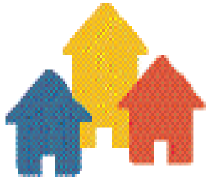

Mortgage Law Central

Legal and regulatory news and analysis for the mortgage industry

April 14, 2008 www.MortgageLawCentral.com Volume 3 Issue 16

Wells Fargo stirs up storm with new broker disclosure

On March 17, Wells Fargo issued a newsflash to mortgage brokers informing them of a newly revised Mortgage Broker Fee Disclosure Form (MBFD).

One Wells Fargo account executive (AE) from Illinois told brokers in an e-mail that the form is being instituted to "ensure that borrowers have clarity with regard to broker fees and how such fees will be paid."

The AE noted that "the mortgage industry and third party lending business have been closely scrutinized in recent months. Newspaper headlines, which have featured the few brokers who have performed less than honorably, have impacted the broker business overall. Given the challenges that we are all facing, Wholesale Lending and Home Equity remains committed to third party lending and our clients."

The new MBFD is divided into two sections. The first section requires the broker to outline and disclose the broker fees that will be charged to process the loan. The second outlines the options available to the borrower for how those fees will be paid, and requires them to select a payment option(s).

Mary Berg, assistant vice president of public relations for the Wells Fargo Home Equity Group, confirmed to *Mortgage Law Central* that effective April 1, 2008, Wells Fargo Home Mortgage (WFHM) and Wells Fargo Home Equity (WFHE) will require brokers delivering loans to WFHM and WFHE to utilize the newly revised Mortgage Broker Fee Disclosure.

Berg said, "This new disclosure will ensure that borrowers have clarity with regard to fees by requiring the broker to outline what compensation the broker is receiving for the loan, and how this amount will be paid. We expect that the new MBFD will provide brokers with an opportunity to build stronger and longer lasting relationships with their borrowers."

In recent days, some mortgage brokers have decried the form as being anti-broker and have suggested a nationwide boycott of Wells Fargo.

Berg declined to comment on such a possibility, stating, "We won't speculate on what brokers will or will not do as a result of this new requirement."

Federal suggestion?

Some industry insiders have indicated that the form may be being instituted to comply with an advisory letter the Office of the Comptroller of the Currency (OCC) put out in 2003 on "Avoiding Predatory and Abusive Lending Practices in Brokered and Purchased Loans."

The letter outlined the OCC's concerns about broker-originated loans and provided specific recommendations for national banks to take to address the risks of such transactions through

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• Originators could get own federal regulator under new plan

Upcoming

• Mortgage trade groups sound-off on the Fed's new rule to reform TILA and HOEPA: A look at the comment letters.

• Housing stimulus bills and FHA reform: How changes in the law will affect the way you do business.

• What's up with the lenders? A look at how tbe big players are changing the competitive stakes.

Key Stats

FinCen reports:

• Of 761 cases of fraud by means of misrepresentation of income, 488 included a mortgage broker.
• Of 496 cases of fraud by means of forged documents, 338 involved a mortgage broker.
• Of 232 cases of appraisal fraud, 113 involved a mortgage broker.
• Of 100 cases of fraud including straw buyers, 66 included a mortgage broker.

Quoteable

"I am all for transparency in our industry, rooting out unethical people and providing an easier way for borrowers to shop loans, but how can we do this if the banks aren't regulated in the exact same way?"

-**Steve Evans** of Stewart Mortgage Services Inc. on the proposed RESPA rule - *Page 8*

EDITOR'S NOTE

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Dear Readers,

Proposals on how to "fix" the mortgage market have become a hot platform in recent days for the presidential candidates to stake their campaigns on. **Hillary Clinton, John McCain** and **Barack Obama** have all been talking housing policy while criticizing their rivals' positions and tallying the campaign contributions by subprime lenders.

Clinton's plan includes new action to help at-risk homeowners restructure their mortgages, the creation of a working group that would investigate ways to broadly restructure at-risk mortgages and report its findings in the next three weeks, an easing in legal liability for mortgage servicers to help unfreeze the mortgage market, and an additional $30 billion in stimulus to help states and localities fight foreclosures in their communities.

Meanwhile, a war of words has broken out between Clinton and Obama over campaign contributions received from subprime lenders. Clinton's camp noted that "the Obama campaign's response to the comprehensive plan Hillary laid out to address the housing crisis today was not to discuss their disagreement with her proposal but to assert that Hillary has received contributions from subprime loan companies. Considering that Sen. Obama has received $1.18 million from subprime lenders and has taken more campaign contributions from the top ten issuers of subprime loans, that attack rings hollow as just words," the Clinton statement said.

The companies Clinton was referring to included Lehman, GMAC, Credit Suisse First Boston, Countrywide, WaMu, Citigroup, CBASS, Morgan Stanley, Centex and Goldman Sachs.

Clinton said Obama had received $434,420 from the top 10 issuers of subprime loans. Comparatively speaking, Clinton reported that she received $364,950.

Obama has previously announced that he will join with Sen. **Chris Dodd** to introduce legislation for a new FHA Housing Security Program, which will "provide meaningful incentives for lenders to buy or refinance existing mortgages, and to convert them into stable 30-year fixed mortgages so that homeowners facing foreclosure can keep their homes."

