a question that seems particularly relevant in 2006. There are thousands of financial literacy programs in the U.S., all offering similar content designed towards a single end: improve Americans' understanding of finances and financial markets in order to improve their future financial well-being. P.10. Everyone from Warren Buffett to Alan Greenspan has championed the cause of improving financial literacy as a key to America's future. It is axiomatic that the more one knows about a subject, the better one's chances are of succeeding at it.
>
> When it came to investigating differences between victims and non-victims of investment fraud, a major hypothesis was that victims of fraud knew less about concepts related to investing than non-victims and consequently would score significantly lower on financial literacy questions than non-victims. The most surprising finding of the entire study was that just the opposite was true: victims outscored non-victims by a statistically significant margin. Investment fraud victims answered 57.75 percent of the eight questions correctly compared to the non-victims who answered 41.00 percent of the questions correctly. P. 17.

Obviously, these results were a problem for the study's authors, so they attempted to explain them away. After all, in their view, "There is no question that increased financial literacy can help individuals thrive in the marketplace . . ." P. 19. They offered three possible explanations for this surprising discrepancy with what cannot be questioned:

1. There is a knowing-doing gap. They know it, but somehow they can't do it.
2. The expert snare. The bad guys praised the victims on their knowledge, which conned them into asking fewer questions.
3. Low persuasion education. This is the theory the survey authors liked best: The financial knowledge helped, but it wasn't enough if consumers weren't trained in how to avoid nasty persuasive techniques marshaled against them.

Some very interesting research paints a very different picture. Maybe traditional financial education doesn't help at all and may even hurt.

The Federal Reserve Board of Cleveland released Working Paper 08-03, "Do Financial Education Programs Work?" by Ian Hathaway and Sameer Khatiwada in April 2008. The paper is available online both from the Cleveland Federal Reserve Bank at *www.clevelandfed.org/research* and from the Social Science Research Network at *http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1118485*. One of the findings is:

> Taken together, the literature does not succeed in establishing the extent of the benefit provided by financial education programs, *nor does it provide conclusive support that any benefit at all exists*. The reason is not clear, but could only be one of three culprits: either (a) financial education simply does not work, (b) financial education does work but the programs are not effective at transferring knowledge (i.e. poorly designed programs), or (c) financial education does work and the programs are properly designed, but program evaluation techniques are not yet adequate in capturing these effects. We believe that option (a) is unlikely, and that some combination of (b) and (c) is more likely. Either way, it is clear that more extensive program evaluation and further research are much needed. P. 5. (Emphasis added.)

Prof. Lauren Willis is much less sanguine as the title of her paper illustrates, "Against Financial Literacy Education," which appeared as Public Law and Legal Theory Research Paper No. #08-10 of the University of Pennsylvania and will appear this November in 94 Iowa L. Rev. The draft version referred to in this article can be found at *http://papers.ssrn.com/abstract=1105384.* She argues that financial literacy education is far from benign; rather, it is an insidious move that:

1. Fails to do any good at all.
2. Pretends that the locus of consumer problems is in the head of consumers rather than the acts, methods, and practices of businesses.
3. Detracts resources from attempts to find any real solution and directs them towards futile, but feel-good education efforts.
4. Discourages governments from changing consumer laws and regulations.
5. Actually makes matters more difficult for consumers by giving them a false sense of confidence.
6. Convinces consumers that any failure is their fault, not the fault of businesses.

When one considers the difficulty in making any sense at all of standard form contracts for such complicated products as annuities and other financial investments, especially by older consumers, financial literacy indeed seems futile. One wonders how well salespersons could do on a standardized comprehension test of what the very long documents really mean, let alone the consumer. It is not so much that businesses could not produce documents and contracts that consumers could be educated to understand, but rather that they deliberately produce documents that are virtually impossible for consumers to process effectively. The documents are lacking in both readability and usability. What level of education would be necessary to combat the misrepresentations and high degree of pressure used by financial salespersons? A very interesting study is found in a *Wall Street Journal* article on a training program once called Annuity University. See *http://www.globalaging.org/pension/us/private/AnnuityU.htm* .

Prof. Willis offers several alternatives to education, but these all require governmental action. Advocacy is good, but it does not do much now for real-world problems. Is there nothing we can do to empower consumers to better protect themselves? Many of us consider education to be an important part of our jobs. We want to do something, but something useful, not something futile. In particular, I have a background in training and would like to provide effective training to consumers, especially some of the more vulnerable ones. The challenge is to find some sort of training goal and training methods that make sense to provide meaningful help in the current consumer environment.

