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REGULATORY BURDENS TO OBTAINING MORTGAGE CREDIT

HEARING

BEFORE THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

ONE HUNDRED FOURTEENTH CONGRESS

FIRST SESSION

ON

EXPLORING REGULATORY BURDENS THAT ARE RESTRICTING MORTGAGE CREDIT, INCLUDING RECOMMENDATIONS TO ALLEVIATE THE BURDEN

APRIL 16, 2015

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REGULATORY BURDENS TO OBTAINING MORTGAGE CREDIT

THURSDAY, APRIL 16, 2015

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The Committee met at 10:01 a.m., in room SD–538, Dirksen Senate Office Building, Hon. Richard Shelby, Chairman of the Committee, presiding.

OPENING STATEMENT OF CHAIRMAN RICHARD C. SHELBY

Chairman SHELBY. The hearing will come to order.

Months ago, this Committee began an examination of the regulatory landscape facing consumers, lenders, and other financial market participants. Our goal has been to identify existing laws and regulations that create unnecessary barriers to economic growth. Some of these may also inadvertently restrict the availability of consumer credit or increase its cost.

Today, we turn our attention to mortgages. Our witnesses are involved in each stage of the home buying process, from the construction of the home to its selection in financing. We have asked them to discuss the state of housing markets across the country, including which lending laws and regulations are working and which can be improved.

Five years after a sweeping new regulatory framework altered the mortgage market in unprecedented ways, I believe it is time to reexamine its effectiveness and its consequences. Dodd-Frank's stated intent is to protect consumers, but some of the regulations promulgated in response to the law have gone so far, they may actually prevent qualified consumers from owning a home. And, borrowers who are able to qualify for mortgages today may face an increased cost of credit due to these rules.

I would hope that we can agree that laws and regulations that reduce mortgage availability or increase the cost of credit for those who do qualify are harming, not helping, consumers. While record low mortgage rates in recent years may have balanced out an increased cost of mortgage credit due to new regulatory requirements, this trend will not continue indefinitely. When interest rates rise, I believe that the impact of these new rules and regulations on home ownership will then be clear.

Today, we will consider ways to refine current law so that it protects consumers while encouraging responsible home ownership. This should be an achievable bipartisan goal, because Members of

this Committee on both sides of the aisle have introduced and supported legislation in this area.

I encourage others to consider ways in which we can work together to make the new regulatory framework true to its legislative intent of protecting consumers while increasing responsible access to credit. This goal can be accomplished without returning to the pre-crisis standards of lax underwriting and access to mortgage loans for those who cannot afford to repay them.

In other words, any changes to the law should not erode consumer protection or encourage irresponsible lending practices. They should address the issue of creditworthy customers being denied loans or charged more for them because of existing laws and regulations. If done properly, such changes could make our financial system safer by allowing regulators to direct their limited resources toward more efficient regulation and ensuring better management of risk.

I look forward to hearing from our witnesses and hope that their perspectives will help this Committee identify specific issues that consumers face every day in purchasing homes and qualifying for credit.

Senator Brown.

STATEMENT OF SENATOR SHERROD BROWN

Senator BROWN. Thank you, Mr. Chairman. Thanks to the witnesses, the four of you, for joining us today.

We know the mortgage market is vast, it is complex, and it is interconnected. Its impact extends from the finances of individual families in Alabama and Ohio to the stability of the global financial system.

Go back to 2008 and the years before. Predatory, irresponsible lenders made dangerous subprime loans and often ignored a borrower's ability to repay. When the real estate bubble burst less than a decade ago, families had their wealth and their equity stripped from their homes, starting a chain of events that resulted in the financial crisis and subsequent economic devastation of the Great Recession.

Dodd-Frank provided a common sense fix to the bad practices in mortgage lending that had been staring us in the face for years. Now, 5 years later, some are suggesting that we weaken some of these standards and we head back to there, where we started.

In 2008, our country learned a painful lesson, that not all mortgage lending is created equal. Unscrupulous lenders offered loans that required no documentation, loans with teaser interest rates that later spiked and undermined a borrower's ability to repay, and loans where borrowers never paid down their principal. These practices had devastating results for families, for communities, for our economy. Borrowers with these higher-cost loans were foreclosed on at almost triple the rate of borrowers with conforming 30-year fixed-rate mortgages. Again, almost triple the rate of borrowers with conforming 30-year fixed-rate mortgages.

The crisis revealed a host of other harmful practices: Steering borrowers to affiliated companies, kickbacks for business referrals, inflated appraisals, loan officer compensation based on the loan product. These practices offered little benefit to the borrower. Even

more troubling, as borrowers' cost increased, so did loan officers' compensation. Members of the organizations testifying before us today felt the impact of these practices firsthand.

After the housing crash revealed the extent of the deterioration in mortgage lending standards, Congress stepped in to do what the market and regulators had refused to do. Dodd-Frank established a common sense rule that requires mortgage lenders to ensure that borrowers have the ability to repay their loans. This means that lenders can no longer make a loan based on the home's value instead of the borrower's ability to pay back the loan.

It should be noted that many lenders did not follow this basic principle during the housing boom. At its peak, 27 percent of loans in this country that were made were subprime products.

At the risk of making matters even more complicated, we may be in danger of overlooking other factors that have tightened credit beyond what Dodd-Frank envisioned. In reaction to the housing crisis and their own financial positions, the GSEs and FHA each tightened lending standards and increased fees that are charged to borrowers. They announced small steps in the FHA's HAWK program, the GSEs' return to 3 percent downpayments to expand credit just this winter, but their loan profiles continue to represent higher FICA scores and downpayments than historical levels.

Lender overlays, higher eligibility criteria than the GSEs or FHA, have also made mortgage credit difficult to obtain. While the Ability to Repay standard was intended to be the base standard, we heard in earlier hearings that lenders only want to make QM loans because they provide liability protection, an additional lender overlay. However, if we expand QM eligibility in order to protect lenders, we also limit the protections for a family buying a home.

A mortgage is the largest financial transaction most people will make in their lifetime. As we have learned across a number of consumer financial products and services, ensuring that the mortgage process, servicers, and fees are transparent and understandable to borrowers is essential if they are to be successful home buyers and homeowners.

Reviewing regulation for their impact on the market and possible duplication is important. But, if we do not address the other challenges that restrict credit, eliminating important home buyer protections under the cloak of access turns the clock back to a dangerous 2008.

I look forward to having a conversation about all of the challenges today, all of the challenges that the housing market faces and the possible solutions. There is not a single answer to fix these complicated problems. But, we cannot return to the days—we cannot return to the days when unscrupulous lenders could make loans that undermined a borrower's ability to repay while charging excessive fees and, thus, putting our entire economy at risk again.

Thank you, Mr. Chairman.

Chairman SHELBY. Thank you, Senator Brown.

Without objection, I would like to enter at this time into the record statements from the Conference of State Bank Supervisors, the Housing Policy Council, Independent Community Bankers of America, National Association of Federal Credit Unions, the Credit Union National Association, Manufactured Housing Institute, the

Community Mortgage Lenders of America, American Land Title Association, the National Association of Mortgage Brokers, and Habitat for Humanity.

Chairman SHELBY. Today, first, we will hear the testimony of Mr. Tom Woods, Chairman of the National Association of Home Builders. Mr. Woods is currently President of Woods Custom Homes.

Senator Cotton, you are with us today and you have a friend. Would you like to introduce him?

STATEMENT OF SENATOR TOM COTTON

Senator COTTON. Yes. Thank you, Senator Shelby.

Today, we have Chris Polychron, the President of the National Association of REALTORS®. Chris is a REALTOR® in Hot Springs. He has been in Hot Springs for 27 years as a leading REALTOR® there, and while we all know him here in this room as President of the National Association, he has also been a leading REALTOR® throughout Arkansas, serving on the Board of Directors for the Arkansas Realtors Association, President of the Arkansas Realtors Association, and President of the Hot Springs Realtors Association. Also, he has been a leader in the Hot Springs community and the local Chamber of Commerce, been President of his local church for almost 20 years, and Chris and I have known each other for almost 4 years, since our good friend, Smokey Campbell, introduced us.

Chris, it is great to see you here in Washington, DC, although I know we both look forward to seeing each other in Hot Springs sometime soon.

Chairman SHELBY. Thank you, Senator Cotton.

Then, we will hear from Mr. J. David Motley, President of Colonial Savings, who is here on behalf of the Mortgage Bankers Association.

And, finally, we will hear from Ms. Julia Gordon, Senior Director of Housing and Consumer Finance at the Center for American Progress.

Your written testimony, all of it, will be made part of the record. We are going to start voting in the Senate around 11, so you proceed as fast as you can with your statements.

We will start with you, Mr. Woods.

STATEMENT OF TOM WOODS, PRESIDENT, WOODS CUSTOM HOMES, ON BEHALF OF THE NATIONAL ASSOCIATION OF HOME BUILDERS

Mr. WOODS. Thank you. The Nation's economic growth depends on an efficient housing finance system to provide adequate and reliable credit to home buyers and home builders, at reasonable rates, and in all business conditions. Home buyers and builders continue to confront challenging credit conditions triggered by a zealous regulatory response to the Great Recession.

In response to the crisis, Dodd-Frank mandated significant mortgage finance reforms and created the CFPB to implement and supervise many of the new requirements. FHFA, the Federal banking agencies, and FHA all have taken steps to ensure that the Nation will never again be at the vulnerability to risky mortgage lending.

The collective regulatory actions, along with the increased compliance costs, has severely restricted the availability of mortgage credit to many creditworthy borrowers. NAHB is concerned about the effect of regulatory constraints on originating loans, particularly for small communities, first-time home buyers, and other underserved market segments.