On the Republican side, McCain recently issued his own comments on the housing crisis, criticizing any proposed government bail out plans. In terms of policy changes, McCain said he opposes reducing the down payment requirement for FHA mortgages and in fact, supports an increase. He would also encourage increased capital in financial institutions by removing regulatory, accounting and tax impediments to raising capital.

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appropriate due diligence, mortgage broker agreements and ongoing monitoring of third-party relationships.

The OCC suggested that, with respect to brokered loans, banks should "have in place a process for review of written agreements between the borrower and the broker to ensure that the agreements conspicuously disclose the fees to be paid to the broker for its services, contain a specific request for such broker services at that fee, and include a signed and dated acknowledgment of receipt by the consumer before the broker commences services."

Although it isn't known if Wells Fargo's form was in any way "inspired" by the OCC's letter, it is not the first bank to issue such a form. Washington Mutual (WaMu) instituted its own mortgage broker disclosure form in the fall of 2007, and it looks as though more banks will be following suit.

Details of Wells Fargo form

On March 19, Wells Fargo issued a second newsflash with additional compliance information related to its new disclosure.

The newsflash indicated that the disclosure will require the broker to outline what compensation the broker is receiving for the loan, and how this amount will be paid.

"Brokers will need to be very clear that the fees discussed and agreed to at the onset of the relationship with the borrower will not change, with the exception of specific 'qualified changes' listed below," Wells Fargo said.

Changes to broker compensation will only be allowed in conjunction with one or more of the following qualified changes:

- Change in loan amount (increase or decrease)
- Loan has been re-locked
- Loan product has changed

Subsequent changes to broker compensation based on a "qualified change" will require a Mortgage Broker Fee Disclosure Addendum (re-disclosure) signed and dated by all borrowers and the broker.

The completed Mortgage Broker Fee Disclosure Addendum must be received by WFHM and/or WFHE at least one business day prior to the close/sign date.

Closing doc changes

Wells Fargo is also modifying the Closing Doc Form (CDF)/Broker Fee Sheet, to reflect and capture Mortgage Broker Fee Disclosure information. The new CDF/Broker Fee Sheet is required to prepare WFHM/WFHE closing instructions for the settlement agent. The CDF/Broker Fee Sheet must match the most recently signed Mortgage Broker Fee Disclosure for both the first loan and the second loan/line.

Any discrepancies between with CDF/Broker Fee Sheet must result in either:

(1) a re-disclosed Mortgage Broker Fee Disclosure if the discrepancy is due to a "qualified change," or

(2) a revised CDF/Broker Fee Sheet to match the most recent Mortgage Broker Fee Disclosure.

The WFHM/WFHE closing department will send closing instructions to the settlement agent based on the CDF/Broker Fee Sheet.

The settlement agent will prepare the HUD-1 based on the closing instructions and submit the HUD-1 to Wells Fargo for approval. In an escrow state, WFHM will not release funds to the settlement agent until a HUD-1 has been approved. In a non-escrow state, WFHM will not release final documents to the settlement agent until a HUD-1 has been approved.

Further, effective with new loan files received on or after April 1, 2008, Wells Fargo receivers will check each file for compliance. Loans not meeting the criteria outlined below will be delayed and not move forward until Wells Fargo is in receipt of a Mortgage Broker Fee Disclosure.

Points of compliance

Brokers must include a Mortgage Broker Fee Disclosure at submission, and ensure all of these requirements are met in order to ensure a smooth process:

The Mortgage Broker Fee Disclosure form must be fully complete, signed and dated by all borrowers and the broker.

The form must be the Wells Fargo Mortgage Broker Fee Disclosure. State-specific forms or forms from other wholesale lenders will not be accepted.

Borrower(s) must acknowledge how much, in dollars, the broker will be receiving by indicating these fee(s) in the top portion ("fees" section) of the first loan section and/or second loan section of the form.

Borrower(s) must acknowledge how those fees will be paid in exact dollar amounts by indicating this in the bottom portion ("options" section) of the first loan section and /or second loan section.

The total dollar amount in the "fees" section of the first loan must match the total of the dollar amount(s) listed in the "options" section of the first loan section.

The total of the "fees"/"options" sections must not exceed the broker price cap policy. Wells Fargo added that effective April 1, 2008, loans in Massachusetts may be eligible to collect a yield spread premium on newly received loans.

New Century's dangerous obsession: New report tells all

A recent report prepared for the U.S. Department of Justice has found fault with accounting firm KPMG for contributing to the April 2007 collapse and bankruptcy of subprime mortgage lender New Century Financial Corporation.

The report, filed on Feb. 29 by bankruptcy court examiner **Michael Missal**, found that "New Century engaged in a number of significant improper and imprudent practices related to its loan originations, operations, accounting and financial reporting processes. KPMG contributed to certain of these accounting and financial reporting deficiencies by enabling them to persist and, in some instances, precipitating the company's departures from applicable accounting standards."

The report said New Century had a "brazen obsession with increasing loan originations, without due regard to the risks associated with that business strategy."

Risky business

It noted that the loan production department was the dominant force within the company, and trained mortgage brokers to originate loans in the aptly named "CloseMore University."