There are some reasonable alternatives—at least they seem reasonable to me—but they have not yet been tested. I have worked on developing a version of the excellent "Ask First!" form developed by Ed Long while he was at the Health and Education Program in Torrance, California. The basic idea is that a consumer refuses to deal with a financial salesperson until:

- The salesperson completes a disclosure form that details matters such as education, means of reimbursement, licenses, disciplinary actions, and so forth.
- The consumer actually calls regulators to see if there have been any complaints.

This will cause some dishonest sellers to simply walk away rather than make a misrepresentation in writing. It also buys time for consumers. It prevents signing on the spot and gives them a fighting chance of learning more before being sucked in.

Another alternative I have worked on is developing a facility usage agreement. Many deceptive sales presentations are made at places such as libraries, and senior centers, which give credibility to sellers. The goal is for the facilities to refuse to deal with anyone who does not agree to a specific code of conduct, which includes items such as not making any sales during the presentation and not collecting any information that would allow them to contact attendees directly. Attendees could, of course, contact the presenters on their own later if

Continued on next page

Consumer Education
Continued from page 5

they wish. Presumably, there is a much better chance, in part through organizational leadership, to convince senior centers and libraries to join in efforts as compared with restaurants and motels, other current venues for those presentations.

Both forms are available directly from me. Send me an e-mail at *josh@ardlaw.com* if you are interested.

There are other alternatives that seem attractive. One is to teach certain easy-to-remember maxims of what to do, e.g., never commit to buy anything at a sales seminar, never give your check routing number over the phone, always call the government to see if there are any complaints about a licensed person before doing business, etc. These are good as far as they go, but it is much harder to think of simple maxims that would be helpful in a world deliberately complicated by sellers of products such as annuities, mortgages, and reverse mortgages, except for something like: Consult a qualified attorney before committing any of your money to anything.

Another might be to try to teach social norms for being an ideal consumer. The model is the so-called copynorm (a model behavior for dealing with intellectual property) inspired by the book *Law and Social Norms* by Prof. Eric Posner. This is a type of education and training that has not been pursued much by consumer advocates. Techniques such as role-playing exercise may help. The goal is more to instill traits and habits rather than factual knowledge. AARP has had some success in training seniors to practice what to say to quickly end a call rather than continuing a conversation with a telemarketer, for example.

Simply ignoring the problem won't help, but it appears that traditional consumer education doesn't, either.

Bar Dues Waived for SBM Members on Full-Time Active Duty in the U.S. Armed Forces

Dues have been waived for up to four years for SBM members engaged in full-time active duty in the United States Armed Forces. The waiver, recommended by the State Bar of Michigan Representative Assembly, is intended to relieve the burden on lawyers whose professional careers have been disrupted by deployments into active military duty.

The American Bar Association has called for all bar associations to consider dues exemptions for military members. Michigan is among the first states to implement such an exemption. The waiver takes effect October 1, 2008 — the same date that dues are payable by SBM members.

Greg Ulrich, a member of the State Bar Board of Commissioners and sponsor of the resolution before the Representative Assembly, hailed the recent Michigan Supreme Court order regarding the waiver.

"The waiver recognizes sacrifices by Michigan lawyers serving in the military," Ulrich said. "They are drawn away from their families and daily lives by their commitment to protect us all."

Ulrich also noted other measures voluntarily undertaken by the legal community to respond to the needs of soldiers and veterans, especially the disabled, such as the University of Detroit Mercy School of Law Veterans Law Clinic and Thomas M. Cooley Law School's Service to Soldiers program.

Share the good news.
Back issues of this newsletter can be found at

http://www.michbar.org/consumer/newsletters.cfm

Consumer Law Section Election Notice
2008 Annual Meeting Officer and Council Election

Thursday, September 18, 2008 ■ 2 p.m. ■ Hyatt Regency, Dearborn

Nominees for Officers

Chairperson: Terry J. Adler
Chair-Elect: Adam Taub
Secretary: Frederick L. Miller
Treasurer: Dani K. Liblang

Additional nominations for officers may be made at the meeting.

Section Council Nominees

Four section council seats will also be filled by elections at the annual meeting. There are two seats with returning council members and two open seats, for a total of four seats with three-year terms expiring in 2011. The Nominating Committee has nominated the following:

Term Expiring 2011: Lorray S.C. Brown (current councilmember)
Michael O. Nelson (current councilmember)
Librado (Larry) Gayton
Scott Mussin
Caleb Marker
Alyson Oliver

Additional nominations may be made from the floor.

SBM

State Bar of Michigan

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