Smaller banks and independent mortgage bankers are leaving the residential mortgage business or merging their banks as the burden of compliance has made it harder and more expensive to do business. This exodus will reduce competition and limit consumer choice. Congress must act now to eliminate some of the barriers to credit availability and support a stronger, more robust recovery of the housing and mortgage markets.

As the mortgage industry deals with the ongoing issues associated with the implementation of the CFPB's Ability to Repay standard, we urge Congress to pass the Mortgage Choice Act. This common sense legislation would clarify the qualifying mortgage rules' definition of points and fees and ensure that consumers can choose the lender and title provider best suited to their needs.

We also urge Congress to pass the Portfolio Lending and Mortgage Access Act. This legislation is intended to ease the ability to repay requirements for community lenders who may fear regulatory and legal consequences of originating a non-QM loan and, therefore, may limit access to credit for some home buyers.

NAHB believes the Federal agencies can and should take actions to alleviate burdensome regulatory requirements to consumer access to mortgage credit. One issue that NAHB is watching closely is the implementation of the CFPB's new mortgage disclosure forms. The new forms are intended to help consumers make informed decisions and avoid costly surprises. NAHB is concerned that any confusion related to the new rules, compounded by the fear of aggressive enforcement actions, will negatively impact a buyer's ability to close on a house in a timely manner.

In addition, lender overlays in the mortgage credit process have been a major factor in the difficulty that home buyers are having to obtain financing. Lenders are currently imposing credit understanding standards that are more restrictive than FHA, VA, and the housing GSEs require. NAHB encourages further efforts to increase certainty for mortgage lenders on the criteria for acceptable mortgage underwriting.

Likewise, fees for Government-backed mortgages continue to be too high, given that the credit quality of the underlying loans has increased.

NAHB urges action on two additional fronts that specifically impact the homebuilding industry, appraisals on new home construction and access to housing production credit. Improper appraisal practices, a shortage of experienced appraisers, and inadequate oversight of the appraisal system continues to restrict the flow of mortgage credit and impede the housing recovery. Despite signs of improvement in recent months, many homebuilders continue to deal with a significant adverse shift in terms and availability of loans for ground acquisition, land development, and home construction. Lenders are reluctant to extend new AD&C credit, citing reg-

ulatory requirements or examiner pressure on banks to shrink their AD&C portfolios.

Finally, while regulatory barriers can be alleviated by the various regulators as well as by legislative reform, NAHB continues to support comprehensive housing finance reform. Comprehensive legislation would ensure that components of reform are not at cross-purposes.

Thank you for your opportunity today.

Chairman SHELBY. Chris, go ahead.

STATEMENT OF CHRIS POLYCHRON, 2015 PRESIDENT, NATIONAL ASSOCIATION OF REALTORS®

Mr. POLYCHRON. Yes, sir. Chairman Shelby, Ranking Member Brown, and Members of the Committee, thank you for the opportunity to testify. My name is Chris Polychron. I am the 2015 President of the National Association of REALTORS®, as Senator Cotton said, from Hot Springs National Park, Arkansas. I am speaking to you today, however, on behalf of over one million members of NAR.

In communities across the United States, REALTORS® help citizens from every walk of life achieve the dream of home ownership. However, millions of home buyers are still on the outside looking in. The Nation's home ownership rate has fallen close to levels last seen in 1990, and the number of first-time home buyers entering the market is at its lowest point since 1987, despite historically low mortgage rates.

Since 2008, we have seen good intentioned but over-corrected policies severely hamper the ability of millions of qualified buyers to purchase a home. We have yet to strike the right balance between regulation and opportunity. We see the need for reform in four areas, and I will briefly discuss each now.

The first area relates to Consumer Financial Protection Bureau. The 3 percent cap on points and fees needs to be fixed. This cap leads to reduced choices for consumers and prevents lenders from making qualified, or QM, loans. We also believe that underwriting standards should not be so restrictive that they prevent smaller community banks from lending to their customers.

The second area is specialty markets. Twenty percent of the home buyers live in rural areas or small towns. We strongly urge Congress to provide the Rural Housing Service with direct endorsement authority to accelerate loan processing for borrowers, and manufactured housing should be encouraged as an affordable housing opportunity. And, Senator Cotton and others here, thank you for S. 682.

The third area is short sales and foreclosures. Streamlining the short sale process will reduce the time it takes to sell a property and reduce the number of foreclosures. We also urge Congress to extend the income tax exemption on mortgage debt forgiveness. On both counts, we would be protecting our communities from foreclosures, which ultimately result in seeing a lot of homes that are boarded up.

And, the fourth area is lending policies. Condos are often the most affordable option for first-time home buyers, including minority and the elderly. However, both the Federal Housing Adminis-

tration and the Government-Sponsored Enterprises need to address overly restrictive policies. In addition, high guaranteed fees, or G-fees, are dragging down the first-time home buyers. Prices should basically be in line with risk.

In closing, let me leave you with this. The Urban Institute recently estimated that we prevented home loans to four million qualified buyers between 2009 and 2013. This would not have happened had we had credit standards similar to the ones we had in 2001, long before the housing bubble. Instead, four million families missed out on buying a home because we are taking protection to an unnecessary extreme. Mr. Chairman, that is the equivalent of 80 percent of the population of your home State of Alabama.

No one wants to see the return to the unscrupulous predatory lending practices that caused the Great Recession. But, what we can do is balance the common sense regulations with increasing access to credit.

Thank you for your time. I look forward to answering questions later.

Chairman SHELBY. Thank you, sir.

Mr. Motley.

STATEMENT OF J. DAVID MOTLEY, PRESIDENT OF BANKING AND MORTGAGE OPERATIONS, COLONIAL SAVINGS, F.A., ON BEHALF OF THE MORTGAGE BANKERS ASSOCIATION

Mr. MOTLEY. Thank you, sir. Chairman Shelby, Ranking Member Brown, and Members of the Committee, I appreciate the opportunity to testify today. I am currently President of Colonial Savings, a community bank headquartered in Fort Worth, Texas. I am a past member of MBA's Board of Directors and I currently serve on the Community Bank Advisory Council for the Consumer Financial Protection Bureau.

As a four-decade veteran of the mortgage banking industry, I can tell you from experience that recently enacted laws have created commendable consumer protections and have made the market safer. However, new regulatory demands imposed under these laws have negatively affected the availability and the affordability of safe, sustainable mortgage credit. Qualified borrowers, including many first-time potential home buyers, continue to have difficulty accessing credit.

MBA has consistently supported reasonable requirements to prevent the repetition of past excesses. However, MBA's data show that mortgage credit availability remains far below the levels seen in normal times prior to the mortgage crisis, and much of this constraint can be attributed to new regulatory demands on mortgage lenders.

Although the CFPB did good work in developing the Ability to Repay rule and the qualified mortgage definition, MBA believes it is time to consider changes to the QM definition. This will mitigate the adverse impact that initial rule has had on access to credit for some qualified borrowers. Additional adjustments to the rule can expand access to sustainable mortgage credit and ensure that lenders can fully utilize all four corners of the QM credit box.

MBA believes that changes to the QM should be made holistically and not based solely on charter type or business model. Ex-

panded product choices under the QM should not be limited to certain providers, and the burden should not be on the consumer to determine which institutions offer particular types of loans. This will only cause unnecessary consumer confusion and reduce competition.

To this end, we support several changes to the QM definition, including expanding the safe harbor, increasing the small loan definition, replacing the current patch for Government-backed loans, and expanding the QM to include certain loans held in portfolio.

With regard to a portfolio exemption, we believe that any such expansion should apply both to banks and to nonbank lenders who originate loans for sale to banks or private institutions that plan to hold them in portfolio. However, in order to protect against the reemergence of loans with particularly risky features, such as pay option ARMs, or stated income loans, or NINJA loans, we believe some of the parameters of the standard QM definition should be retained for portfolio QM loans.

We also strongly support legislation that would exclude title insurance fees paid to lender affiliate companies from the calculation of points and fees under QM.

Beyond these changes to QM, there are several other areas that could be addressed to facilitate increased access to credit for qualified borrowers. First, we strongly believe that the CFPB should offer authoritative written guidance to accompany its rules. The absence of timely written guidance from the CFPB has resulted in confusion and slowed the implementation process of several important regulations. This is particularly important in light of the forthcoming TILA–RESPA integrated disclosure rule that will take effect in August.

Second, the cost to service mortgage loans has increased dramatically. This is due to new CFPB rules as well as the punishing treatment of mortgage servicing rights under the Basel III framework. Under that rule, banks are required to hold extraordinary amounts of capital to support the MSR asset, making it less likely for banks like mine to retain mortgage servicing. These increased costs directly impact consumer access to credit and make new mortgage production less attractive to lenders. To address this situation, MBA supports Congressional efforts to mandate a study into the effect of Basel III on mortgage servicing rights.

Third, MBA believes that FHFA should direct the GSEs to adopt the latest validated credit scoring models on an expedited basis. The newer models help score borrowers with limited credit experience, including first-time home buyers. Using updated models, lenders will be able to extend loans to a greater number of qualified borrowers.

Finally, in addition to addressing many of the regulatory hurdles currently facing the mortgage market, MBA believes that Congress should continue its work from last year to address comprehensive housing reform.

Again, I am grateful for the opportunity to testify before you today. MBA commends your efforts to examine the regulatory hurdles preventing qualified consumers from accessing credit and we are eager to work with the Committee to improve the availability

of sound mortgage credit for American consumers. I will take your questions whenever you are ready.

Chairman SHELBY. Thank you.

Ms. Gordon.