"Although a primary goal of any mortgage banking company is to make more loans, New Century did so in an aggressive manner that elevated the risks to dangerous and ultimately fatal levels. The increasingly risky nature of New Century's loan originations created a ticking time bomb," the report said.

The report detailed several instances in which senior staff had reportedly tried to advise management of the risks and failures of certain ventures, and were allegedly rebuffed.

In 2004, for example, a senior officer questioned the "sticker shock" that some borrowers were experiencing in regards to loans with low initial "teaser rates." Another leading employee questioned the proliferation of stated income loans the company was originating. One senior officer said that New Century's practice of making frequent exceptions to its underwriting guidelines was the "number one" problem. And New Century's former chief credit officer said that the company had "no standard for loan quality" beyond whether or not the loans could be sold into the secondary market.

Further, in early 2006, a senior officer reported that the performance of the "80/20" loans the company was originating in bulk was "horrendous."

Despite these concerns, the report said, "Senior management turned a blind eye to the increasing risks of New Century's loan originations and did not take appropriate steps to manage those risks."

The report also said that New Century's management "did not set an appropriate 'tone at the top.' Many former New Century employees rationalized the company's actions with the belief that the company was conducting business in the same manner or even better than its competitors."

The report noted that even if New Century's practices were not outside the norm of the industry, that "this would not absolve anyone from failing to follow applicable accounting rules, legal standards or prudent business practices."

New Century is not commenting on the report's findings, beyond stating that its release will allow the bankruptcy process to move forward.

KPMG's role

Regarding KPMG, the report said that it may have recommended improper changes to the repurchase reserve calculation that were made in late 2006. The report also said that KPMG "improperly acquiesced in New Century's reliance upon aggressive or stale assumptions in its residual interest valuation models," and that KPMG "failed to insist that New Century cure significant internal control deficiencies with respect to the valuation of residual interests."

At times, the report said, KPMG "acted more as advocates for New Century, even when its practices were questioned by KPMG specialists who had greater knowledge of relevant accounting guidelines and industry practice."

For example, the report noted, "When one KPMG specialist persisted in objecting to a particular accounting practice on the eve of the company's 2005 Form 10-K filing — an objection that was well-founded and later led to a change in the company's practice — the lead KPMG engagement partner told him in an e-mail: 'I am very disappointed we are still discussing this. As far as I am concerned we are done. The client thinks we are done. All we are going to do is piss everybody off.'"

KPMG has strenuously denied it ignored accounting rules in its auditing for the company, which resulted in senior New Century executives benefiting from generous bonuses that would otherwise not have been paid – and which otherwise masked the real financial condition of the lender.

For example, the report indicated that based on accounting errors, New Century's senior management received financial performance bonuses in 2005 that were at least 300 percent more than they should have been, while other officers received bonuses that were approximately 130 percent to 279 percent higher than appropriate.

Lessons learned

"Regardless of the truth in this matter, the

appearance of sins, whether of omission (error) or commission (fraud), can sully the reputation of any professional services firm," said **Rodney Nelsestuen**, senior analyst at TowerGroup.

Inci Kaya, a quantitative analyst at TowerGroup, cited reputation risks to both financial institutions and their hired consulting firms because of the challenges of satisfying customers in a marketplace where consultancy work is increasingly competitive. "The pressure to find in favor of those who hire your firm creates an opening and, in some cases, an incentive for moral lapse," she said.

For financial institutions, TowerGroup stresses the importance of avoiding situations that may lead to conflicts of interest or put undue pressure on their professional services providers. Beyond specific areas of concern such as accounting, the following steps are fundamental elements of a comprehensive approach to integrated risk management. At the core, it is a board-level responsibility to demand that the institution:

- Maintain strong internal controls with independence and with arm's-length audit processes, whether internally or externally provided.

- Avoid complacency with chosen providers by maintaining a rigorous selection process. Demand high levels of integrity from key officers.

- Maintain a policy of rewarding whistle-blowing instead of allowing a culture of fear to permeate the institution.

- Insist on the conservative application of accounting rules instead of accommodating a more liberal interpretation in the face of pressure to demonstrate improved financial results.

- Understand that while fiduciary responsibility may uncover devastating news about an institution's finances, early intervention is still the best hope for taking corrective measures to remedy the situation both internally and externally.

Mortgage co. fights for rights to vanity phone number

The U.S. Court of Appeals, Third Circuit in Philadelphia has remanded a lawsuit back to district court to determine whether the Business Edge Group violated Federal Communications Commission (FCC) laws by targeting and subscribing to a vanity toll free number, then selling the number to Champion Mortgage Co.

The question may never have reached the courts. But after Champion Mortgage tried breaking a joint agreement to use the number, Business Edge set the legal wheels in motion by filing a lawsuit against the mortgage company, alleging breach of contract for terminating the agreement while still owing $375,000.

The U.S. District Court for the District of New Jersey granted judgment for targeted business based on the premise that Business Edge violated a FCC regulation which prohibits entities from acquiring toll free telephone numbers to sell — and from hoarding the numbers.

Business Edge appealed. And after hearing arguments from both sides on Jan. 3, the Court of Appeals Third Circuit issued its finding on March 11.

