From: Peter Ogilvie <firstrez@calcentral.com> on 04/10/2008 04:06:35 AM

Subject: Regulation Z

I realize I am a day and a half late with this. We were given the incorrect email address to which to send our comment and I just discovered the error a few minutes ago.

Am forwarding the letter I sent originally yesterday afternoon just because I want to give the Board the opportunity to hear from California and our association. We all used the same bad address, I'm afraid.

A thousand pardons.

Peter Ogilvie
President
California Association of Mortgage Brokers

Begin forwarded message:

> **From:** Peter Ogilvie <firstrez@calcentral.com>
> **Date:** April 8, 2008 1:37:05 PM PDT
> **To:** regs.comments@federalreserve.gov
> **Subject: Docket No. R-1305, Comment on Reg Z Revisions**
>
> The text below, on California Association of Mortgage Brokers letterhead sent to you a few minutes ago, to be included in public comment on the proposed Reg Z revisions brought forth by the Board of Governors of the Federal Reserve Board.
>
> Sending this in the body of an email text may make it easier to transfer to whatever media is most useful for the Board's purposes.
>
> Thank you,
>
> *Peter Ogilvie* , CMC
> President,
> California Association of Mortgage Brokers
>
> First Residential Mortgage Corporation
> 1414 Soquel Ave., Suite 212
> Santa Cruz, CA 95062-2133
> (831) 459-6073 Voice
> (831) 459-6078 Fax
>
> *
>
> Date: April 7, 2008
>
> To: Board of Governors, Federal Reserve System
>
> From: Peter Ogilvie, President, California Association of Mortgage Brokers
>
> Re: Docket No. R-1305, Proposed Revision to Regulation Z, Truth in Lending.
>
> On behalf of the members of the California Association of Mortgage Brokers, I would like to commend you on your efforts to address some of the problems that have arisen in the mortgage industry over the past several years.
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> Our association of more than 4,000 licensed mortgage brokers, affiliates and support staff is dedicated to the highest standards of professional and ethical conduct and committed to consumer protection and the preservation of maximum reasonable access to the American dream of home-ownership. We are proud of our long-standing and well-established record of combatting predatory lending practices in all their forms.
>
> We were the first to define "predatory lending," in an effort to combat it, as originator compensation taken without

regard to the costs or consequences to consumers. Our “Ten Tips to Avoid Predatory Lending” was issued and reissued in press releases in our attempts to alert consumers to the dangerous schemes employed by unscrupulous loan originators and how to evade their traps.

Yet, during the excesses of the mortgage market of the past few years, we found ourselves unable to combat the invasion of shady operators whose business model was marked by rapacious greed and rampant fraud who were overwhelming the industry to which we had dedicated our careers, the industry that had helped tens of millions of families achieve the goal of home-ownership. While the collapse of the market those excesses brought about has sent most of the quick-buck hustlers packing, still, structural inefficiencies and potentials for abuse remain. We welcome, therefore, the Board of Governors’ efforts and applaud many of the provisions of the new, revised Regulation Z.

There is much good to say about the proposed revision. Time, however, demands that we forgo the pleasure of addressing what is right and turn our attention to those provisions we find so glaringly wrong.

There are two general areas of disagreement we have with the proposals. Some of the provisions would have direct, negative impact on the broker mortgage delivery channel and our ability to make a living serving the needs of our clients. Other provisions would restrict consumer access to credit, depriving countless deserving home buyers and home owners of reasonable financing at affordable cost.

Since we brokers believe we offer significant value to borrowers by bringing a wide variety of loan products from dozens of lenders to our communities which would — without us — be served by a handful of direct lenders at most, the interests of mortgage brokers and consumers are often closely aligned. Nevertheless, for the sake of brevity, we will address each aspect as though it was a consumer argument or a broker argument.

Higher-Priced Loan Triggers in the Rule are Set Too Low

The higher loan cost triggers are too low and will, from time to time, pull in significant portions of the Alt-A and prime market unless they are raised to 4.0 % and 6.0%. Thresholds of 3.0% and 5.0%, based on the annual percentage rate (APR), would have the immediate unintended consequence of putting many non-conforming, prime jumbo loans, currently in process, into higher priced status.

Rates on prime, jumbo 30-year fixed loans are running up to 1.5% higher than conforming loans. Jumbo loans with an equity position of less than 20% of the property value require private mortgage insurance, the cost of which is included in calculation of the APR, as would points borrowers might choose to pay to bring down their note rate. With the coupon rate for 30-year Treasuries presently at 4.375%, the APR on such loans could easily exceed the 7.375% higher-priced threshold the Rule proposes. The same thing holds true for jumbo adjustable rate mortgages (ARMs) today.

