



H.R. 3126, the Consumer Finance Protection Agency Act of 2009

New Agency Could Effectively Eliminate the Mortgage Broker Origination Channel

The Administration has proposed a Consumer Finance Protection Agency (CFPA), which targets mortgage brokers with regulations that will effectively eliminate this mortgage origination channel for consumers, limiting competition, increasing prices, and reducing service. Consumers will be forced to obtain mortgages directly from banks, which are not currently equally bound by disclosure requirements about compensation and fees.

H.R. 3126 has been introduced in the House of Representatives to create the new CFPA. While the legislative language does not specifically reference mortgage brokers, the broad authorities H.R. 3126 provides to the new agency could severely harm the mortgage broker origination channel if the Administration moves forward with its plans outlined in its *White Paper*.

Mortgage Brokers Provide a Valuable Service to Consumers

Mortgage brokers find the most appropriate mortgages for their customers by searching through the products of multiple lenders to identify the best loan rates and terms. They also guide homebuyers through the complicated loan process. Because the lenders are saving money on personnel and overhead costs associated with originating a mortgage, the loan products that mortgage brokers offer are at wholesale prices. Mortgage brokers are compensated by their customers for the cost of originating the loan. A consumer can pay such compensation by selecting a slightly higher interest rate, through a yield spread premium. Mortgage brokers are required by existing federal law to disclose all of their fees to the borrower. Even after being compensated for their work, the mortgage brokers are able to offer consumers mortgage loans at rates that are competitive to retail rates that would be offered if a consumer went directly through a lender. While the mortgage crisis has revealed problems across the mortgage industry, ethical mortgage brokers have always provided a valuable service to their customers. Consumers benefit from mortgage brokers' ability to shop around for the best rate and from the individualized assistance that mortgage brokers offer through the process.

The following pages contain our suggestions for changes that must be made to H.R. 3126 to ensure that the mortgage broker origination channel can continue to provide a valuable service to consumers in the home buying process.

LANGUAGE SUGGESTION #1 - COMPENSATION

On Page 54, line 2 insert “form, nature, or amount” so the sentence reads: “The Agency shall not prescribe a limit on the form, nature, or amount of compensation paid to any person.”

Yield Spread Premiums

H.R. 3126 Language: Page 53, Line 19 - “The Agency may prescribe regulations establishing duties regarding the compensation practices applicable to a covered person, employee, agent, or independent contractor who deals or communicates directly with a consumer in the provision of a consumer financial product or service for the purpose of promoting fair dealing with consumers.”

Discussion: While the language in H.R. 3126 is broad, the Administration’s intent has been made clear. According to page 66 of its *White Paper*, the new CFPA should be authorized to “ban often invisible side payments to mortgage originators – so called yield spread premiums or overages – that are tied to the borrower receiving worse terms than she qualifies for, if the CFPA finds that disclosure is not an adequate remedy. These payments incentivize originators to steer consumers to higher-priced or inappropriate mortgages.”

NFMP believes that while loan originators should be prohibited from being incentivized by lenders to offer products that are against borrowers’ interests, a ban of yield spread premiums will have the practical effect of removing consumers’ option to pay for closing costs through the interest rate. The term “yield spread premium” (YSP) is misused in the *White Paper* to refer to incentivized steering. This is an inaccurate characterization of a financial term that refers to the premium that is received when an interest rate is raised. Many times a borrower does not have enough cash up front for closing costs and fees. In this situation, they can choose a higher interest rate, which will allow them to roll closing costs and originator fees into the rate. Consumers do not have to accept a higher interest rate and the corresponding premium. If they do, then the premium can offset their costs to obtain the loan. If they choose not to, then they obtain a lower interest rate. YSP allows borrowers to choose low-cost and zero-point financing for their homes.

Consumers should be able to finance closing costs and origination fees as they deem appropriate for their individual circumstances (i.e. cash available at closing, length of time planning to remain in home, refinance, etc.) While incentive compensation should be banned, YSP should be preserved so consumers can finance all or part of their closing costs. To achieve this goal, language should be added stating that the CFPA should not be able to limit the form or nature of compensation paid to any person. This language preserves the ability for a mortgage originator to be compensated by the lender (nature) through the interest rate (form).

Limits on Compensation

H.R. 3126 Language: Page 54, Line 1 - “The Agency shall not prescribe a limit on the total dollar amount of compensation paid to any person.”

Discussion: Because mortgage closings are based on percentage of the sales price as opposed to specific dollar amounts, the limitation on cap should reflect this market reality. The term “dollar amount” should be replaced with “amount,” so that the sentence reads: “The Agency shall not prescribe a limit on the total amount of compensation paid to any person.”