STATEMENT OF JULIA GORDON, SENIOR DIRECTOR OF HOUSING AND CONSUMER FINANCE, CENTER FOR AMERICAN PROGRESS

Ms. GORDON. Good morning, Chairman Shelby, Ranking Member Brown, and Members of the Committee. I direct the Housing and Consumer Finance Team at the Center for American Progress, a nonpartisan think tank dedicated to improving the lives of Americans through progressive ideas and action.

The other witnesses have ably sketched a picture of today's mortgage market, so I thought I would spend a moment revisiting yesterday's, when toxic, risk-layered mortgage products proliferated. These were aggressively pushed on consumers who could have qualified for more stable and affordable products and perversely incentivized brokers and lenders to strip home equity through excessive and deceptive fees.

In the capital markets, investors poured money into the private label securitization machine in search of yield, while financial innovations aimed at managing risk actually spread that risk to every corner of the system.

When the bubble burst, millions of Americans lost their homes, many unnecessarily due to a thoroughly broken mortgage servicing system. And, tens of millions more lost jobs, retirement savings, and, maybe worst of all, trust in the financial system.

In the wake of the crisis, Congress and the American public supported comprehensive financial reform legislation to realign incentives and strengthen oversight. Yet, now, less than a decade later, the mortgage industry tells us if only Congress will roll back some of these crucial reforms, they will lend more.

Yet, more lending without the core Dodd-Frank protections in place is exactly the wrong medicine for today's ailing market. If these important guard rails are improved, the likelihood of seeing a return to predatory and unsustainable lending is high and any gains in home ownership would be temporary and possibly dangerous. There will be no true recovery until public confidence is restored, and a Congressional about-face on reform will set that effort back years.

Now, make no mistake. The CLEAR Relief Act, for example, is no simple tweak to adjust a lending standard. It is an evisceration of Dodd-Frank's core principle, which says that a lender should not make a loan unless it has reasonably determined that the borrower can afford to pay the entire loan back.

Note that the qualified mortgage definition, or QM definition, that this legislation seeks to extend is not actually an underwriting standard like Ability to Repay is. It is a liability standard. It designates a category of mortgages so inherently super-safe that lenders need not fear any legal accountability if the loan goes bad. It excludes riskier products, such as negatively amortizing or balloon mortgages. It requires underwriting to the maximum possible payment in the first 5 years of an adjustable-rate loan. It limits exces-

sive points and fees. And, it excludes borrowers whose total debt-to-income ratios exceed a certain threshold.

The legislation would confer this same absolute legal immunity on loans with virtually any terms and features as long as they are held in portfolio for 3 years by a bank with less than $10 billion in assets. And, just note, that definition covers all but the largest 110 depository institutions in America and well over half of all mortgage loan originations.

Proponents of this bill argue that because loans are held in portfolio, lenders have an incentive to ensure a borrower will succeed, and in the case of small community banks, that has often been true, which is why those banks have a whole list of significant exemptions from Dodd-Frank that I have detailed in my written testimony.

But, larger institutions have a much more checkered past and far less of an ability to ensure quality underwriting from all their originators. You will recall that Washington Mutual was a portfolio lender and its collapse was due entirely to loans that could not have met current QM status.

What is more, by only requiring 3 years in portfolio, this product could entice—this could entice lenders to create loans whose price or other features dramatically increase after the 3-year deadline, just like the ones that brought down the system before.

Some of these other roll-back efforts are equally misguided and I discuss them further in my written testimony.

Instead of gutting Dodd-Frank, let us get to work together on finding more effective and less dangerous ways to increase access to safe, high-quality mortgage credit. Congress should complete comprehensive housing finance reform, extend the Mortgage Forgiveness Debt Relief Act, convert the mortgage interest deduction to a credit, and allow agencies to support housing counseling. FHFA and FHA should continue to provide better demarcation of responsibility, fix the broken servicer compensation system, and pilot more effective ways to reach underserved markets.

As memories of the crisis fade, let us not open the doors to a new round of predatory unsustainable lending. Instead, let us work together to create a healthier and more equitable housing market that drives economic growth and promotes opportunity for America's families.

Thank you.

Chairman SHELBY. I thank all of you. Thank you, Ms. Gordon.

I am going to ask each of you to briefly respond to this question. What are the two top—two or three, I should say—two or three regulatory barriers that you have identified as constricting mortgage credit and how should they be fixed, just briefly? We will start with you again, Mr. Woods.

Mr. WOODS. The first, I would say, is it needs to address the points and the overall cost of the loan, depending—there is a bill that you have today that is out there to do that, and I think that would be helpful. It is having a tremendous effect.

Chairman SHELBY. Uh-huh.

Mr. WOODS. The second thing is I believe that the guidelines should always be in writing. We have a real problem today that many times, and particularly with the auditors and whatever,

there are verbal instructions given as to how they are to treat a loan, but it is not in writing, so it leaves it to somewhat——

Chairman SHELBY. Is it ambiguous? I mean——

Mr. WOODS. It is somewhat ambiguous, and the real problem becomes, and I am going to speak to this more as a community banker, you are scared to death about your little bank. You really do not want to be written up. And, so, you are going to step back even farther from the line, and when you do that, that is going to limit the fact of your doing business or if you will do business.

Chairman SHELBY. Basically, you are talking about certainty, are you not?

Mr. WOODS. I am talking about certainty. You are exactly right. Just tell me what the rules are. I can play by the rules. But, I cannot play the game if I do not know what the rules are.

And, then, just the cost of the compliance. And, again, I am talking mostly smaller community bankers. Certainly, in the big banks, they have less ability to spread that cost.

Chairman SHELBY. That is right.

Mr. WOODS. So, if you have to add personnel to a small community bank, they are not making billions of dollars. They are making thousands of dollars——

Chairman SHELBY. And they are not making loans——

Mr. WOODS.——and that one person makes them unprofitable.

Chairman SHELBY. And they are not making loans if they are not——

Mr. WOODS. They are not making loans.

Chairman SHELBY. Chris.

Mr. POLYCHRON. Chairman Shelby, I would say one area, and especially, like, in my market in Hot Springs National Park, Arkansas, FHA has made the restrictions on condo loans to where very few of our developments qualify for those loans. They are an excellent opportunity for first-time home buyers, elderly, minorities, as well——

Chairman SHELBY. Tell me why. Are they cheaper, basically, than a single detached home?

Mr. POLYCHRON. Yes, sir, they are cheaper, A, and they are—a lot of our young people are wanting to move to the downtown areas——

Chairman SHELBY. And what is the barrier, refusal to make the loan, or what is it?

Mr. POLYCHRON. Well, basically, the restrictions require 100 percent or a high percent of the whole development before it can be done. They are usually run by private boards and those people are not qualified, and as a result, they just do not finish the process. We have been working with FHA to try to alleviate that and, hopefully, something will happen soon.

I agree with Mr. Woods, second, that—take GE Finance. They recently announced they are going out of business because the cost to do business——

Chairman SHELBY. No, they are not going out of business. They are selling to somebody.

Mr. POLYCHRON. Well, they are selling their——

Chairman SHELBY. Yes.

Mr. POLYCHRON. They are going out of the finance business for us——

Chairman SHELBY. Right. Right. Right.

Mr. POLYCHRON.——and, you know, they listed compliance, regulations, cost of doing business.

Chairman SHELBY. Mr. Motley, one or two, your top ones.

Mr. MOTLEY. I think that one of my top points is the restrictive nature and the very prescriptive nature of the QM rules themselves, for instance, the 43 percent DTI ratio, and I will give you an example. Just last week, we had a self-employed borrower that was making an application with our company. It was a jumbo loan, so we could not avail ourselves of the GSE patch. So, this was a jumbo loan. Our investor required that the loan be QM.

In this particular case, this borrower had been self-employed not quite 24 months, which is required under Appendix Q of the QM rule. So, even though we had great income history, we had a record of good credit, we had good downpayment, all of that, it did not meet the QM standard because he had—we could not justify or could not show that he had been self-employed at that level of income for 24 months, only 23. So, we could not make that loan.

It did not matter that it was an 80 percent loan. It was not a high level, high LTV loan. But, that is the kind of one-size-fits-all in Dodd-Frank that just does not work. We need some ability to exercise prudent judgment. We are not talking about going back to NINJA loans. We just want to have the ability to make prudent loans——

Chairman SHELBY. So, you think that is a literal interpretation of the 24-month deal——

Mr. MOTLEY. I do.

Chairman SHELBY.——rather than a little bit of flexibility, just a little. And, you thought that was a good loan, did you not?

Mr. MOTLEY. Yes, sir.

Chairman SHELBY. OK. Ms. Gordon.

Ms. GORDON. I do agree regarding the uncertainty in a variety of areas, but I will mention a couple of other things. One is pricing and downpayment, and that is because we are suffering from a problem with income and wealth inequality in this country, especially for communities of color who represent the majority of home buyers of the future. I would strongly suggest that we do more risk pooling, particularly Fannie and Freddie, rather than really excessively tiering the pricing, but we——

Chairman SHELBY. Explain what you mean exactly. You are talking about——

Ms. GORDON. So, Fannie and Freddie had historically—they created this national mortgage market so we were not that dependent on what happened in particular regions of the country, you know, if one region had a downturn, and they made mortgages really a commodity. So, there was basically a price most people in the country kind of knew what their mortgages would be.

Because of the crisis, when Fannie and Freddie went into conservatorship, the conservator created this very steep grid of, you know, you pay a lot more for a mortgage, for example, if you are only able to afford a smaller downpayment——

Chairman SHELBY. OK.

