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S.B. 949 and H.B. 6367 -- Residential Mortgage Fraud

Banks Committee public hearing -- February 24, 2009

Testimony of Raphael L. Podolsky

**Recommended Committee action: DELETION OR REVISION OF
SECTIONS 1 AND 2 OF THE BILL**

Sections 1 and 2 of these bills inappropriately apply the newly created felony of "residential mortgage fraud" to consumers when it should be limited to fraud by lenders and brokers. The bills do not require that anyone, including the lender, have been harmed by the conduct, nor that the person to whom a misrepresentation was made in any way relied on the information in making a lending decision. See I. 35-38. Conviction of one "act" of fraud is a Class C felony (one to 10 years in jail) and two "acts" (which could include two misrepresentations in a single mortgage application) is a Class B felony (one to 20 years). See C.G.S. 53a-35a. Moreover, the bills provide for forfeiture of any property used in or realized through the fraud.

In its present form, the bills invite serious criminal prosecutions against the victims of overreaching lenders and brokers and, indeed, gives those lenders and brokers a powerful weapon to use against homeowners as a collection tool by threatening to have them arrested and prosecuted. Connecticut criminal law already prohibits as a larceny the obtaining of property by false pretenses. See C.G.S. 53a-119(2). The purpose in creating a separate mortgage fraud statute is presumably to escalate its importance and to induce prosecutors to prosecute and to seek heavy penalties.

It is well known that most of the fraud committed in subprime lending has come from lenders and brokers, not from borrowers. For example, some brokers of subprime mortgages considered it acceptable to pad mortgage applications to make them more marketable. The purpose of Sections 1 and 2 should be to prevent lenders and brokers, who are licensed by the state and subject to a duty of fair dealing, from engaging in fraudulent behavior. The penalties proposed by the bills are not appropriate, however, for use against a borrower. For example, under these bills, a homeowner who drives to a meeting with a mortgage broker who induces the borrower to include inaccurate information in a mortgage application can be convicted of a Class B or C felony and have his car seized and forfeited, even if no lender relies on the information and even if the application is denied and no credit is extended.

As a regulation of an industry in which presumably the arrest of a lender or broker for one violation suggests that many undetected violations have occurred, these bills may be reasonable. As the basis for the prosecution of a borrower, they are overkill.