Compensation At Closing

H.R. 3126 Language: Page 53, Line 19 - “The Agency may prescribe regulations establishing duties regarding the compensation practices applicable to a covered person, employee, agent, or independent contractor who deals or communicates directly with a consumer in the provision of a consumer financial product or service for the purpose of promoting fair dealing with consumers.”

Discussion: While the language in H.R. 3126 is broad, the Administration’s intent has been made clear. According to Page 66 of its *White Paper*, the new CFPA “could consider requiring that originators receive a portion of their compensation over time, contingent on loan performance, rather than in a lump sum at origination.”

This is not a feasible method of payment because of the nature of the mortgage broker industry. This proposal will result in fee tracking and accounting nightmares for the industry. Mortgage loans are bought and sold in huge secondary markets that will now have to account for payments to unknown third parties (brokers). Comments have been made that “this is how the insurance companies do it,” however, there is a substantial difference. Insurance agents are agents of the company through which the policy is issued. An insurance policy generally stays with the same insurer over a long term, as does the agent. The agent has the benefit of collecting renewal payments over a long term and has a relationship with the insurer.

Mortgage loans that are bought and sold in the secondary markets do not carry that benefit for the originator. A loan is generally a one-time transaction for the broker. The mortgage broker does not generally have the opportunity to build a long term “book of business” with multiple ongoing and renewing accounts that continue to generate income. To ensure that the mortgage originator is able to be paid for their work at the time of closing, language should be added stating that the CFPA should not be able to limit the form of compensation paid to any person.

LANGUAGE SUGGESTION #2 - DUTIES

Add language to **Sec. 137. Duties**, stating that an agreement should be made between the mortgage originator and the consumer up front about whether the mortgage originator is acting as: an intermediary between the consumer and the lender; on behalf of the consumer; or on behalf of the lender. The duties imposed on a covered person should reflect such agreement.

H.R. 3126 Language: Page 52, Line 15, Sec. 137. Duties – The Agency shall prescribe regulations imposing duties on a covered person, or an employee of a covered person, or an agent or independent contractor for a covered person, who deals or communicates directly with consumers in the provision of a consumer financial product or service, as the Agency deems appropriate or necessary to ensure fair dealing with consumers.

In prescribing such regulations, the Agency shall consider whether –

- The covered person represents implicitly or explicitly that the person is acting in the interest of the consumer with respect to any aspect of the transaction.
- The covered person provides the consumer with advice with respect to any aspect of the transaction
- The consumer’s reliance on any advice from the covered person would be reasonable and justifiable under the circumstances
- The benefits to consumers of imposing a particular duty would outweigh the costs.
- Any other factors as the Agency considers appropriate.

Discussion: While the language in H.R. 3126 is broad, the Administration’s intent has been made clear. According to page 66 of its *White Paper*, the Administration suggests:

“granting the CFPA the authority to impose carefully crafted duties of care on financial intermediaries. For example, the CFPA could impose a duty of care to counteract an intermediary’s patent conflict of interest, or to align an intermediary’s conduct with consumers’ reasonable expectations as demonstrated by empirical evidence. The CFPA could also consider imposing on originators a requirement to disclose material information such as the consumer’s likely ability to qualify for a lower interest rate based on her risk profile. In that regard, the CFPA could impose on mortgage brokers a duty of best execution with respect to available mortgage loans and a duty to determine affordability for borrowers.”

Rather than allowing the government to dictate the relationship between a mortgage broker and the consumer, an informed decision about this should be made by the consumer. Such a model of establishing the relationship with the consumer up front has proven effective with respect to Realtors. Consumers should be able choose an originator who is: an intermediary between the lender and consumer, an originator working on their behalf, or an originator working for the bank. Regulations should be reflective of these different relationships.

In all of the aforementioned scenarios, it is the underwriter and not the originator who ultimately decides whether a mortgage is affordable to the borrower. Lenders create the loan programs and lending parameters, not brokers. A lender and its professional underwriting staff determine that affordability by the borrower has been sufficiently determined. Brokers do not underwrite loans; this function is within the lender's sphere of operation and responsibility.

Duty of best execution is a vague term that places every member of a legitimate industry in jeopardy. Does a broker simply have to offer the best product he has available to fill the borrower's needs, or if another broker might have a better product is the broker required to send the borrower to the other broker? There is competition in every marketplace for every industry in the country. This proposal appears to be aimed at doing away with the customer's personal responsibility to shop and compare for the best price he or she can find.