While much of the impact of the Rule falls on the originating entity, there would be serious consequences for consumers if thresholds, as proposed, were implemented. If, as above, jumbo borrowers, many of whom are self-employed professionals who depend on stated income underwriting to qualify for financing, become subject to the strictures of higher-priced loans, a substantial segment of the population would be effectively locked out of the mortgage market pending a change on overall economic conditions.

Our deeper concern is that recent history has shown that there is another kind of threshold operating in the mortgage industry and, perhaps, in other industries as well: a regulatory limit beyond which enterprise will abandon markets rather than deal with the onerous burden of compliance and the risks of failure to meet ill-defined standards. This is the danger inherent in setting triggers too low, or, as in the discussion of stated income underwriting below, of leaving too much to interpretation.

Reasonable Stated Income Qualifying Must be Allowed for Subprime Borrowers

The Rule does not bar stated income or low-documentation underwriting in higher-priced loans outright; it merely prohibits a “pattern or practice” of making consumer loans without consideration of borrowers’ ability to pay back the loan, that is, without verifying income and assets other than the collateral.

First, we respectfully offer that the “pattern or practice” standard is sufficiently vague, and the penalties for non-compliance severe enough to discourage all but the most intrepid entrepreneur from offering stated income or no/low-documention loans. While the Board’s stated intent is to allow such loans, this provision amounts to a tacit prohibition of them.

Second, we would point out that many families for whom subprime, higher-priced, mortgages are the only financing available, are the borrowers who need alternative qualifying methods the most.

While stated-income and other low-documentation loans have been used inappropriately in large numbers over the past few years, that does not negate the fact that these loans were created to address real needs of worthy borrowers whose income-producing efforts do not produce the documentation standard underwriting criteria demands. Modern high-volume, electronic underwriting, increasingly prevalent in the industry, has narrowed the gate through which borrowers must pass, even as consumers respond to a constricting economy by depending more and more on off-the-books, outside-guidelines means of supporting themselves and paying their obligations.

Legitimate sources of support such as contributions of occupant relatives to household income, common in many communities, may not be included in qualifying income, even though these contributions are routinely used to make mortgage payments. Income from second jobs are not included unless the second job has been held for a minimum of two years. Similarly, self-employment income cannot be counted unless the self-employed borrower has been independent for at least two years even though he or she has long experience in the same field as an employee.

Examples of means of earning income which do not fit into the strait gate of standard underwriting are countless; stated income and low-documentation loans are the only means available today for borrowers who depend on these alternative strategies to support themselves and their families. To the degree that availability of stated income and low-documentation loans is decreased, deserving borrowers who are fully capable of meeting their obligations will be barred from the dream of homeownership, or from refinancing their homes to achieve their other sound financial goals.

Ability to pay may be measured by other means than income documentation such as a record of having timely paid important obligations under borrowers' current income-producing strategy. Lack of available income documentation may be offset by the fact that borrowers' overall obligations are decreasing through new financing, and/or that borrower's equity position is strong enough to provide assurance of lowered risk to the borrower and the investor. These and other prudent alternatives to income and asset documentation must be permitted in the revision of Regulation Z when put in force.

The Federal Reserve's own Guidance of December, 2005, may provide apt language for allowing stated income and reduced documentation loans in cases where mitigating factors clearly minimize the need for full documention of income, and we would encourage the Board to incorporate such reasoning into the revised Rule.

Mandatory Escrows for Subprime Borrowers will Lock Out Some

Requiring property tax and insurance escrows for borrowers is not projected to have a significant effect on broker practice or the brokerage mortgage delivery channel. It will ensure that borrowers tax payments and insurance premiums are kept up and that these expenses will be anticipated by consumers applying for home financing. Permitting borrowers to opt out of escrows after one year is a reasonable provision that gives consumers the right to pay these costs as they wish once they have shown they can afford to do so.

The Board should be aware, however, that, certain borrowers will find it difficult-to-impossible to obtain a mortgage due to the additional financial hurdle of adequately funding the escrow account at closing.

Escrow or impound accounts for hazard insurance routinely require a minimum of 14 months' premiums paid in advance. Depending on the time of year a home purchase is to close, borrowers may have to bring up to eight months' property tax to the closing table. In some areas, for a median-priced home, funding the escrow account could mean an additional cost of $4,000 to $6,000, or more, to home buyers.

Disclosure Requirements Must be Equivalent Across All Mortgage Origination Channels

The Federal Reserve Board of Governors has singled out one mortgage distribution channel for special treatment, setting a much higher performance bar for some originators — mortgage brokers — while letting other originators in other channels carry on very similar practices as the ones it objects to in regards brokers, without rebuke, control, or increased disclosure. This is unacceptable. It is an arbitrary and capricious exercise of the power given the Federal Reserve to regulate the mortgage industry that will, if carried forward, cripple a viable source of mortgage financing, one that has, as stated earlier, helped millions of Americans realize the dream of homeownership.

