Blog Talk Radio Show

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Q & A with Lykken on Lending Team and Glen Corso

General Questions

Q: Throughout the MBA analysis of this legislation the term “loan originator” is used. Sometimes it seems to mean an origination company and sometimes a commissioned loan officer or broker. When they say “loan originator” do they ever mean the company?

A: *The term "loan originator" as used in the Dodd-Frank act (DFA) means either the loan officer or broker, not the mortgage company. However a term that DFA uses more frequently, "mortgage originator", can mean the loan officer, broker or the mortgage banking company in table funding transactions only.*

Q: Whose unique identifier will be put on loan documents, the company’s or the individual’s?

A: *The individuals'.*

Q: When will any of the new provisions begin to change the origination process? Specifically LO compensation? Skin in the game?

A: *Short answer is most likely in 18-24 months after the President signs the law. However the longer answer is it could be as short as 12 months (considered very unlikely) or as long as 42 months (also considered very unlikely.)*

Q: Will the rules put out by CFPB preempt State consumer laws?

A: *NO. The states can enact laws that are tougher than the CFPB regulations.*

Q: Will origination companies be able to operate under a standard set of rules across State lines?

A: *Only bank-owned companies will be able to do that and the law makes it harder for the federal banking regulators to preempt state laws in the future.*

Q: Will National Bank originators be able to operate under a single set of rules across State lines?

A: *Certainly more than independent mortgage banking companies will be able to. However as noted it will be harder in the future for federal regulators to preempt state laws.*

Loan Officer Compensation

Q: Will the new provisions prohibit an LO from collecting more commission than usual for loans that are closed at a rate higher than the par rate? Can the company receive more, but not share it with the LO?

A: *The DFA states that an originator's compensation (loan officers and brokers) cannot vary according to the terms and conditions of the loan, except for the principal balance. The company can receive more and not share it with the LO. The law also specifically allows volume incentives.*

Q: What is the "usual" commission rate?

A: *The law does not talk about "usual" commission rates.*

Q: Can that vary by loan size, by product, by LO, by branch, by region, by company?

A: *The definitive answers will have to wait for the regulations. There is nothing in the law that prohibits a company from varying compensation by loan officer or by region.*

Q: Can a LO give up part of his commission to give his customer a better deal?

A: *The law prohibits a loan officer's compensation from varying according to the terms and conditions of the loan. If an LO gives up part of their commission to give the customer a better deal then the LO's compensation is varying according to the terms and conditions of the loan, which is in violation of the law.*

Q: Can an LO who is also a net branch manager receive the net branch profit that results from their personal production, as they do now?

A: *The way the law is written the answer would appear to be no if the net branch profit is calculated in a way that it can vary based on the terms and conditions of each loan. DFA prohibits, for any mortgage loan, a mortgage originator from directly, or indirectly, receiving compensation that varies based on the terms and conditions of the loan.*

Q: Can they get any extra profits that come from other LOs production?

A: *We will have to wait for the regulations to answer this definitively, but the way the law reads is problematic. An LO who is also a branch manager, would fit the law's definition of a "mortgage originator". And the law states that for any loan a mortgage originator may not receive compensation directly or indirectly that varies based on the terms and conditions of the loan. The law does not say that has to be a loan that the originator worked on personally. It is possible the regulator could interpret the law that way, but there is no guarantee they will.*

Q: Can company owners receive profits from their own production above the normal commission they would earn as commissions?

A: *DFA specifically exempts secondary marketing profits from the sale of closed loans from the prohibitions on compensation varying according to the terms and condition of the loan. So if the company is selling closed loans the profits it earns from those sales are exempt from the prohibition and the profits can be distributed to the owners in the normal course of business. If the company is a mortgage broker then the prohibition would apply.*

Q: If an FHA loan is more profitable for a origination company than a conventional, but more costly for the borrower, is it "steering" to use FHA instead of conventional financing?

A: *Mortgage originators, including mortgage banking companies, are prohibited from steering consumers to loans that the consumer lacks a reasonable ability to repay, that have predatory characteristics or that are qualified mortgages under the ability to repay test to mortgages that are not qualified mortgages. So if steering the consumer from a conventional loan to an FHA loan violates any of those standards it would be prohibited.*

Q: If a Creditor can receive compensation on the sale of a closed loan, can the creditor share those profits with the LO?

A: *No since the law prohibits the originator from either directly or indirectly receiving compensation that varies on the terms and conditions of the mortgage.*

Q: If a LO quotes a rate and price to a customer based on the standard rate and price offered on his Company's price sheet, but the price for that rate improves before the loan is locked by the LO can the LO participate in the improvement?

A: *Since interest rate is a term and condition of the loan, and since the LO's compensation cannot vary based on a term or condition, except principal balance, the answer is no.*

Skin in the Game/Risk Retention

Q: Will there be any required Risk Retention on Ginnie, Fannie or Freddie loans?

A: *All FHA, VA and USDA guaranteed loans are exempt from risk retention. Since these are the only loans that can go into Ginnie Mae pools, Ginnie Mae MBS are exempt from risk retention. For all other MBS, including MBS guaranteed by Fannie Mae and Freddie Mac, loans backing the MBS will have to meet the qualified mortgage exemption in the law in order to be exempt.*

Q: Will Risk Retention be required on Jumbo loans?