Ms. GORDON.——even though you still have to have Private Mortgage Insurance to cover that, and that has been a real problem, particularly for the folks who were hardest hit by the crisis and who may have less family wealth.

I also hope that the whole mortgage industry can work together on the problems of wage stagnation and income inequality because that is just a big part of the market problem today, is affording a home.

Chairman SHELBY. Sure.

I will address this to you, Chris. In your testimony, you express support for legislation allowing communities to appeal to the CFPB for consideration as a rural community. You know, the small towns and the rural areas of America make up a lot of America, as you testified. Would you elaborate on what could be at stake if otherwise rural communities are not technically recognized by the CFPB as rural and so forth? Go ahead.

Mr. POLYCHRON. I can even give you a personal example in my own State.

Chairman SHELBY. OK.

Mr. POLYCHRON. We recently had a State director make a ruling that one of our areas was no longer rural. We had no recourse but to go to her, and we ultimately convinced her——

Chairman SHELBY. But, you were not urban, though, were you?

Mr. POLYCHRON. No.

Chairman SHELBY. OK.

[Laughter.]

Mr. POLYCHRON. And, we finally convinced her that it was rural. If we had not had the ability to bring that back up, those people would not have been afforded the opportunity to do a 502 through Rural Housing. So, I would tell you that other reasons—there are areas like, take Fayetteville, Arkansas, where the University of Arkansas is. A lot of that population is counted in the Census and it would make it look like that area is urban when it really is not.

Chairman SHELBY. It is a distortion, is it not?

Mr. POLYCHRON. It can be a distortion, yes, sir.

Chairman SHELBY. OK. I have a number of other questions I will submit for the record. We are into time constraints.

Senator Brown.

Senator BROWN. Thank you, Mr. Chairman.

Ms. Gordon, I will start with you, and then I have a question for Mr. Motley. Working families trying to buy a home, as you pointed out, seem to have the deck stacked against them. Stagnant, slow wage growth, increasing student loan debt burdens, combined with the recent increase in home values can reduce a family's ability to save for a downpayment or reduce their other debts to qualify for a loan. What impact are these—we have heard about Government regulations as the major reason, or almost the only reason from other panelists. What impact are these economic factors having on the housing market?

Ms. GORDON. So far, we have not actually seen any evidence that the problem in the housing market is the financial reforms. We have seen quite a lot of evidence that downpayment requirements and general tightness of the credit box are a problem, particularly since some of the biggest actors in the system still use old credit

models that do not take new developments into account. And, we also have seen how a lot of the uncertainty, the uncertainty about the system generally, with Fannie and Freddie still in conservatorship, as well as uncertainty about repurchases, about default servicing costs and the like, that is really holding the market back.

We really have seen no evidence so far, and there have been some studies and surveys on this, that QM is really making much of a difference, and particularly for smaller institutions who have a number of exemptions. By and large, community banks are lending the same way they always did.

Senator BROWN. Thank you.

Mr. Motley, the title of today's hearing is about helping borrowers get access to mortgage credit. So far, we have heard a lot from the panel about what Congress could do to help lenders. Thank you for that insight and those thoughts.

According to *Bankrate.com,* the interest rate on a 30-year mortgage averages around 3.8 percent, even with a 660 credit score and paying 5 percent down. That sounds like a pretty good deal by any historical standard.

If the issue, therefore, is not the cost of a mortgage, what prevents you from making this kind of loan, and how does a proposal like allowing lenders to charge higher fees give homeowners—give potential homeowners, give borrowers more access to affordable credit?

Mr. MOTLEY. Let me answer your last question—I will answer your last question first. Low- to moderate-income borrowers typically are going to have smaller loans, smaller purchases. So, fees, closing costs, are often reflected in fixed amounts rather than a percentage of the loan. So, a smaller balance loan is going to hit that 3 percent points and fees cap sooner. So, if I cannot premium price the loan, raise the interest rate, to cover some of those fees through premium, then I am not going to be able to make that loan and stay within the 3 percent points and fees cap and, therefore, a QM.

Now, there is another regulator——

Senator BROWN. But, you could make the loan. You just could not get QM protection, correct?

Mr. MOTLEY. Right. That is correct. So, I have got to weigh the option of going with a rebuttable presumption risk as opposed to a safe harbor.

Now, I can only raise the rate so far because there is another Governor on this protection for consumers. Currently, in order to stay in a QM state, I cannot go above 150 basis points above the average prime offer rate. Now, the average prime offer rate is a lookback. It is an index that was published, let us say, last week. So, in a rising rate environment, I am automatically squeezed when I look at that calculation. So, I need to have that APOR margin, the margin over APOR, increase so that I can counteract the effect of potentially rising interest rates.

And you know that interest rates are historically low. They have been low for a long time. We all think, eventually, they are going to go up. They have not yet, but that would help, if we could have a 200 basis point spread over APOR and still retain QM status, as

well as we could handle more small balance borrowers if we could increase the points and fees cap.

Senator BROWN. Well, I think it is—thank you for that response. I think it is important to remember these mortgage rules provide legal liability protection. Nothing prohibits you from making these loans if you think they are good quality loans and the chances of repayment are high. They really shift the burden to the borrower to show that a lender knew they could not pay back the loan.

Obviously, that is the story of QM, understanding that lenders can go ahead. They can make that loan. They just do not have the legal liability protection afforded by QM. I think it is very important to make that point. The Government is not telling anyone they cannot make these loans. They just do not get the legal protection afforded by QM, so I think it is important to note that the lender here is making a business decision. Is this loan likely to be paid back?

Let me ask one more question with Ms. Gordon. The CFPB released updated small and rural lender definitions earlier this year in response to concerns about the previous definition, as you know. How does the new proposal change the small and rural lenders that qualify for exemptions? Are there other exemptions that they already qualify for?

Ms. GORDON. Well, like I said, in my written testimony, I actually provide a whole list of exemptions that smaller lenders already have, and the new proposals, I think, will also be helpful and, to me, really demonstrate how the CFPB is really trying to take into account the concerns of the mortgage industry.

I should note on your previous question that there is also an exception from the 3 percent points and fees cap for loans under $100,000, which covers quite a lot of the loans that go to low- and moderate-income people around different parts of the country, though maybe not right here in Washington, DC.

Another compromise that the CFPB created was as passed by Congress, there actually was no safe harbor. There was just something called a rebuttable presumption, which is lawyer talk for who has the burden of proving what. And, the industry went into CFPB and said, we really feel like we need this real legal immunity and they were given that extra that was above and beyond what the statute had said.

So, there have been quite a lot of compromises with CFPB. I think in a number of them, consumer groups have worked with business groups very productively and, I think, will continue to do so at the CFPB. And, at this point, this is why I do not think on most of these things we really need Congressional rollbacks of the actual statute.

Senator BROWN. I think the point you make, and then I will yield, Mr. Chairman, about the cost of homes, you said the $100,000 figure. The median list price in the Midwest region, according to the National Association of REALTORS®, for home sales is $152,000. And in the Cleveland area, 9,000 homes—so, it is not a small sample—it is $128,000. In Akron, it is $108,000. Across the border in Indiana, it is around that same price. So, that is a lot of homes, that is the median price.

Thank you, Mr. Chairman.

Chairman SHELBY. Senator Cotton.

Senator COTTON. Thank you.

I would like to discuss legislation I cosponsor with Senator Donnelly that Mr. Polychron mentioned earlier, S. 682, the Preserving Access to Manufactured Housing Act. Ms. Gordon, I would like to start my questions with you. Were mortgage loans a prime driver of the financial crisis in 2007, mortgage loans to manufactured housing owners?

Ms. GORDON. So, actually, mortgage loans to manufactured housing owners have been a problem far longer than the financial crisis. You know, there are two different ways that those loans can be titled. They can be titled as real estate or as chattel, and the chattel loans have long had far fewer consumer protections, and those loans have always been a lot more expensive than loans for site-built homes.

And, so, the many households who rely on manufactured housing, which is a really important, as you know—I mean, in your State—actually, I am looking around the room, in all of your States, manufactured housing plays a really important role in some communities. You know, that was in particular need of consumer protection even before some of the excesses that were associated with the Wall Street private label securities, because you are right, the manufactured housing did not really have that intersection.

I think it is really important to help increase safe and affordable credit for manufactured housing and, in fact, have been urging the Federal Housing Finance Agency to include—to incentivize more and better manufactured housing loans through their Duty to Serve rulemaking by actually including chattel loans as well as real estate titled loans, and I think that is going to be a really important effort, and I have also been working with some business groups on that.

I do not think the right way to go about solving the very real problem of credit for those loans is by removing consumer protections that attach to higher-cost credit.

Senator COTTON. So, I infer the answer to my question is no, mortgage loans to manufactured housing owners were not a prime driver of the 2007 and 2008 financial crisis.

Ms. GORDON. Well, they were not a prime driver of what happened on Wall Street, but they were very much a part of the lost wealth and foreclosures of families.

Senator COTTON. Were those loans a primary part of collateralized debt obligations or credit default swaps that caused the problems that led to the financial crisis?

Ms. GORDON. Absolutely not.

Senator COTTON. You state in your written testimony that if our legislation passed, the Preserving Access to Manufactured Housing Act, quote, "a lender could charge nearly 10 percentage points higher than a prime mortgage rate," end quote. I infer that you think that that is a bad thing.

Ms. GORDON. So, higher-cost loans are sometimes—I mean, there are a lot of reasons, a lot of good business reasons to charge higher rates under certain circumstances. But, studies have repeatedly shown that higher rates are actually in and of themselves an additional risk factor. So, if you are in a situation where those higher

rates are important and necessary, giving consumers some extra protections against other predatory features is really important.