LANGUAGE SUGGESTION #3 – PRIVACY OF CREDIT REPORTS

Add language to Section 192. Amendments to the Secure and Fair Enforcement for Mortgage Licensing Act of 2008, stating that mortgage originators' credit report information should not be made available for public viewing.

H.R. 3126 Language: Page 220, Line 4, Section 192 makes amendments to the SAFE Act.

Discussion: An important issue about the SAFE Act that needs to be addressed is with respect to the public availability of the credit reports of mortgage originators. It is the policy of many states that all state, county, and municipal records are open for personal inspection and copying by any person. As a result of this policy, the requirements of the SAFE Act for mortgage brokers to furnish a copy of their credit reports to the state to prove financial character means that mortgage originator credit reports will be available for public viewing. This public access to unredacted credit report information will potentially subject all licensed mortgage professionals to identity theft.

The purpose of the requirement under the SAFE Act was to ensure that all licensees were of adequate financial character to originate mortgages. The purpose was not to make the sensitive and private information used to make such a determination available to the public.

Language should be added to Section 192 to clarify that the information required under the SAFE Act to determine financial character should not be made available for public viewing.

LANGUAGE SUGGESTION #4 – PRESERVATION OF RECOVERY FUND

Delete “and” on Page 222, Line 14 and insert “or” so the sentence reads: “The Agency may prescribe regulations setting minimum net worth or surety bond requirements for residential mortgage loan originators or minimum requirements for recovery funds paid into by loan originators.

H.R. 3126 Language: Page 222, Line 14 - The Agency may prescribe regulations setting minimum net worth or surety bond requirements for residential mortgage loan originators and minimum requirements for recovery funds paid into by loan originators.

Discussion: The SAFE Act prescribed states to adopt either a minimum net worth, surety bond, or recovery fund for licensed mortgage originators. Many state legislatures have contemplated the three options and have selected to implement a recovery fund. For example, in Florida’s recently passed statute to comply with the SAFE Act, it created a recovery fund, which would be capitalized by fees paid by all licensees. The language in H.R. 3126, that would require that mortgage brokers to meet either a net worth or surety bond requirement would put states, like Florida, out of compliance with the federal law. Florida considered this year the idea of a surety bond or net worth for mortgage brokers and has ultimately decided not to adopt these options but instead to adopt a recovery fund, as was allowed for under the SAFE Act.

On Page 222, Line 14 the word “and” should be replaced with “or” so that all three options – minimum net worth requirement, surety bond requirement, or recovery fund - remain available to states as they enact the requirements of the SAFE Act.

LANGUAGE SUGGESTION #5 – INTEGRATION OF RESPA/TILA DISCLOSURES

Add language at the end of Section 132. Disclosures and Communications, (d) Combined Mortgage Loan Disclosure, withdrawing the effective date of disclosure regulations that have been published but have not yet become effective, so that all new disclosures are a result of the Combined Mortgage Loan Disclosure required in this Act.

H.R. 3126 Language: Page 47, Line 9, Sec. 132 Disclosures and Communications, (d) Combined Mortgage Loan Disclosure – Within 1 year after the designated transfer date, the Agency shall propose for public comment regulations and model disclosures that combine the disclosures required under the Truth in Lending Act and the Real Estate Settlement Procedures Act into a single, integrated disclosure for mortgage loan transactions covered by those laws, unless the Agency determines that any proposal issued by the Board of Governors and the Department of Housing and Urban Development carries out the same purpose.

Discussion: RESPA provides borrowers information on the settlement charges for residential real estate transactions, while TILA provides borrowers information on the costs and terms of credit transactions for such properties. For a consumer to fully understand the costs of a transaction, both RESPA and TILA disclosures are essential. However, while better disclosures will greatly improve consumer understanding, having two very different sets of disclosures provided to the consumer at application and at closing will create confusion and potential harm.

H.R. 3126 is right to merge RESPA and TILA forms so that consumers will receive a single, integrated disclosure. The RESPA and TILA reform efforts have operated independently to date and there is evidence that the disclosures will not be harmonious.

If the upcoming implementation of separate disclosures is not halted, lenders and other settlement service providers will incur enormous costs to make systems changes for the new disclosures. In addition, successive systems changes to comply with RESPA, and then TILA, will unnecessarily increase costs at a time when neither the industry nor borrowers can afford them. If the CFPB legislation is later enacted, these costs may prove unnecessary.

The changes to RESPA and TILA should be suspended and implementation postponed in favor of a joint effort to reform the disclosures required under these laws to achieve compatibility between the forms required under both laws.