

SUMMARY OF PROPOSED LOAN ORIGINATOR RULES

The Consumer Financial Protection Bureau (CFPB) invites the public to comment on proposed rules governing mortgage loan originations by October 16, 2012. Visit www.regulations.gov to submit your comments. These proposals clarify and expand on existing regulations governing loan originator compensation and qualifications. They also implement new laws, including a restriction on the payment of upfront discount points, origination points, and fees on most mortgage loan transactions.

Background

The mortgage market crisis focused attention on the roles that loan officers and mortgage brokers play in the loan origination process. Most consumers take out only a few home loans during their lives. As a result, they often rely on loan officers and brokers to guide them. But prior to the crisis, training and qualification standards for loan originators varied widely, and compensation structures frequently gave loan originators incentives to steer consumers into loans with higher rates or other unfavorable terms. Often, consumers paid loan originators an upfront fee without realizing that their creditors also were paying the loan originators commissions that increased with the interest rate or other terms.

The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) expanded on previous efforts by lawmakers and regulators to strengthen loan originator qualification requirements and regulate industry compensation practices. The Bureau is proposing new rules to implement the Dodd-Frank Act requirements, as well as to revise and clarify existing regulations and guidance on loan originator compensation.

The Bureau also is proposing rules to implement a new Dodd-Frank Act requirement that addresses broader consumer confusion about the relationship between certain upfront charges

and loan interest rates. For mortgage loans in which a mortgage brokerage firm or creditor pays a loan originator a transaction-specific commission, the Dodd-Frank Act bans the imposition on consumers of upfront discount points, origination points, or fees that are retained by the creditor, broker, or an affiliate of either. Although bona fide upfront payments to independent appraisers and other third parties would still be permitted, this change would require creditors in the vast majority of transactions in today's market to restructure their current pricing practices.

However, the Bureau is proposing to use its exemption authority under the Dodd-Frank Act to allow creditors to continue making available loans with upfront points and/or fees, as long as they also make available an alternative loan, as described below. The Bureau believes this approach would benefit consumers and industry alike. Making both options available could make it easier for consumers to evaluate different pricing options, while preserving their ability to make some upfront payments if they want to reduce their periodic payments over time. And the proposed approach would promote stability in the mortgage market, which otherwise would face radical restructuring of its existing pricing structures and practices to comply with the new Dodd-Frank Act requirement.

Summary of the Proposal

Restriction on Upfront Points and/or Fees

The proposed rule would generally require that, before a creditor or mortgage broker may impose upfront points and/or fees on a consumer in a closed-end mortgage transaction, the creditor must make available to the consumer a comparable, alternative loan with no upfront discount points, origination points, or fees that are retained by the creditor, broker, or an affiliate of either (a "zero-zero alternative"). The requirement would not be triggered by charges that are passed on to independent third parties that are not affiliated with the creditor or mortgage broker.

The requirement would not apply where the consumer is unlikely to qualify for the zero-zero alternative.

In transactions that do not involve a mortgage broker, the proposed rule would provide a safe harbor if, any time prior to application that the creditor provides a consumer an individualized quote for a loan that includes upfront points and/or fees, the creditor also provides a quote for a zero-zero alternative. In transactions that involve mortgage brokers, the proposed rule would provide a safe harbor under which creditors provide mortgage brokers with the pricing for all of their zero-zero alternatives. Mortgage brokers then would provide quotes to consumers for the zero-zero alternatives when presenting different loan options to consumers.

The Bureau is seeking comment on a number of related issues, including:

- whether the Bureau should adopt a “bona fide” requirement to ensure that consumers receive value in return for paying upfront points and/or fees, and different options for structuring such a requirement;
- whether additional adjustments to the proposal concerning the treatment of affiliate fees would make it easier for consumers to compare offers between two or more creditors;
- whether to take a different approach concerning situations in which a consumer does not qualify for the zero-zero alternative; and
- whether to require information about zero-zero alternatives to be provided not just in connection with informal quotes, but also in advertising and at the time that consumers are provided disclosures within three days after application.

Restrictions on Loan Originator Compensation

The proposal would adjust existing rules governing compensation to loan officers and mortgage brokers in connection with closed-end mortgage transactions to account for the Dodd-Frank Act and to provide greater clarity and flexibility. Specifically, the proposal would:

- Continue the general ban on paying or receiving commissions or other loan originator compensation based on the terms of the transaction (other than loan amount), with some refinements:
 - The proposal would allow reductions in loan originator compensation to cover unanticipated increases in closing costs from non-affiliated third parties under certain circumstances.
 - The proposal would clarify when a factor used as a basis for compensation is prohibited as a “proxy” for a transaction term.
- Clarify and revise restrictions on pooled compensation, profit-sharing, and bonus plans for loan originators, depending on the potential incentives to steer consumers to different transaction terms.
 - The proposal would permit employers to make contributions from general profits derived from mortgage activity to 401(k) plans, employee stock plans, and other “qualified plans” under tax and employment law.
 - The proposal would permit employers to pay bonuses or make contributions to non-qualified profit-sharing or retirement plans from general profits derived from mortgage activity if either: (1) the loan originator affected has originated five or fewer mortgage transactions during the last 12 months; or (2) the company’s mortgage business revenues are limited. The Bureau is proposing

two alternatives, 25 percent or 50 percent of total revenues, as the applicable test.

- Even though contributions and bonuses could be funded from general mortgage profits, the amounts of such contributions and bonuses could not be based on the terms of the transactions that the individual had originated.
- Continue the general ban on loan originators being compensated by both consumers and other parties, with some refinements:
 - The proposal would allow mortgage brokerage firms that are paid by the consumer to pay their individual brokers a commission on the transaction, so long as the commission is not based on the terms of the transaction.
 - The proposal would clarify that certain funds contributed toward closing costs by sellers, home builders, home-improvement contractors, or similar parties, when used to compensate a loan originator, are considered payments made directly to the loan originator by the consumer.

Loan Originator Qualification Requirements

The proposal would implement a Dodd-Frank Act provision requiring both individual loan originators and their employers to be “qualified” and to include their license or registration numbers on certain specified loan documents.

- Where a loan originator is not already required to be licensed under the Secure and Fair Enforcement for Mortgage Licensing Act (SAFE Act), the proposal would require his or her employer to ensure that the loan originator meets character, fitness, and criminal background check standards that are equivalent to SAFE Act requirements and receives training commensurate with the loan originator’s duties.

- Employers would be required to ensure that their loan originator employees are licensed or registered under the SAFE Act where applicable.
- Employers and the individual loan originators that are primarily responsible for a particular transaction would be required to list their license or registration numbers on certain key loan documents.

Other Provisions

The proposal would implement certain other Dodd-Frank Act requirements applicable to both closed-end and open-end mortgage credit:

- The proposal would ban general agreements requiring consumers to submit any disputes that may arise to mandatory arbitration rather than filing suit in court.
- The proposal would generally ban the financing of premiums for credit insurance.
- In its proposal, the Bureau describes rule text that may be included in the final rule to implement a Dodd-Frank Act requirement that the Bureau require depository institutions to establish and maintain procedures to assure and monitor compliance with many of the requirements described above and the registration procedures established under the SAFE Act.

Implementation

The CFPB plans to issue final rules by January 2013 to meet Dodd-Frank Act requirements. The Bureau is requesting comment on how long to provide for implementation.