Senator COTTON. Section 1431 of the Dodd-Frank Act empowers the Consumer Financial Protection Bureau to allow points and fees up to 10 percent on high-cost mortgages. Do you think that section of the Dodd-Frank Act is not sufficiently protective of consumers?

Ms. GORDON. Well, one of—what Dodd-Frank did was they actually revisited the thresholds that had previously existed for HOEPA loans, which are the high-cost loans, and those thresholds had been established at a time where, generally, rates were really, really high for all mortgages, and they adjusted them downward to reflect the new rate environment.

And, I should note that the CFPB actually has extremely broad exception authority to virtually everything in the statute, and working with the CFPB continues to make sense, and they have continued to balance interests pretty well. But, I do not think there is any reason to revisit the statute, no.

Senator COTTON. So, I would note that our legislation simply acknowledges the economic fact that mortgage loans for manufactured housing are often a quarter of the cost of homes for site-built, or site-built homes, and the origination costs, though, do not always fall that low and, therefore, these fees can be somewhat higher.

Mr. Polychron, would you like to describe the importance of manufactured housing in places like Hot Springs National Park, Garland County, in Arkansas?

Mr. POLYCHRON. Yes. Manufactured housing is a big part of it, especially for minorities, for people that cannot afford the higher-priced homes. I would submit that even if the cost was, say, ten basis points higher, a lot of times, that manufactured home buyer can still purchase a home and have payments less than he would with a higher-priced home, and I think that individual would like that option.

Senator COTTON. Would it be fair to say that, sometimes, that can even be lower than what they might be paying for rent in places like Arkansas?

Mr. POLYCHRON. It would be by far. Rents have gone sky high in our State, mainly because the difficulty to get credit. I foresee renters at some point, hopefully soon, converting to home ownership again.

Senator COTTON. Thank you.

Chairman SHELBY. Senator Menendez.

Senator MENENDEZ. Thank you, Mr. Chairman.

Mr. Chairman, I think about this topic and I go back to the time we were here, where mortgage lending was at the heart of the financial crisis and borrowers of modest means received risky subprime loans they could not afford as financial companies chased profits and left taxpayers on the hook for the downside. And, we know the damage that the crisis caused. Families lost their homes, their jobs, their savings. Businesses had to close their doors and communities were devastated by foreclosures.

So, the crisis reminded us how important a healthy mortgage market is to our economy, not just to financial stability, but to families' ability to build wealth and strong communities. And, as our

economy continues to recover, the pathway to home ownership, I believe, must remain open and affordable.

Now, I understand no legislation is perfect, and in areas where regulations are an obstacle, we should look to improve them. At the same time, it can be tempting to blame regulation for broader market challenges or to use unrelated problems as a pretext for rolling back consumer or financial stability protections. So, I look forward to working with my colleagues on the Committee to find ways to improve access to credit, but to consider all the elements of that.

In that context, Mr. Woods, in your testimony, you discussed the recent moves by Fannie and Freddie to back well underwritten loans with downpayments as low as 3 percent in cases where borrowers can demonstrate their ability to repay and other compensating factors. As, I think, almost everyone here knows, saving for a downpayment can be a significant obstacle for a family to purchase a home. Would you say that this decision by Fannie and Freddie represents a positive step by giving a greater number of creditworthy borrowers an opportunity to responsibly and affordably purchase a home?

Mr. WOODS. I think it is a very responsible—I am sorry. I would say it is a very positive step. There is one indicator out there that for years stands out when we talk about the 3 percent, or 2, or wherever you are at. VA loans perform quite well, and they are zero down loans, and they have always performed, but they have some other guidelines within them that help that process. Plus, that individual has some training in responsibility.

Senator MENENDEZ. Mm-hmm. Do our other witnesses agree?

Ms. GORDON. Absolutely. I think that the ability to get a home with a lower downpayment is absolutely critical for today's home buyers. And, I want to note that what is really important when you are thinking about lower downpayments is making sure you are not layering other risks in there. It was not low downpayment products that caused the crisis. It was the risk layering. And, so, that is why, especially when it is so important right now to have these low downpayment products, because families really do not have that much wealth, that is why it is absolutely not the time to ease up on the other protections.

Mr. MOTLEY. Senator, I agree with Ms. Gordon completely. As long as the 97 percent loan is prudently underwritten, we are not layering risks, I think it is a good step toward reviving the housing market.

Senator MENENDEZ. Mm-hmm.

Mr. POLYCHRON. And, Senator, I would concur. I would also add that the lowering of the FHA fees from 1.35 to 0.85, you know, on a $200,000 house made a difference of $90 a month, and it certainly brought more first-time home buyers into the market.

Senator MENENDEZ. Good. Now, let me ask you another question. Almost all of you discussed in your testimony how updated credit score models can improve loan underwriting and expand access to a broader population of potential buyers, particularly in underserved communities. The developers estimate these new models can provide scores for anywhere between 15 and 40 million previously unscored consumers.

Can any of you share with me what are the biggest obstacles to widespread adoption of the newer, better models? Is it implementations by the GSEs or is it other factors?

Mr. MOTLEY. In my opinion, it is implementation by the GSEs. They just have not gotten around to technologically utilizing those models.

Ms. GORDON. Well, there are some other obstacles, as well, which is that particularly rent reporting, which is a big part of the newer experiments with scoring more people, you are relying on a lot of private landlords, often mom-and-pop landlords, to do that reporting, and I think that is going to be a challenge to make sure it is done right. But, I think it is really important and will allow many more people to be scored.

On scoring utilities, I think there are some special problems there that you have to really make sure you have consumer protection. Many folks benefit from utility subsidy programs, particularly in the colder States, and utility companies are well known for a lot of billing problems. So, this has to be done carefully, but I think both FICO in updating their models and VantageScore have been really working on this quite carefully and it is very important that Fannie and Freddie get contemporary with this.

Senator MENENDEZ. Thank you, Mr. Chairman.

Mr. MOTLEY. And, I would just follow up with that, is that for years, we have used alternative credit like you are talking about with utilities, with a rent bill, something that is not reported to the credit bureau. But, being able to have this put into a system and actually graded will assist us in evaluating borrowers who have thin credit.

Chairman SHELBY. Thank you.

Senator Sasse.

Senator SASSE. Thank you, Mr. Chairman.

Ms. Gordon, not to keep you in the crosshairs the whole time, but I appreciated some of your comments about PMI and mortgage insurance. I think that many of the comments that you have made, though, about the possibility of exemptions from Dodd-Frank, I wish we could have the time to take you to a small town in Nebraska and you could sit with some community bankers. And, so, I wonder if we could do that as a thought experiment.

Many of these folks do not have any sense that they were a contributing factor to the fall of 2008. It is not entirely clear to me if you think they are guilty. They think that they are guilty in the eyes of Washington and lots of regulations that they cannot navigate. I will not bore you with all the technical archana, but in a lot of towns in Nebraska, the average mortgage is well under $100,000, and I have sat with these community bankers and it does not make economic sense for most of them to be writing mortgages at all. They do it as a community service, but it is not an economically viable business.

Could you explain, in small town Nebraska, where a lot of mortgages are less than $100,000, do you think they did something wrong in the run-up to 2008, and if so, what?

Ms. GORDON. I do not see small community banks as the root of the problem in 2008. I would love to work with you on a positive agenda for helping smaller institutions be competitive. I think it is

important to note that smaller institutions have been declining for decades, long before the crisis, and a lot of that is because the economics of the business right now tend to, you know, push toward larger institutions where you can spread the fixed costs better.

I think there is quite a lot that can be done in the area of technology to help bring down the costs of compliance, because, I mean, we could get rid of all of Dodd-Frank tomorrow, but there would still be myriad other regulations that banks would have to comply with and a lot of that is susceptible to technology. Some of the larger institutions have the resources to do that.

And, I think it is really important, and that regulators should be involved in this, too, in trying to make sure we are developing the infrastructure of sort of off-the-shelf, cloud-based resources that can be used.

I have talked to a lot of small lenders. I know when they think about replacing their technology systems, that sounds almost insurmountable to them, and this is true in the small nonprofit sector, as well. Unfortunately, it just has to be done to keep current, and I would love to work on a positive agenda to help do that for that sector. I think that sector is very important.

Mr. MOTLEY. And, if I could follow up on that just a little bit——

Senator SASSE. Please.

Mr. MOTLEY.——talking about the infrastructure necessary to incorporate and to build these regulatory requirements into our systems. You know, 2 years ago, we had three people in our compliance area. We had two workers and an administrative person. We now have 12 people in our compliance area.

And, when you think about TRID, a 1,700-page document, well, my goodness, we had to hire all those people so they could read it, so they could figure out how to implement it and figure out how to—what does this mean to the business process every day. And, then we have to go train on it, and we have to make sure that our loan officers know how to do it.

And, specifically with TRID, you have got this new waiting period between the time that you issue a closing disclosure and the time that you can actually close on the mortgage or consummate the mortgage. That means that real estate agents, builders, title people all have to be trained. So, this is a tremendously difficult task that we have in front of us to try to implement TRID.

So, it is just to say what Ms. Gordon is saying, is that the training burden of implementing these regulations is really quite great. And, I would follow with that and say that we are hopeful that we can get the CFPB to delay via rule implementation of enforcement on this TRID rule, because we have really been inundated over the last 24 months with myriad new rules and we are up to here. We are choking. We are about to drown.

Senator SASSE. That is helpful.

I have got less than a minute left, so Ms. Gordon, could we go back to you just for a minute. So, then, go upstream one step. Give the 45-second—I think that is all the Chairman is going to let me have—give the 45-second answer to what was the contributing factor of the housing bubble for lower-income and middle-income families in rural places where housing is cheap. What regulatory prob-

lem was not being addressed that they contributed to that required any new regulation in 2008.