"The issue we address is whether Business Edge's actions violated an FCC regulation which prohibits entities from acquiring toll free telephone numbers in order to sell them and from hoarding toll free telephone numbers," Circuit Judge **Julio M. Fuentes** said. "We conclude that Business Edge did not sell the telephone number at issue to Champion and that the case must be remanded for a determination of whether Business Edge engaged in hoarding."

In the beginning

At some point prior to 1998, Business Edge acquired the toll free telephone number 1-800-242-6740, referred to as "the Number." **Sheldon Kass**, president of Business Edge, testified during a deposition that he acquired the Number because the number also spelled the word "champi0n" and had potential to be used by Champion Mortgage.

After subscribing to the Number, Business Edge routed all calls to the Number to an unnamed mortgage company — then contacted Champion, stating it had an 800 number that spelled "Champi0n" and that when people misdialed Champion's toll free telephone number, using a "zero" rather than the letter "o," they were being routed to another mortgage company, court records show.

When Champion marketing manager **Cindy Stancavish** called the Number to validate Business Edge's claim, she found that another mortgage company did not identify itself, leading callers to believe they were speaking with Champion.

This gave even more incentive to the mortgage company to use the Number.

First offer rejected

Because of the perceived loss of business, Champion offered to purchase the number from Business Edge for $60,000, but Business Edge rejected the offer. The parties then entered into the 1998

Agreement pursuant to which Business Edge would route calls to the Number to Champion for 10 cents per minute, plus $3 per each customer that called the Number.

The purpose of the 1998 Agreement was to set up a trial period to show Champion the volume of traffic to the Number so it could determine whether to enter into a longer-term agreement with Business Edge, according to court records.

Business Edge and Champion signed the 1999 Agreement, whereby Champion would pay $25,000 per month for five years in exchange for Business Edge routing calls made to the Number exclusively to Champion.

The agreement was in effect from August 1999 through December 2002. But in January 2003, Champion sent Business Edge a letter stating that the contract violated an FCC regulation, and demanded reimbursement for the payments that had been made on the contract.

IOU $375,000

Despite the letter, Champion continued to pay on the 1999 Agreement through April 2003, but failed to pay the final $375,000 remaining on the 1999 Agreement when the contract was terminated.

Business Edge then filed a complaint in state court, claiming breach of contract for Champion's failure to pay the final money owed. Champion removed the case to federal court on diversity grounds, arguing the case be transferred to the FCC under the doctrine of primary jurisdiction because resolution of the case requires interpretation of FCC rules and policies.

In contrast, Business Edge contended that there was no technical sale of the Number, so there could be no FCC violation. The district court determined on the eve of trial that no material issues of fact were in disput,e and the case could be disposed of as a matter of law.

The district court ruling indicated the court found it was just as well suited as the FCC to determine the principal issue in the case. The district court held that "toll free subscribers shall not hoard toll free numbers" and that "no person or entity shall acquire a toll free number for the purpose of selling the toll free number to another entity or to a person for a fee."

The district court then focused on whether Business Edge acquired the number in order to sell it to Champion and held that the 1999 Agreement violated the FCC.

"Finding that both parties had unclean hands in creating the 1999 Agreement, the court excuses Champion from further payments under the contract and denies restitution of the payments previously made," the district court ruled.

Business Edge appealed.

Hoarding numbers

The Court of Appeals considered "whether the 1999 Agreement should be invalidated because Business Edge improperly hoarded toll free telephone numbers," Judge Fuentes said. The FCC defines "hoarding," as "the acquisition of more toll free numbers than one intends to use for the provision of toll free service, as well as the sale of a toll free number by a private entity for a fee."

"It is possible that Business Edge acquired more numbers than it intended to use for the provision of toll free service, in violation of the prohibition on hoarding," Judge Fuentes said. "Given the record before us, we believe Business Edge clearly violated the spirit of the law as it did not intend to use the Number for its own customers."

But the Court of Appeals also found that the record was inadequate to determine whether Business Edge actually engaged in hoarding – and remanded the case to district court.

Mortgage litigation: Trends to watch

Some of legal and regulatory risks impacting the financial services industry have been following an alarming trend for the past few years. Understanding those trends and what cases have helped to set them can help brokers and lenders understand how to avoid a lawsuit.

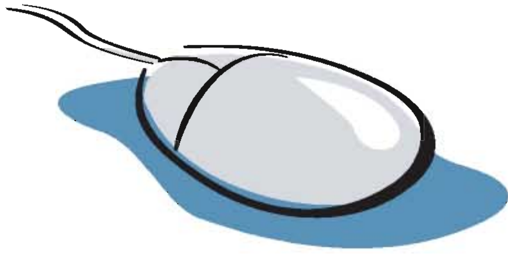
Jeff Nielsen, managing director of Navigant Consulting, said mounting subprime losses, increased media attention and increased Congressional attention have all combined to cause an increase in civil litigation and government investigations. In fact, of the subprime-related federal filings in 2007, 43 percent were borrower class actions. The borrower claims generally related to inadequate disclosure through the origination process, improper charges, discriminatory prices or unearned fees. Nielsen said 32 percent of the subprime-related filings last were against mortgage brokers and loan correspondents.

