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California, Illinois Attorneys General Investigate Mortgage Origination Practices

A sense of foreboding has crept in to the financial markets this year, as the volume and quantity of political rhetoric relating to subprime mortgages has grown. Politicians, activist groups, and regulators have threatened mortgage loan originators of all stripes with the spectre of increased regulation and oversight. Meanwhile, lawsuits have sprung up throughout the country on behalf of borrowers and investors.

Two state Attorneys General have taken the process a step further. Late last week, Illinois Attorney General Lisa Madigan made public a subpoena her office issued against Countrywide Financial earlier this year. Countrywide is the nation's largest mortgage lender and its largest loan servicer. Although details of the subpoena are not known, Madigan's office made it clear that she is investigating Countrywide's loan origination practices and that Countrywide has already started to produce documents in response to the subpoena. Subsequently, sources from California Attorney General Jerry Brown's office confirmed that Brown has also issued a subpoena to Countrywide.

The Countrywide subpoenas indicate that the individual state Attorneys General are focusing on the subprime lending fallout, and these subpoenas may just be the tip of a spear aimed at lending institutions. The political climate has changed over the past several months, fanned by populist sentiment, and investigations like the ones against Countrywide have little or no downside for elected officials. Madigan and Brown are not the only large-state Attorneys General to engage on mortgage lending practices; New York Attorney General Andrew Cuomo already has begun high-profile investigations and has charged Washington Mutual of colluding with appraisers to inflate home values; and Texas Attorney General Greg Abbott recently introduced his own plan for foreclosure prevention measures directly to four home mortgage lending and residential loan servicing companies.

In January 2006, 49 state Attorneys General (every state other than Virginia) announced a \$295 million settlement with Ameriquest Mortgage Co. after a two-year investigation and amid charges that Ameriquest and its loan officers engaged in deceptive loan origination practices. The Ameriquest settlement failed to have a widespread political effect, but it is

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reflective of a growing trend among state Attorneys General to work in tandem for maximum impact. The recent disclosures of the subpoenas from Madigan and Brown show that the trend of cooperative investigations is continuing.

Banks and other mortgage originators should consider their options to get in front of any investigation, whether it comes from Madigan, Cuomo, Brown or another state Attorney General. A preemptive review of internal procedures, processes and controls may be advisable. A lending institution will want to be as prepared as possible to show that it had well-defined procedures and policies, solid internal controls, and an overall atmosphere of compliance and sound business practices.