Ms. GORDON. Well, here is what happened, and this is what is so important now, is those small community banks did not cause the crisis, but their larger brethren, in fact, did, and what we have seen during the lobbying before Dodd-Frank was passed, during Dodd-Frank, and after Dodd-Frank is, actually, you see a lot of institutions that are not the kind of banks that you are talking about kind of hiding behind the skirts of those banks and using them as an excuse to get out of the regulations that are really important for the institutions that were, in fact, involved in the shenanigans that ultimately led to the crisis.

Senator SASSE. So, just to interrupt for a second, though, but, I think, in earlier questioning, you said there are potentials for exemptions from Dodd-Frank and from other regulatory regimes that could be applied to these people. Let us not talk about whether or not big banks did some—were bad actors and they are hiding behind the small banks. I am asking you, why was there new regulation necessary on mortgage products for $50,000 and $75,000, period? These exemptions could be used, but they are not being used. So, what was the problem that required these new rules to be applied to lower-income and middle-income people in places where housing markets are cheap?

Ms. GORDON. So, lower-income and middle-income people were the victims of this crisis and what we had to do was regulate the products. You know, the page six——

Senator SASSE. And, so, those products are evaporating——

Ms. GORDON. Page six has a list of the exemptions which were put in there because we know a lot of those community banks have a model where they make the 3- or 5-year balloons, right. They do—you know, they may service fewer than 5,000 loans. They have a lot of exemptions here, but the fact is, when you regulate an industry, you have to regulate for the vast middle of the industry and this is—I think these exceptions are a very appropriate way, and if there is a reason that they are not using those exceptions or taking advantage of them, I think that is a training and education and regulatory issue we should work on.

Senator SASSE. Yes. I do not think that is accurate. I think there were mortgage products that were available with 15 to 20 pages of paperwork that are now hundreds of pages, and I think your answer is, regardless of whether or not there is a problem, let us empower bureaucrats, and then later you can come and supplicate before the bureaucrats and see whether or not you can get a carve-out. That is not what is happening, though. The access to mortgages is being reduced and eliminated in rural communities, and the argument is, you could go and ask for regulators to later give you the freedom to offer products that were not a part of the problem.

Ms. GORDON. So, if you look at who is originating mortgages right now, actually, small institutions are originating more than ever and their profits on mortgages are increasing faster than the profits for any other sector of banks making mortgages. So, you know, I hear that there is an issue. Many of these exemptions were baked into Dodd-Frank. These were not just regulatory decisions.

Others were regulatory decisions made after they heard from representatives of these small banks. But, I do not see why an exemption is different than not having the rule. The fact is, you do not have to do the rule if you have an exemption.

Senator SASSE. I wish we had more time. Thank you.

Chairman SHELBY. Mr. Motley, let me pick up on something you said, then whatever you want to add, and then I will recognize Senator Warren. You said a minute ago, as I understood it, that you had to go from 2 people to 12 people on compliance, is that correct?

Mr. MOTLEY. Yes, sir.

Chairman SHELBY. That is six times the cost of personnel.

Mr. MOTLEY. Yes, sir.

Chairman SHELBY. Somebody has to pass that on or you go out of business, right? It is added to the cost of doing business.

Mr. MOTLEY. Yes, sir. It is added to the cost of doing business. I am not doing any more loans, but I have more compliance——

Chairman SHELBY. Is there not some way, picking up Senator Sasse's comments, to streamline these regulations and put them in plain, unambiguous English where people will know what is certain there and what is not? Could it be——

Mr. MOTLEY. Yes, sir——

Chairman SHELBY. It looks to me like——

Mr. MOTLEY.——I believe it is, and we support holistic fixes, not carve-outs for individual things.

Chairman SHELBY. No, no——

Mr. MOTLEY. We want some holistic fixes that allow lenders to have underwriting guidelines that are prudent.

Chairman SHELBY. When you say fixes, you mean certainty and guidelines?

Mr. MOTLEY. Yes, sir.

Chairman SHELBY. OK. Senator Warren.

Senator WARREN. Thank you, Mr. Chairman.

You know, I agree with a lot of what has been said here today. Access to mortgages is painfully tight, especially for people who are not well to do, and we should find responsible ways to increase access to credit. I am there.

But, once again, there are a lot of proposals that are being pitched as improving access to credit that are really about letting the mortgage industry dig deeper into consumers' pockets, and I think a good example of this is the Mortgage Choice Act. After the crisis, Congress decided that a lender could get the protection of the Qualified Mortgage Rule only if the points and fees on a mortgage were less than 3 percent of the loan amount. Now, if the lender is affiliated with the title company, the cost of title insurance through that affiliate counts toward the 3 percent cap, which makes sense because most of the cost of title insurance is commissions, and most of that revenue is going to find its way back into the lender's pocket.

You know, the 3 percent cap is an important step toward fixing the broken noncompetitive market for title insurance. For other forms of insurance, not title insurance, where there is a competitive market, between 50 and 80 cents of every premium dollar goes to

paying out claims. But, for title insurance, according to the GAO, it is five cents, one nickel out of every dollar that is collected.

The GAO also reports that more than 70 cents on every dollar is pure commission for the title agents. Subjecting affiliated title insurance costs to the 3 percent cap should help bring some competition and lower these artificially inflated prices.

Now, Mr. Motley, as you know, the Mortgage Choice Act would blow up the 3 percent cap by exempting the affiliated title fee. It says that you can separate it and get money from two different sources. In your testimony, you claim that applying the cap to affiliated title insurance fees has made, quote, "low-balance loans serving low- and moderate-income borrowers much costlier to originate and, consequently, less available to consumers." In other words, the cap—that is the part this part of your testimony is about—is making it harder for people to get low-dollar loans.

Now, I care a lot about the question about access to low-dollar loans, so I have looked closely at the data since the 3 percent cap went into effect last year and I just cannot find any data to support that claim. I have also asked companies to give me some data to back up the claim, but so far, nobody has done that.

So, I notice that you do not cite any data in your testimony and I would like to know what data you are looking at to support your claim.

Mr. MOTLEY. Senator, I am actually considering the combination of the affiliated title insurance—we had an affiliated title insurance company. With the new rule, as you have stated, we were required to include the title insurance premium, and I would disagree with you in the sense that the title insurance premium in Texas, anyway, is the vast majority of the total fees charged to a consumer. It is not a minority. It is the majority of those costs.

Senator WARREN. Well, all I can do is look at the Government Accountability Office report on this——

Mr. MOTLEY. OK.

Senator WARREN.——and that is that for title insurance, the amount that is paid out is a nickel for every dollar brought in. If you have got better data than the GAO, then please bring them in.

Mr. MOTLEY. OK. I will get back to you with that. But, with regard to the——

Senator WARREN. I would like you to.

Mr. MOTLEY. With regard to the affiliated title insurance question, I had a title insurance—we had an affiliated title insurance company for about 6 or 8 years. One of the reasons that we had that title insurance affiliated company is because we felt like we could provide better service to our mortgage customers, particularly in a refinance scenario, where I could actually meet or beat the costs of a competitor by using my affiliated title——

Senator WARREN. Mr. Motley, since we have very limited time, let me just stop you right there. I have no doubt that you can get revenue from your title insurance company and you can get revenue from your mortgage lending business. The question I am asking is what data you have to support your claim in your testimony in which you said specifically, low-balance loans serving low- and moderate-income borrowers are much costlier to originate and, consequently, less available to consumers because of the 3 percent cap.

I cannot find any data to support that and I just want to know what you are using.

Mr. MOTLEY. Thank you. Let me say that what happens is, with an affiliated title company, I have got to include those affiliated title charges in my loan origination cost, so that becomes part of my costs and fees. So, at a certain level, I go over those caps.

Senator WARREN. I understand that, that you are not going to get as much money. The question is, why does that stop you or raise the cost? Do you have any data to support——

Mr. MOTLEY. Well, it is not just that I may not make as much money. It is also a competitive issue, because when I look at my affiliated company and my disclosure to the borrower on my good faith estimate, my costs are going to be higher than if I used a non-affiliated company, or if someone else was comparing my disclosure to a non-affiliated company.

Senator WARREN. I am going to take that as you have no data, other than how you describe your business model on how you make money. Maybe I should just ask this——

Mr. MOTLEY. I will try to get—I will get back to you with some data.

Senator WARREN. I would be delighted to see that.

Let me ask this another way. Data from both Fannie and Freddie Mac and the mortgage industry show that the average mortgage origination fees are under 1 percent of the loan amount. So, that means for a $100,000 loan, a lender can typically charge more than $2,000 for title insurance and still be under the cap. Since claims are only eating up about five cents of every premium dollar, that leaves about $1,900 in commissions before you hit the cap. Is that not enough?

Mr. MOTLEY. Senator, you are asking me about the commission structure with title insurance companies and I am not involved in that business anymore.

Senator WARREN. Well—thank you. I just want to say, the Mortgage Choice Act should not fool anyone. The CFPB has already exempted the vast majority of smaller lenders from the QM rule, including the points and fees cap, for any loan they hold on portfolio. So, this is really about bigger lenders. This is about trying to get bigger fees from consumers. It is about preserving a cash cow for the mortgage industry and not about access to credit and I urge my colleagues to oppose this bill.

Chairman SHELBY. Senator Corker.

Senator CORKER. Thank you. This is an interesting hearing.