Nielsen said the public's need to place blame for mortgage crisis has helped to create the trends in litigation the industry has been facing. And he doesn't expect that to disappear anytime soon.

Matthew Previn, partner with Buckley Kolar LLP, said three major developments that have helped to set the trends should be monitored, including the expanded use of the disparate impact theory, servicers' ability to exercise foreclosure rights and regulation through enforcement.

The trends

Previn said the firm has noticed a significant increase in disparate impact



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claims based on nationwide studies and aggregated Home Mortgage Disclosure Act (HMDA) data. The lawsuits don't generally refer to the specific HMDA data provided by an individual lender who sued, but aggregated across the industry.

"A good example of that is case law brought by the NAACP against 18 lenders," he said. It's a case we think has significant flaws based on the fact that the allegations are aggregated across the mortgage industry and don't target any specific practice."

Some of the companies named in the suit included Countrywide, Ameriquest, and Wells Fargo. The NAACP named specific studies and public statements from government agencies and consumer groups that alleged blacks were more likely to get higher-interest loans than whites or other borrowers. The complaint, however, didn't mention any specific examples of borrowers who were discriminated against.

According to a 2006 study by the Center for Responsible Lending, African-Americans were 31 percent to 34 percent more likely to receive higher rates and more expensive subprime loans than whites, even when creditworthiness and credit risk were equal, the NAACP said in their suit.

"These statistical disparities are not mere happenstance, but instead result from a systematic and predatory targeting of African-Americans," the lawsuit stated.

ECOA and FHA

Previn has also noticed an expanded use of disparate impact theory in Fair Housing Act and Equal Credit Opportunity Act cases. Challenges have been noticed when lenders decide not to make loans on row houses, houses valued below a specific amount and other property types. These suits have challenged underwriting criteria established by lenders. Some of the cases have been settled, while others are outstanding, Previn said.

"We are also seeing challenges to underwriting policies not to lend in certain jurisdictions, for example, fair lending claims are being brought based on lender's policies not to make or purchase loans secured by properties located in Puerto Rico," he said.

Several similar suits have been filed as a result of not making or purchasing loans secured by properties on Indian reservations. The most prevalent form of fair lending litigation Previn has noticed is discretionary pricing. "This is really the heart of most of the more serious claims we've been defending. These are claims based on allegations that a racially neutral discretionary pricing policy has a disparate impact on minority borrowers."

Alleged broker mark-ups are just one examples of this type of litigation. Mortgage brokers should be cautious of a trend like this because these suits conclude a lender is responsible for a broker's alleged discriminatory actions, Previn said. That's something that could impact the future of business relationships of brokers and lenders.

The defenses

Previn said that many of the federal circuits have endorsed disparate impact theory of liability under the FHA and ECOA based on the reasoning of Title 7 Jurisprudence premised on an understanding of the broad purpose of the statute. In *Smith v. City of Jackson*, the Supreme Court clarified that the disparate impact theory is grounded in the statutory text of Title 7.

The Supreme Court voted unanimously that the prohibition of discrimination of someone because of race supports only disparate treatment claims, but not disparate impact claims. There are two separate provisions of liability in Title 7. The Supreme Court said one of those provisions supports the disparate treatment of liability, while the other supports disparate impact liability because of the provisions' language, Previn said.

"This is significant because neither the FHA nor ECOA contains the effect language that the Supreme Court identified in Title 7 as creating the disparate impact cause of action," Previn said. "Both statutes contain only the language the Supreme Court voted supports only the disparate treatment claims. No circuit has since revisited whether FHA and ECOA allow for disparate impact claims in light of *Smith v. City of Jackson*."

However, there is a District of Columbia opinion in an ECOA case that the statue should not be read to recognize disparate impact liability.

Buckley Kolar has raised the issue in a couple of pending cases, Previn said. "It remains to be seen how receptive the courts will be to this defense. I actually believe it's a strong argument based on the text of the statute. If it makes its way to the Supreme Court, I believe it will be found that the FHA and ECOA do not support disparate impact liability. The problem is, district courts will be less likely to make new law and potentially ruffle feathers, given the sensitivity surrounding mortgage lending right now."

Other defenses raised by fair lending cases include moving to dismiss on the basis of *Bell Atlantic Corp. v. Twombly*, a case in which the Supreme Court clarified the pleading standard in federal court.

More attorneys have been moving to dismiss on the basis of Twombly when allegations are not lender specific should fail under the clarified standards. The courts of appeals are still working their way through what Twombly means for fair lending cases, so Previn said it's too early to tell what the case will mean for moving to dismiss similar cases in the future.

Mortgage industry bashes new RESPA rule

It appears that many in the mortgage industry are not happy with the new Good Faith Estimate and corresponding changes to fee disclosures. Many of the comments that HUD has received so far on its new RESPA reform rule have focused around perceived discrepancies in the way the rules treat mortgage brokers versus lenders and other loan originators.

Regarding fairness and equality, **Steve Evans** of Stewart Mortgage Services Inc. said, "I am all for transparency in our industry, rooting out unethical people and providing an easier way for borrowers to shop loans, but how can we do this if the banks aren't regulated in the exact same way? Bank originators don't need to, and do not, disclose YSP or other fees and this gives them a HUGE opportunity to hide compensation from the borrower. If the mission is truly for transparency in the industry and protecting the borrower, then make the banks follow the same rules! Anything short will not accomplish your goals."