A: *Securities backed by jumbo loans will be exempt from risk retention if all the jumbo loans in the pool meet the qualified mortgage risk retention exemption in the law.*

Q: For loans which meet the definition of loans for which risk must be retained, who retains it, the originator or the issuer of the security?

A: *The regulators (the federal banking regulators, the SEC, FHFA and HUD) will decide whether both the securitizer and the originator will have to retain risk on securities that are not exclusively backed by loans that are exempt from risk retention.*

Q: Can it be split and if so, can the split be negotiated by the buyer and the seller?

A: *The regulators will determine the split through regulation.*

Q: What if it is held in a Bank's portfolio and not securitized?

A: *Risk retention only applies to loans that are securitized and sold.*

Q: If a lender makes a loan that is not a "qualified mortgage" that it keeps in its portfolio, is its capital requirement any higher than if it were a "qualified mortgage"?

A: *DFA does not make any changes to bank capital requirements based on whether a loan is subject to, or exempt from, risk retention. However we cannot rule out that the federal banking regulators might make such changes in the future.*

Q: Who is the issuer in an assignment of trade (AOT) transfer of loans for an originator to an aggregator?

A: *DFA imposes risk retention on securitizers , not issuers. However the way the law defines securitizer could include the originator in an assignment of trade transfer of loans. Securitizers are defined as the issuer of an asset-backed security, or the person who organizes an asset-backed security transaction by transferring or selling, either directly or indirectly, assets to the issuer of an asset-backed security. We will have to wait for the regulations to more definitively answer that question.*

<u>Appraisals</u>

Q: Is HVCC going away?

A: *DFA amends TILA to require the Federal Reserve to issue interim final regulations on appraisal independence within 90 days of the date of enactment of DFA. Upon issuance of those regulations HVCC goes away. The interim final rules will then be replaced at some point by rules jointly issued by the Federal banking agencies, FHFA and the Consumer Financial Protection Bureau.*

<u>Underwriting</u>

Q: Will portfolio lenders be prohibited from making "good ole boy" loans? Will they be required to fully document their loan decisions with income verification, etc.?

A: *All loans will be subject to an ability to repay test under TILA. In order to satisfy the ability to repay test a lender will have to fully document income and assets of a borrower. However for banks operating in rural areas there will be more flexibility on portfolio loans with respect to deferral of principal repayment, balloon loans and qualifying borrowers for ARMs.*

Q: Will Minimum Standards apply?

A: *The regulations implementing the ability to repay test will be issued by the Consumer Financial Protection Bureau and will apply to all lenders and all loans.*

Q: Will the borrower be able to avoid foreclosure because the full underwriting was not done?

A: *Consumers will be able to raise the ability to repay test and any alleged violations as a defense to a foreclosure action with no time limit on when the defense can be raised.*

Q: The Ability to Repay section of the Act says that you should not consider the equity in the property being mortgaged when determining the ability to repay the loan. Does this say that you will no longer be able to consider LTV in qualifying a borrower for a loan?

A: *Nothing in DFA prevents lenders from setting a minimum downpayment, or requiring a certain level of down-payment. In order to satisfy the ability to repay test a lender will have to evaluate the borrower's income and assets (except for the equity in the home being financed) against the monthly payment due on the loan (PITI).*

Q: Will you no longer be able to sue higher qualifying ratios on lower LTV loans?

A: *We will not know what flexibility lenders will have in adjusting qualifying ratios according to LTV until regulations are issued. The CFPB will be in charge of those regulations and the law gives them broad latitude.*

Liability

Q: The Act mentions liability of up to actual damages or 3x compensation for violations. Does this mean LOs will be fined for violations or the company?

A: *The individual loan originator and the company are both liable.*

Q: Would this liability apply if it were determined that an LO received extra compensation base on "the terms of the loan" or for putting the borrower in a loan that they cannot afford?

A: *The penalty of 3x compensation is for a violation of the anti-steering (i.e. LO/broker compensation) rules. The penalty for violation of the ability to repay rule is 2x the finance charge paid by the consumer and it is assessed against the company.*

Q: The anti-steering section says the CFPB is to establish regulations which seem to establish a "fiduciary duty" in the LOs dealing with the borrower. Is this right?

A: *That is an overstatement. What the CFPB is directed to do is establish regulations that would prohibit or condition terms, acts or practices that are not in the best interests of the borrowers. A fiduciary duty requirement goes beyond that to state that you have an affirmative duty to act in the best interests of another person. So in the future, loan officers, brokers and lenders will be prohibited from steering, will be required to determine a borrower's ability to repay a loan and will be prohibited from any unfair or deceptive act or practice. But you still will be able to offer the borrower loan choices; i.e. between an ARM and an FRM, and permit the*

borrower to make the choice between the two, even if you believed one loan type was better for them than the other.

Q: Wouldn't this change dramatically the risk of being an LO or of employing LOs?

A: *There will be greater risk going forward in being an LO and employing LOs, but consumers will still need mortgages to buy homes and that business will be available to be done by those that master all these new rules and learn how to live within them and still be effective.*