Mr. Motley, a large group of us on this Committee wrote a letter to FHFA about the Common Securitization Platform they are developing, asking to make sure we had enough outside advising, if you will, to make sure that it was not just crafted only for Fannie and Freddie's use. Do you think it would be appropriate for somebody from the mortgage industry to actually participate in that panel?

Mr. MOTLEY. Yes, sir, I do.

Senator CORKER. OK, and just for the record, I hope that is something that we will pursue.

I want to follow up on Senator Warren's comments. What I see happening here is people, generally speaking, on my side of the

aisle are trying to develop legislation to change the rules of Dodd-Frank to create better access to mortgages, if you will. What I see happening on the other side of the aisle is that Senators, instead of pursuing it that way, they are trying to create better access to mortgages by trying to get FHA and Fannie and Freddie and others to loosen up on the Government side. So, it is an interesting thing. Republicans are trying to write legislation to fix it, but what is happening is my friends on the left are trying to push the federally owned entities from getting them to do the same exact thing. So, both of us, if you look at it, really, both of us are trying to create access to credit. We are just doing it in different ways.

And, I would just like to ask the question, would it not make more sense, instead of maybe us pursuing this route and then pursuing that route, would it make more sense for us just to go ahead and do comprehensive housing finance reform and create certainty and solve the problem once and for all? I would just like for the witnesses to potentially respond to that.

Mr. MOTLEY. It absolutely would.

Mr. WOODS. It would.

Mr. POLYCHRON. [Inaudible.]

Ms. GORDON. I support comprehensive housing reform, as you know, but we would also still need the regulatory protections of Dodd-Frank.

Senator CORKER. Yes. Well, that was not the question, so——

[Laughter.]

Senator CORKER. So, I think—really, as I hear this, really, it is pretty fascinating. I mean, I do not think my friends on the left would disagree that they are constantly urging Mel Watt and urging Fannie and Freddie and FHA to make access to credit more available by not using legislation. This side of the aisle is pursuing it the other way.

And, I do not know. You know, we have heard this, it is often quoted—it is too often quoted—we seem to finally do the right thing after pursuing every other route. I just think we are kind of spinning our wheels and trying to avoid the essence of what needs to be done here, and that is housing finance reform done that creates certainty for all of you, right? I mean, this would sort of be over and done, and I hope that once we get through playing around, if you will, with the issue, dealing with the fringes, we can get to that, and with that, I have no other comments, unless you want to make one, Mr. Polychron.

Mr. POLYCHRON. I would, if I could, Senator Corker.

Chairman SHELBY. Go ahead.

Mr. POLYCHRON. The only thing as a practitioner that I would be caution—I would be fearful of tax reform is—and I know in your bill——

Senator CORKER. I did not say anything about tax reform.

[Laughter.]

Mr. POLYCHRON. Well, house reform.

Senator CORKER. Well, housing and tax reform are very different.

Mr. POLYCHRON. I understand.

Senator CORKER. OK.

Mr. POLYCHRON. But, at the same time, anything that would impair a practitioner from a 30-year mortgage is a no-no. I mean, it is just going to hurt our business.

Senator CORKER. Well, I do not think anybody that I know of on this panel has seriously proposed any legislation that would do away with a 30-year mortgage.

Mr. POLYCHRON. Yet.

Senator CORKER. Has anybody up here done that?

Mr. POLYCHRON. Not yet. No, sir.

Senator CORKER. All right. Thanks a lot. I appreciate it.

[Laughter.]

Chairman SHELBY. Senator Reed.

Senator REED. Thank you very much, Mr. Chairman, and thank you to the panelists for your testimony. I apologize. There was a simultaneous hearing in the Armed Services Committee and I had to be there.

Ms. Gordon, Dodd-Frank established numerous protections for borrowers, particularly middle-class borrowers, and the changes that are being proposed, if enacted, how would they affect sort of the middle-class borrower, in your view?

Ms. GORDON. Well, a number of the changes we have talked about today would make mortgages both more expensive and more risky. I mean, just to go back to the Mortgage Choice Act for a second, or the so-called Mortgage Choice Act, affiliates were a big part of what was going on in the run-up to the crisis. There were kickbacks and upselling rampant throughout the system, which ends up making a mortgage more expensive than it has to be, and it is very anti-competitive. It is always interesting to me that that is not seen on all sides of this room.

And, Dodd-Frank could have made the choice to simply ban these affiliate arrangements. It did not do that. It just said, if you want to be in that super safe category of QM mortgages, you cannot go above this points and fees cap, which seems to me to be a fairly minimal and very reasonable way of enabling affiliate relationships to continue, even though they could have gone another way.

Particularly this question of all portfolio loans being QM, I think that is especially dangerous, just because with a QM loan, there is nothing anybody can do about it if it goes bad, and you do not want to kind of blow open this whole exception where any kind of loan, no matter how dangerous or risky it is, suddenly gets this special legal immunity. And, I think that is especially important for folks who are not going to have the money to hire a big fancy lawyer and for whom, really, every dollar out of their budget matters. We want to get them as fairly priced credit as we can.

Senator REED. Thank you.

Let me just, to Mr. Polychron and Mr. Motley, ask a question, because we are all looking at, on both sides, access to credit for borrowers that are capable of sustaining the credit. And, one of the factors that I am hearing in Rhode Island, particularly for first-time young home buyers, is this extraordinary student debt. So, when they walk in to see you, they could have a job. They could be decent and hard working and we could have all these QM regulations, but you are just going to say, sorry, you owe $180,000. How

much is student debt really squeezing the mortgage market or denying people a mortgage loan? Are you seeing it? Mr. Motley.

Mr. MOTLEY. Yes, sir, we are, and statistics, I think, from your organization, the REALTORS® Association, show that the percentage of first-time home buyers in today's purchase money market is about 29 percent, whereas, typically, that is above 40 percent. So, we are certainly seeing a smaller piece of the market being comprised of first-time home buyers. We are required—if there is a repayment on that student debt, we have got to include it.

Senator REED. Right.

Mr. MOTLEY. And, so, we are seeing it affect credit.

Senator REED. And Mr. Polychron.

Mr. POLYCHRON. And I would agree with that. In fact, it was into the 50s. It was 56 percent first-time home buyers at one time, and it has definitely affected it, as you would expect.

Senator REED. And, I would presume—you know, this goes to the access to credit. Legitimately, you cannot give loans to these young people, typically young people, although nowadays maybe not so young, because they just are carrying so much debt.

So, one of the consequences in terms of your business, but also in terms of the opportunity to own a home, is not related directly to QM or anything else. It is this huge, staggering student loan debt, which Senator Warren and Senator—I am looking down on my colleagues on both sides are trying to deal with—and I think that is important to note.

Again, I think we want to look carefully and listen to the issues that are arising, but I think we want to tread very carefully in terms of making changes that would disrupt the market.

And, the other thing, too, is that, I hope, that over the last few years, despite all of these factors, my impression is that we are seeing fairly substantial profitability in the industry. Is that the case, Mr. Woods, with community banks, or——

Mr. WOODS. I think that community banks are struggling. I think they are doing better today than they were 4 years ago or 5, but I do not know that they are doing better. But, if you look at a long historical line, that is true.

I wanted to point out two other things with your question on the entry-level buyers and the credit.

Senator REED. Yes, sir.

Mr. WOODS. I want to point out to you how important that is. The truth of the matter is, if the entry-level piece of the market is not working, the rest of the market will not work, because the entry-level buyer, while he may buy my new house, he more likely will buy a used house——

Senator REED. Right.

Mr. WOODS.——and the owner of that used house will move up to another and another. Many times, we have transactions that have three and four transactions behind them. So, you cannot overlook how important that segment of the market is.

I would like to point out one other thing that I think exacerbates the situation, and at least in the crash, if you want to call it that, was a big part of it. Back to community banks. In many cases, the regulators came in and simply told the community bank that they had to cut their portfolio of construction loans, whether they are

model homes or spec homes or whatever. In many communities, that is the only loan that bank is making that makes any money. Their community is growing and they are trying to help that.

You go in and all of a sudden you tell the builder, you have got to get rid of your specs. We will not renew the loan on the specs. You just dumped a bunch of things on the market and now our competition is going to drive down the prices of all the other houses.

Second, when you take away the models, you have just put that builder out of business. That may have been one of the largest employment bases in that community, and the real problem is for the banker, when he tries to force that customer, he can only force his best customer out of the bank. It is the only one that might stand a chance of going and getting a loan at another bank. However, in this situation, that rule was for everybody. So, immediately, that whole access was cutoff, and I do not want that to go unnoticed.

And, what I have seen as a homebuilder, and if you look at our testimony, the real problem is we cannot get loans today. So, we cannot start that engine back up.

Senator REED. My time has expired, but I want to thank you, Mr. Woods, for making that very important point. It is not just the fact that the young 25-year-old college graduate cannot get the loan to buy the first house. It is that that first house is stuck and they cannot move to the second bigger house and the third house, *et cetera*.

Ironically, maybe the solution to this problem is not messing around with these rules but is making sure that people are not coming out of college with $180,000—or graduate school with $180,000 worth of debt.

Thank you, Mr. Chairman.

Chairman SHELBY. Senator Heller.

Senator HELLER. Mr. Chairman, thank you, and to you, the Ranking Member, and also to our expert panel that we have with us today. Thank you for taking time and being here with us.

I want to comment, if I may, just a little bit on what Senator Corker said earlier, and emphasize that he has worked very hard on trying to get some comprehensive reform in the housing industry and it is something that I supported. I worked with him, with both sides, Warner, Tester, others seeing the necessity of this.