While commenter **Mark Vogel** acknowledged that the RESPA rule had some good points, he said, "I'm still unclear as to why we keep TARGETING mortgage brokers. I'm sick and tired of the continued attacks on the broker community. …You keep targeting the yield spread premium. …Why are you trying to close down the mortgage broker? Are you trying to create a monopoly for the banking industry? Do you realize that you will be forcing people to only have the opportunity to obtain a mortgage loan from a small list of banks." Vogel added, "Stop putting all the disclosures on the mortgage broker. Put everyone on the same playing field. Banks also know their profit on the loans just like we do and they should have to report the income on the HUD as well."

But **Larry M.**, a former broker who has been a loan officer with a "major lender" for eight years, made the point that "the large majority of my fellow mortgage professionals are straight 100 percent commission-based employees. In other words, we are self employed. If we're not getting and closing the business then we don't make any money to feed our families and pay our bills."

He noted that his employer keeps 40-50 percent of the revenue he generates and added that he is capped on the amount of additional compensation he could generate through an origination point.

"When I compete with brokers, I seldom charge an origination point so that I have a chance of capturing that clients business. Brokers get paid off points and YSP. Brokers and the mortgage bankers working for that broker, can beat my rate and still make good YSP because of the wholesale relationship with a lender. At one point in this business, I would get beat on a loan/rate by my own company....because a broker was using our wholesale rates," he said.

"Brokers should not be required to give back the YSP. They have overhead just like any small business. To regulate and institute new laws, requirements, training, etc. is fine. But to regulate my pay — to tell a self-employed professional how much money they can make or cannot make, borders on Socialism," he said. "If compensation regulations stifle the very nature of commerce, then eventually every "person" — and I use this word not "professional" — will be an order taker. If you think there are problems now with our industry, just think what you'll get when you're sitting in front of $12/hr. bank employee."

GFE simplification?

Larry M. did agree, however, that a uniform GFE or Closing Cost Estimate should be used. "I say this because there is a vast majority of the general public that won't take the time to read or perform any due diligence prior to shopping for a mortgage loan. This has always been true and it will remain so. Therefore I do agree that 'some' form of standardization is needed on this document. The overall disclosure process is an attorney's dream. This will never be simplified. As long as attorneys review and have their say in this part of the process...it will never be streamlined," he said.

Vogel, however, criticized the new GFE, saying it was "not simplified and is more confusing." He urged HUD, as NAMB and other industry groups have done, to make a standard GFE that matches the HUD-1 Settlement Statement.

"Do not create any additional forms as more paperwork is not helping," he said. "It just creates more confusion."

Pushing for greater simplicity was **Cindy Meyer** of All California Mortgage, who told HUD, "I really feel like the whole thing is being approached incorrectly. When I was a loan assistant and the borrower seemed to be confused, I would have them recite the details of their loan program to me. Borrowers have to sign and read so many forms that they become numb and now we are going to be giving them MORE to read, sign and listen to."

Thus, Meyer offered a suggestion: "Why not have a blank form that the borrower fills out explaining the loan program, payment, etc? This is really the only way to make sure that they know what they are getting into. If they fill out the form incorrectly, then the loan advisor will know what information they are not understanding. This, to me, seems better than having sign a ton of forms and hoping that it is all sinking in."

For more on these initiatives, log on to MortgageLawCentral.com.

Senate strips bankruptcy roadblock from foreclosure bill

On April 2, Senators **Chris Dodd** (D-CT) and **Richard Shelby** (R-AL), Chairman and Ranking Member of the Senate Committee on Banking, Housing and Urban Affairs, announced that they have developed a bipartisan agreement to help address the nation's housing crisis.

The House plans to offer its own version of the legislation.

The foreclosure bill being considered by the Senate contains the following provisions designed to address the problems faced by families and their communities in light of the foreclosure crisis:

- **FHA Modernization**. To ensure that additional families can access the FHA program, which provides safe, fixed-rate mortgages, significant FHA reform is included to modernize, streamline and expand the reach of the FHA program. Under this bill, the FHA loan limit is increased from 95% to 110% of area median home price with a cap at 132% of GSE limit (currently, $550,000), allowing families in all areas of the country to access homeownership through FHA. Downpayments of 3.5% will be required for any FHA loan and counseling requirements are enhanced to help provide for stable homeownership.

- **Assisting Communities Devastated by Foreclosures.** Homes that have been foreclosed upon and are sitting unoccupied lead to declines in neighboring house values, increased crime and significant disinvestment. To ensure that communities can mitigate these harmful effects of foreclosures, $4 billion is provided to communities hardest hit by foreclosures and delinquencies. These supplemental Community Development Block Grant Funds will be used to purchase foreclosed homes, at a discount, and rehabilitate or redevelop the homes to stabilize neighborhoods and stem the significant losses in house values of neighboring homes.

- **Providing Pre-Foreclosure Counseling for Families in Need**. To help families avoid foreclosure, this bill provides $100 million in additional funding for housing counseling. These funds will be distributed by the Neighborhood Reinvestment Corporation by the end of 2008 to ensure families can quickly get the help they need. As many as 250,000 additional families connect with their mortgage servicer or lender to explore options that will keep them in their homes as a result of these counseling funds.

