BUSINESS MATTERS

The County Council's unintended problem

By Richard Parsons
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The Montgomery County Council has done it again.

With nothing but the purest of motives, they have forged boldly ahead with new legislation expanding local regulation of mortgage lending practices, an issue traditionally reserved by State and federal agencies.

In response, dozens of lenders in Montgomery County have announced they will no longer write mortgage loans in the County, citing the vague terms and unreasonable penalty provisions of the law that would leave them open to almost unlimited liability for offering certain customers "excessive" points and fees or "less favorable" terms. Since neither of these terms is adequately defined in the bill, the lenders would seem to have a point. More importantly, the secondary mortgage market, which underwrites much of the retail lending in any community, responded unambiguously with major national players simply closing up shop and walking away from Montgomery County if the bill goes into effect.

The immediate impacts, of course, are falling most heavily on the very people the law was supposed to protect. Chief among them are families with lower incomes and less-than-perfect credit, many of them minorities, who are trying to gain access to Montgomery County's lucrative housing market.

Given the fact that home ownership is one of the best investments any family can make, the true impact of the bill has been to restrict the variety and availability of many of the loan products that were designed to make home loans more affordable for many of these same people.

From the outset, the proponents of this bill, led by Council member Tom Perez, have oversold both the scope of the problem they were trying to address and their ability to impact the national wholesale loan market, which is where the unintended consequences of this bill began to resonate.

In selling this bill, and the perception of a bigger problem than actually exists, proponents sought to sweep up all "subprime" loans, including the very same low-down-payment loan that allowed me to buy my first home a few years ago, into their all-inclusive definition of "predatory" loans. To me, that seems more like predatory legislating, because many of these loans are anything but predatory, they are empowering. You may pay a slightly higher interest rate for a loan with 2% down instead of the standard 20%, but a 20% down payment on a $400,000 Montgomery County home comes out to $80,000 and can be a serious barrier to home ownership for many first-time buyers.

There are many lessons here, among them the value of our system of checks and balances. Just as this ill-conceived bill was supposed to go into effect, the courts got involved and stayed the implementation of the law pending the outcome of the legal challenge brought by a group of lenders.

They are arguing that state and federal laws already preempt local governments from regulating lending practices, and whether or not the lenders who have pulled out will get back into this market will depend on the final outcome of the case.

In the meantime, the Council's best option is to simply repeal the law. That is the only action that will send a clear signal to the lending community that we do want consumers to enjoy the same choices in mortgage lending that other communities continue to enjoy. If there is a need for any further legislation in this area, the Council would be well advised to sit down with the industry and, unlike last time, listen to their input in drafting any future bills so that the proper balance can be struck between consumer protection and healthy competition in the marketplace.

Finally, the biggest danger of "predatory legislating" is the tendency to stifle honest debate when those who voice concerns about a bill are labeled insensitive to discrimination. Such suggestions, in a progressive County like this, leave many of the most knowledgeable critics unable to speak out.

The community loses from less than a full debate of the merits, which could have resulted in a better bill in this case and fewer consumers getting hurt with either a higher monthly loan payment, or a delayed settlement, and other unintended consequences that we now see.

In many ways, this will be a test of our leaders. Council members Knapp and Denis already passed the test by speaking out against this bill and having the courage to vote against what they knew was a bad idea. For other Councilmembers, including Tom Perez, the bill's main sponsor, this is a test of who is enough of a principled leader to admit they made a mistake and take the necessary corrective action.

The best efforts of the Montgomery County Council notwithstanding, the law of unintended consequences is still alive and well.