The Rule will require early disclosure of broker compensation, in dollar amounts, which may not change through the course of mortgage processing to funding. No such requirement, or a reasonable equivalent thereof, taking into account the differences between the practices of each channel, is mandated for lenders.

The Board supports this disparate treatment of loan originator types by bringing forth a study involving 1,008 borrowers, conducted in 2001 by AARP, in which borrowers who had utilized the services of brokers to obtain financing, and borrowers who had gone to lenders, were asked if they had relied on the originator with whom they had contact, and how much. According to this study, 70% of the borrowers who had gone to brokers, and 52% of the borrowers who had gone to lenders, relied on the broker or lender "a lot," to use AARP's expression.

Based on this difference of 18%, the Board apparently has decided that consumers need extra disclosure from brokers, while the 52% that relied on lenders need no additional protection: lenders must meet the requirements of the Truth In Lending Act and furnish their borrowers a Good Faith Estimate, but are not required to disclose their compensation and there is no restriction on changes in the amount of fees or compensation to be imposed at closing. This is inequitable and represents a danger to consumers who may — as did those 52% — rely on their lender to provide the best loan for their circumstances, when, in fact, the lender and the originating employee acting for the lender are under no such obligation; the originator's sole responsibility is to sell the mortgage products offered by the lender, to whom they owe a certain level of loyalty, which they do not owe to their customers.

The Board is further requiring brokers to furnish a disclosure which states that they may be influenced by lender payments to provide a loan with less favorable terms than would be arranged if the lender was not paying the broker -–– whether or not that broker is bound by case law or statute to avoid all such incentives and put the benefit of the borrower uppermost in the transaction as is required of all licensed mortgage brokers in our State of California. No such disclosure is mandated for lenders. Again, such disparate treatment is unacceptable.

Should lenders be required to furnish a disclosure to the effect that they will only offer the lender's products to their customers? That, if the kind of loan best suited to the borrower's circumstances is not offered, the customer will have to go elsewhere for a loan? That the loan officer or mortgage loan salesperson dealing with the customer may receive extra compensation — a bonus — for selling a loan with a higher interest rate than that for which the borrower qualifies?

The fact that more than 50% of the borrowers who went to lenders in AARP's study were relying "a lot" on the lender to give them a loan that best suited their plans, goals, and qualifications, would seen to indicate that such a disclosure is necessary. If the proposed broker disclosure, casting aspersion on the characters of professionals in one channel is to be mandated, there must of necessity be an equivalent disclosure for originators in the other mortgage distribution channels.

The revised Rule requires that broker (and no others) disclose all compensation to be received for arranging a loan in a firm dollar amount which may not change through closing. The California Association of Mortgage Brokers supports early disclosure of compensation, but demands that, as above, the same standard be applied to all originators and all mortgage delivery channels.

We do, however, respectfully object to brokers alone being required disclose compensation in dollar terms, in complete divergence from industry-wide practice for decades. This change is purported to make the transaction easier to understand and more transparent to borrowers, yet millions upon millions of consumers have successfully gone comparison shopping for loans on the basis of certain "points" (percentages of the requested loan amount), plus fees.

Points-plus-fees has marked borrower shopping across all mortgage channels whether the originating entity was a bank, a credit union, a thrift, a finance company, a mortgage bank, or a brokerage. Wholesale lenders from time immemorial have offered their products to brokers in points-plus-fees terms.

We fail to see the justification for imposing such a change on our industry at this time and we find it capricious and unacceptable. Requiring brokers to declare their compensation in concrete, in dollar amounts, would not permit that compensation to change regardless of substantial increases in the loan amount being borrowed, placing constraints on brokers not required of other originators.

"Steering," or incentivizing originators in any channel to put borrowers in loans with worse terms than those for which they qualify in order to increase compensation to the originator is the very definition of predatory lending practices, is a scourge of the mortgage industry and anathema to CAMB members and decent, ethical mortgage originators of whatever stripe.

The way to stop that execrable practice is to separate compensation from the terms of the loan for which a borrower qualifies, which may allow borrowers to choose a higher-than-par rate in exchange for financing through the rate, some or all of closing costs, which may include the originators' compensation.

We are prepared to support early disclosure of originator compensation in terms of points-plus-fees, with the acknowledgement that the disclosed compensation may be paid in whole or in part by the lender or whole or in part by the borrower, depending on that borrower's selection of terms and closing cost financing. The points — percentage of the loan amount — or the disclosed fees — in dollar amounts — may not change throughout the transaction and must be the same at closing as were originally disclosed. We do, however, respectfully demand that an equivalent disclosure be required of all mortgage originators regardless of mortgage delivery channel.

In closing the California Association of Mortgage Brokers wishes to express our appreciation to the Board of Governors of the Federal Reserve for giving us this opportunity to comment on the proposed rule.

Sincerely,

Peter Ogilvie, CMC
President,
California Association of Mortgage Brokers

(831) 459-6073 Voice
(831) 459-6078 Fax