- **Enhancing Mortgage Disclosure**. To ensure that consumers are provided with timely and meaningful disclosures in connection with mortgages, the bill expands the types of home loans subject to early disclosures (within three days of application) under the Truth In Lending Act (TILA) including refinancings. The bill requires that disclosures be provided no later than 7 days prior to closing so borrowers can shop for another loan if not satisfied with the terms. The bill requires a new disclosure that informs borrowers of the maximum monthly payments possible under their loan, and also increases the range of statutory damages for TILA violations from the current $200 to $2000 to $400 to $4000.

- **Preserving the American Dream for Our Nation's Veterans**. To assist returning soldiers avoid foreclosure, this bill lengthens the time a lender must wait before starting foreclosure from three months to nine months after a soldier returns from service and also provides returning soldiers with one year relief from increases in mortgage interest rates. In addition, the Department of Defense is required to establish a counseling program to ensure veterans and active service members can access assistance if facing financial difficulties. Also included is a provision that increases the VA loan guarantee amount, so that veterans have additional homeownership opportunities.

- **Standard Property Tax Deduction**. To make tax relief available to all American homeowners, the bill will provide a standard deduction – $500 for single filers and $1,000 for joint filers – for the 28.3 million non-itemizers who pay property taxes. Present law allows only those who itemize deductions on their Federal tax returns to deduct state and local property taxes from their income.

- **Mortgage Revenue Bonds**. To provide for refinancing of subprime loans, mortgages for first-time homebuyers and multifamily rental housing, $10 billion of Federal tax-exempt private activity bond authority is included in this bill. The measure also exempts interest earned on the bonds from the alternative minimum tax.

- **Extension of Net Operating Loss Carryback**. To aid homebuilders and other businesses hit hardest by the economic slump, this bill will extend a law allowing corporations to apply excess net operating losses to tax returns from prior profitable years and receive any applicable refunds. For 2008 and 2009 losses, the provision would extend the "net operating loss (NOL) carryback" to four years (back to 2004 and 2005, respectively) from the two years currently in law. Measures to prevent companies from abusing the intent of the provision are also included.

- **Tax Credit for Purchase of Homes in Foreclosure**. To encourage the purchase of homes already in foreclosure and of homes on which foreclosure has been filed, this bill creates a $7,000 tax credit for buyers of such homes, to be claimed over two years. Homes in foreclosure bring down the value of property nearby. Encouraging the purchase of more homes in foreclosure will restore property values for all homeowners.

Industry News

Originators could get own federal regulator under new plan

The U.S. Treasury Department is thinking big.

On March 31, with the goal of improving competitiveness, advancing tools for market stability and enhancing financial innovation, the Treasury released a dramatic blueprint for a modernized financial regulatory structure.

Among the slew of recommendations was a proposal for the creation of a new Mortgage Origination Commission (MOC) to evaluate, rate and report the adequacy of each state's licensing and regulation of the mortgage origination process.

The Treasury recommended retaining state-level regulation of mortgage origination practices, but would create a new federal-level commission, the MOC, which would be led by a director appointed by the President.

The commission membership would include federal banking regulators and appropriate state representation. The Treasury said that legislation would be needed to set forth or task this Commission to establish minimum standards for originators, including personal conduct and disciplinary history, minimum educational requirements, testing criteria and procedures, and appropriate license revocation standards.

ABC's of the MOC

The MOC would provide important information to the marketplace about the strength of state's mortgage compliance standards, said Treasury Secretary **Henry Paulson Jr.**

"Mortgage origination is one of the best case studies for the importance of regulatory structure. It raises the question of the proper balance between federal and state oversight, and requires a balancing of innovation, consumer choice and expanded access to credit with protecting consumers from predatory lending and deceptive or incomplete disclosure practices," Paulson said.

"Simply put, the mortgage origination process was broken," Paulson said. "We are aggressively addressing the immediate problem, working to increase the availability of affordable mortgage financing, prevent avoidable foreclosures and to minimize the economic disruption of the housing correction. We concluded that it was also appropriate to put forward a proposal to address the policy issues arising from the current turmoil, to avoid a recurrence of recent events and to respond to the fact that a very large percentage of the problematic subprime mortgages originated in the past four years were originated by state-regulated entities."

The MOC would evaluate, rate, and report on each state's adequacy for licensing and regulation of participants in the mortgage origination process. These evaluations would grade the overall adequacy of a state system by descriptive categories, indicating a system's strength or weakness.

"These evaluations could provide further information regarding whether mortgages originated in a state should be viewed cautiously before being securitized," Paulson said. "This powerful commission, coupled with the Federal Reserve's strong regulatory proposal regarding the HOEPA rules, should go a long way in preventing recent issues from recurring."

The blueprint calls for the federal government to ensure that each state reports and grades the personal conduct and disciplinary history of each licensed mortgage salesperson, requires minimum educational requirements for mortgage salespeople establishes testing criteria and procedures for mortgage salespeople implements license revocation standards for mortgage salespeople who violate the rules.

