

Mortgage and countrywide comprehensive home essay



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Such actions lead to a surplus of housing, housing prices to fall, and ultimately numerous foreclosures. Many consider these unethical behaviors as a key contributor to the United States 2008-2009 economic recession. As a group, in this paper, we plan to answer the following questions: 1. Are subprime loans an unethical financial instrument, or are they ethical tools that were misused? 2. Discuss the ethical issues that caused the downfall of Countrywide Financial. 3. How should Bank of America deal with potential ethical and legal misconduct discovered at Countrywide?

Are the subprime loans an unethical financial instrument, or are they ethical tools that were misused? To understand subprime loans we have to go back to Orange County, California in the 1970s. During that time rural farmland was being converted into suburbs. And subprime lending was created as a way for people to buy homes even if their credit was poor. Essentially, subprime lending is when financial institutions make loans to people who may have difficulty maintaining the repayment schedule.

These loans are characterized by higher interest rates, little or no collateral and less favorable terms in order to compensate for higher credit risk.

Subprime loans fall into three categories: First is the interest-only mortgage, in which borrowers pay only the loan's interest for a set period of time. The second type allows for monthly payments, but borrowers often opt to pay a smaller amount than needed in order to reduce the owed loan amount. Third, borrowers can find themselves with mortgages featuring a fixed interest rate that converts to a variable rate after a set of period.

One of the tools of the subprime loans is the adjustable rate mortgage (ARM). ARMs generally permit borrowers to lower their initial payments if they are willing to assume the risk of interest rate changes. Many ARMs have relatively short initial fixed-rate periods when the ARM bears an interest rate that is substantially below current average rates. We feel subprime loans are ethical financial tools that unfortunately got misused by unscrupulous people in the banking industry. In order for Countrywide to increase profits they convinced people who qualified for regular loans that subprime loans were a better option.

Additionally they created the ultimate unethical tool called the liar loans. These were mortgages that did not require borrowers to verify income or asset minimums. The extent of the 2008-2009 financial crises has made it clear that unethical subprime loans can wreak havoc for not only consumers but the global economy. Discuss the ethical issues that caused the downfall of Countrywide Financial. At the top of its game, Countrywide had everything going for it until something no one considered happened... the United States economy began to slow.

In 2007, Countrywide had depreciated over \$20 billion and absorbed over \$1 billion in losses. By 2008, Countrywide accrued over \$8 billion in subprime loans with a 7 percent delinquency rate. In 2008, Secretary of Housing and Urban Development, Alphonso Jackson, reported that more than 500, 000 Countrywide consumers were in danger of foreclosure. The blame was placed primarily on subprime lending and adjustable rate mortgages.

Countrywide countered by saying that there were other reasons for delinquencies and foreclosures.

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However that same year, as foreclosures did in fact double, Countrywide was forced to lay-off thousands of its employees. Countrywide tried to ease loan terms for more than 81, 000 homeowners with a new program called the Countrywide Comprehensive Home Preservation Program. This program was implemented to allow consumers to refinance or modify loans with an adjustable rate mortgage for a lower interest rate, or switch to a fixed-rate mortgage. Countrywide continued to come under scrutiny for giving out so-called " liar loans" which are mortgages that require no proof of the borrower's income or assets.

Those with liar loans in the time of the financial crisis could not pay their mortgages, nor could they refinance their homes because of the plummeting housing prices. The core of the unethical behavior here is that corporations themselves impart the appetite for the huge salaries and attractive bonuses to their executive personnel for handling risky business ventures.

Countrywide's CEO Angelo Mozilo was motivated by greed. He used power and position in the corporation in order to acquire higher wages, a better bonus package and largely better compensation for the work that he was disastrous at.

To feed his greed he helped create liar loans or no document required loans. Countrywide also aggressively pushed subprime loans to borrowers who would ordinarily qualify for prime loans because subprime loans yield higher interest rates. How should Bank of America deal with potential ethical and legal misconduct discovered at Countrywide? Bank of America, one of the United States' top financial institutions, offered to buy Countrywide Financial

in 2008 amidst Countrywide's financial crisis. Countrywide may have had other reasons why it allowed itself to be bought by Bank of America.

One reason may have been that Countrywide thought Bank of America was better able to handle the ethical investigations concerning Countrywide. Bank of America had decided to retain David Sambol in the position of Executive Managing Director of Business Segment Operations at Countrywide. In addition, David was paid a large compensation package. A majority of the public was outraged that Sambol had received such a generous compensation after his involvement in Countrywide's questionable business dealings.

With the outcry over the events at Countrywide and other companies that had participated in the use of subprime mortgages being so great, in 2008 the United States Congress held a series of hearings to investigate the dealings in the subprime market. After the hearings, Bank of America announced that Barbara Desoer would be replacing David Sambol. Angelo Mozilo, co-founder of Countrywide, is being investigated by the SEC for potential fraud for the sale of company stock that netted Mozilo over \$400 million between 2002 and 2008. By Bank of America buying Countrywide, they inherited many problems that Countrywide had.

In conclusion, Bank of America needs only to follow the guidelines outlined by The Sarbanes-Oxley Act. That is after it has completely removed all employees found guilty of the ethical and legal misconduct previously discussed. The Sarbanes-Oxley Act requires top management must now individually certify the accuracy of financial information. In addition,

penalties for fraudulent financial activity are much more severe. Also the Act increased the independence of the outside auditors who review the accuracy of corporate financial statements, and increased the oversight role of boards of directors.

We feel the best answer would have been to simply work with the homeowners at whatever the cost to keep them in their homes. Yes this would have come with a huge price tag but considering the bad press and lawsuits that have followed...This would have been a much better course of action. References Ferrell, O. C. , Fraedrich, J. , & Ferrell, L. (2013). Business Ethics: Ethical Decision Making and Cases. Mason, OH: South-Western/Cengage Learning. Tarbox, K. (2012, February 10). Who Qualifies for the \$26 Billion Foreclosure Settlement?

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