The blueprint also includes short, intermediate and long-term recommendations to achieve an improved financial regulatory structure.

Triple threat

Intermediate-term recommendations focus on eliminating some of the duplication in our existing regulatory system. The long-term recommendation is to create an entirely new regulatory structure using an objectives-based approach for optimal regulation. The structure will consist of:

* **A market stability regulator** – This position would be filled by the Federal Reserve because the agency's role can continue through traditional channels of implementing monetary policy and providing liquidity to the financial system. The Federal Reserve would be provided with a different and critical regulatory role with broad powers focusing on the overall financial system.
* **A prudential financial regulator** – This position combines all federal bank charters into one charter and consolidates all federal bank regulators into a single prudential regulator.
* **A business conduct regulator** – This regulator would be responsible for monitoring business conduct across all types of financial firms, including key aspects of consumer protection, such as disclosure, business practices, chartering and licensing of certain financial firms.

Mortgage industry gives thumbs-up

Industry reaction to the blueprint has been mostly supportive.

"This is the most sweeping proposal for restructuring the financial regulatory environment since the Great Depression," said **Gibran Nicholas**, chairman of the CMPS Institute. "This is the most effective, comprehensive, and well-reasoned proposal we've seen from the government since the mortgage, housing, and credit crisis began nearly nine months ago."

Nicholas said that one major disappointment in the blueprint was that mortgage salespeople who work for federally chartered banks would not be subject to the same licensing rules as the rest of the industry. "Although federally chartered banks have their own guidelines that need to be followed, all individuals who sell mortgages to consumers should be required to follow the same guidelines," he said.

George Hanzimanolis, president of the National Association Mortgage Brokers (NAMB), expressed support for the MOC, saying the effort appears to compliment efforts by the House and Senate to create a federal clearinghouse or registry for all loan originators.

In defining the role of the MOC, NAMB believes federal regulators should closely follow the guidelines established in H.R. 3915 and S. 2595. NAMB also said the MOC should have oversight over all mortgage originators, including those employed by subsidiaries of federally chartered banks.

NAMB has long contended that real consumer protection can be achieved by creating a single national registry that includes all mortgage originators; and to create national standards that include professional education, and passage of an examination and criminal background check.

The Mortgage Bankers Association (MBA) likewise voiced support for the blueprint.

" Today's report will initiate a crucial policy discussion, one which is especially important at this time of turmoil in the credit markets," said MBA Chairman **Kieran P. Quinn**.

"One of the most significant problems for the mortgage industry and its customers is the explosive growth of inconsistent state regulations," Quinn said. "We share Treasury's goal of more effective mortgage originator oversight. Specifically, we support more rigorous licensing, nationwide registration for all originators, and mortgage broker net worth and bonding requirements."

A step forward

Rep. **Barney Frank**, chairman of the House Committee on Financial Services called the Blueprint a "constructive step forward," but said the plan goes too far in diminishing the role of the states, and not far enough in conferring needed new powers on the Federal Reserve over non-bank financial institutions for which they now have greater responsibility.

Illinois AG sues broker over padded loans, undisclosed fees

Advantage Mortgage Consulting, Inc. and President *Robert Enright* are facing a lawsuit filed March 26 by Illinois Attorney General **Lisa Madigan** that alleges deceptive practices.

Madigan's lawsuit alleges that the defendants employed a variety of schemes to convince consumers— including many on the brink of foreclosure — that they would pay lower monthly mortgage payments when, in fact, their monthly rates later increased significantly.

Specifically, the defendants allegedly used deceptive refinancing schemes, padded loans with higher than stated fees, failed to disclose prepayment penalties and brokered adjustable rate mortgages with consumers who believed they were agreeing to fixed-rate mortgages, according to the complaint.

"Advantage Mortgage Consulting deceived consumers, convincing them to enter unknowingly into mortgages they simply could not afford or did not need," Madigan said. The lawsuit was filed on the heels of 20 complaints filed with the office's fraud bureau against the company.

The suit asks the court to rescind the contracts signed as a result of these deceptive practices and offer full restitution to affected consumers. Finally, Madigan's suit asks the court to order the defendants to pay all costs associated with the investigation and prosecution of the lawsuit.

The suit would also seeks an order prohibiting the company from engaging in deceptive business practices and imposing a civil penalty of $50,000 for each violation committed with the intent to defraud and a $10,000 penalty for each instance where a violation was committed against a person 65 years of age or older.

Washington makes mortgage fraud a felony

Washington State Governor **Chris Gregoire** on March 21 signed legislation that will purportedly help Washingtonians find more affordable housing and offer protections against foreclosures.

In response to a souring housing market last fall, Gregoire formed the Task Force for Homeowner Security to evaluate instability in the national subprime market. The measures she signed stem from the task force's recommendations.

One increases the Washington State Housing Finance Commission's debt limit, set in law, from $4.5 billion to $5 billion. This change will allow the commission to issue additional bonds to fund its low-income, single family, first-time homebuyer programs and its low-income, multi-family housing development programs.

A second measure strengthens consumer protection, prohibits certain lending practices and requires clear, concise disclosure of a loan's terms. The bill has teeth: It makes mortgage fraud a felony.

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service provider.
It's not just about
service anymore.

In 2000,
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