And, I think that the key to all this happening and happening right is one thing that you said, Chris, and that is to ensure that every American, especially young families, have access to a 30-year mortgage. I think we all agreed on that. But, we also agreed that there needs to be a secondary market for a backstop. I think the committee, that group that was working together, also recognized the importance of a secondary market, making sure that these securities could be traded, but with the rules and regulations necessary to assure that we do not have 2008 all over again. No State was hurt harder in that recession than the State of Nevada, and I think that you are well aware of that.

I want to go back to something that the Chairman and the Ranking Member discussed earlier in this, and I am just taking a look at the CFPB's rural and urban designation map. The CFPB has been trying, and, frankly, unsuccessfully, to define what rural and

what urban is. In fact, at one point, CFPB even said that Yucca Mountain was in an urban area. Now, I will support that designation if that keeps nuclear waste out of the State of Nevada——

[Laughter.]

Senator HELLER.——but I think they did reverse that particular decision.

I am looking at this map and I am seeing communities like Pahrump, Mesquite, Moapa Valley, Fallon, I mean, these are very small, very small communities. Fernley, Yerington, Minden, you can go on and on, Dayton, they are all listed.

Senator McConnell and I have introduced legislation similar to what the House did. In fact, the House passed legislation that would allow rural constituents to make an appeal and present information to the CFPB and challenge their rural and urban designation. That passed the House, I think with a 401 to 1 vote.

I would like to get from you, one, do you think there ought to be an appeals process, and number two, starting with you, Mr. Woods, whether or not you would support this legislation.

Mr. WOODS. I would, and I do believe there should be a process for appeal. There has to be. Mistakes are sometimes made and they need to be pointed out and a way to correct them.

Senator HELLER. Thank you.

Chris.

Mr. POLYCHRON. And, I addressed this a little earlier in that I agree with you 100 percent. We actually had an incident in Arkansas that precipitated that. You know, the appeal does not mean that they are going to hear eight million appeals. I think the facts are going to speak for themselves, whether they qualify or do not qualify, and in many cases a decision will be able to be made quickly. So, I strongly believe in the appeal process.

Senator HELLER. I listed eight of them, so——

[Laughter.]

Senator HELLER. Mr. Motley.

Mr. MOTLEY. I agree with the appeals process, and I would also urge you to emphasize that consumers will reap the most benefit from this Act if the types of loans identified by CFPB as being critical for meeting the credit needs in rural areas, including loans that do not meet the 43 percent debt-to-income ratio, are considered qualified mortgages if either they are held in portfolio or sold to a creditor that holds them in portfolio.

Senator HELLER. Thank you.

Ms. Gordon, I would love to get your support.

Ms. GORDON. Well, so we have not taken a position on that legislation. The whole issue of rural designation is, of course, one of those things that is rife with complexity among a variety of agencies administering a variety of programs that go well beyond just housing-related programs.

I will note we have been very engaged with FHFA on their Duty to Serve rulemaking, where strengthening credit to rural communities is a really important part of what Congress asked them to do there. They are, in the process of that rulemaking, also looking at the question of rural designation, and I think that is a really important place to intervene, as well.

Senator HELLER. Thank you. Thank you.

I know I am a broken record here, but about 25 percent of the homes—more than 25 percent of the homes still in Nevada are underwater. We have lost probably half of our community banks in the State, probably half of our credit unions, also, so you can imagine—in fact, I would say that I think the statistics show that about 8 percent of the homes sold in the State are short sells.

Mr. Polychron, you are well aware of the Mortgage Debt Relief Act and the attempts of that. I call it ghost income, where the IRS is trying to tax individuals for income they have never seen. What would be the impact to the housing industry if the Mortgage Debt Relief Act were to expire at the end of the year?

Mr. POLYCHRON. It would be big, and I thank you for sponsoring that. You know, the thing I have never understood about that is that someone that has a home that he sells for a profit, or she sells for a profit, is not taxed, yet the individual that is underwater, that takes a loss on that home, does get taxed. I mean, where is the fairness in that? I have never understood that. But, it is there, and without it, those people are going to be renters again. So, I support your bill.

Senator HELLER. Mr. Polychron, thank you for your comment.

Mr. Chairman, my time is up, but again, I want to thank the witnesses and for holding this hearing. Thank you, Mr. Chairman.

Chairman SHELBY. Thank you.

Senator Merkley.

Senator MERKLEY. Thank you very much, Mr. Chair, and thank you all for your insights from your various professions and organizations.

I do think that there is common cause on this Mortgage Debt Relief Act and the concern about short sale streamlining that was mentioned earlier.

One issue that has not really been explored too much here today is the Preserving Access to Manufactured Housing Act. I gather a version of it passed in the House, so we may have more discussion here.

In Oregon, we had, long before the 2008 crisis, a real challenge in our manufactured housing park industry, and the way it worked is people would buy a home, a new home, to be placed into a park. They would buy a park package. But, what they did not realize is the rent could be raised at any time and there was fairly much a shortage of supply in this park world, plus a lot of the parks would only allow a new home to be placed in their park.

And, so, after someone had moved in, then the park would raise the rent or, alternatively, raise the utilities. And, for every $100 of rent or utilities per month that were raised, it diminished the value of the house by $20,000. You can imagine how quickly your new house was worth very little.

So, therefore, the lenders who might lend for these particular homes were very nervous about it, so they wanted to do short-term loans. They wanted to do very high interest rate loans, which made a lot of sense because there was enormous risk embedded in this. People did not own the land and they did not control the rent and they did not control utilities.

And, we looked at a number of ways to try to avoid this. What we heard time and time again from owners in these parks was, if

I had understood how this works 6 months ago, I would never have bought this house. And, so, we had different proposals to—how could owners understand the deal they are getting into, the fact that the rent is not controlled, the utilities are not controlled, the fact that you cannot move your house to another park, the fact that moving your house, if you can find another park that would take it, would be extraordinarily expensive, because it is really operated as a predatory operation.

And, then when a person had to sell their home because the rent had raised sufficiently, the only person who would buy it would be the park owner. The park owner would then lower the rents and sell the house to a new family.

So, this is the type of predatory operations that do not serve low-income families well, and I can certainly understand why lenders would be very reluctant to enter into that world, or only at extraordinarily high terms, but then were charging much more. As the expression goes, it is expensive to be poor. You are paying far more in interest than an ordinary person.

Should we be addressing any of these factors, and how does this affect this conversation about changing the terms of the loan parameters for lending on manufactured housing that is placed into a situation where you do not own the land or control the utility or rent costs? Would anyone like to comment on that?

Mr. POLYCHRON. Do you think some of these could be an exception, I mean, just maybe to Oregon? I am not singling out Oregon, but, I mean, you know, I have not experienced that in my own State, and I do not know if you all have experienced that, either.

Mr. WOODS. I do not have any experience in it, so I am afraid I am not a very good——

Senator MERKLEY. OK. Very good.

Ms. GORDON. I mean, I will be happy to speak to this. I do not think it is unique to Oregon that the folks in investor-owned communities have problems with security of land tenure and with rising costs and all sorts of other rules, like if you want to sell your unit, you cannot put up a sign, or, you know, there are all kinds of rules that are very difficult.

I think that is why you have seen a movement toward resident-owned communities, where the decisions are made with the best interest of the owner residents in mind, and that is—it is particularly important now as FHFA writes this Duty to Serve rule that they use their market power, because Fannie and Freddie both do lend in this area and should be probably doing, or finance in this area, and should be doing more of that. It is important to use that power to make sure that there are better rules of the road for investor-owned communities and for chattel lending, as well, to make it much safer.

It is very predatory. There was a discussion earlier about whether manufactured housing caused the 2008 financial crisis. But, manufactured housing has its own crises. You know, there was a statistic in a recent article that in the year 2000, 75,000 manufactured homes were repossessed and that is something of an epidemic. We would not stand for that in site-built housing.

So, this is especially not the time to be removing more protections in that area. We should be thinking about what additional

protections we can provide, because this is an important source of potentially affordable housing when it is done fairly.

Senator MERKLEY. Yes. That is what I want to emphasize—is this really is an option for so many folks who are looking for a less-expensive house, but when that dream of owning your house turns into a nightmare, and particularly many seniors located into this situation and then discover, well, your rent is going to go up $200 this year. Well, there went $40,000 of equity, now you cannot sell the house, *et cetera,* it becomes—then it does become a nightmare that really does not serve low-income Americans well. So, I just wanted to draw attention to that as we consider how we might modify the financial strategies related to this.

Mr. MOTLEY. Senator, we at the MBA think it is a very important State issue and we would like to review it and review your concerns earlier.

Senator MERKLEY. Thank you, and I look forward to working with you all. I think we all want the mortgages to be affordable but not predatory, so they become a form of wealth construction or addition in America, really part of the American dream, but not predatory wealth-stripping strategy.

Thank you.

Chairman SHELBY. Senator Scott.

Senator SCOTT. Thank you, Mr. Chairman.

Mr. Polychron, one of my experiences as a small business owner for a couple decades, it seems, maybe even a little longer in my lifetime, it appears the time with my gray hair that I had to cutoff——

[Laughter.]

Senator SCOTT. It is just not that funny, though. Anyway——

[Laughter.]

Senator SCOTT.——just a quick question for you, sir. As an insurance guy working in business, one of the things that I experienced with my couple thousand customers is most wanted customization. They wanted the ability to have a serious conversation about their set of needs and then to have a product designed for it. It appears to me that we are really heading in the exact opposite direction, where one size fits all. A case in point, the debt-to-income ratios of the 43 percent rule.

From my perspective, it just appears that, while well intended, the fact of the matter is that perhaps we are going to carve out a major segment of the population that would be creditworthy if they were able to consider more factors. The classic example from my life was when I started my business, I had to have a relationship loan from my lender, who took a chance. It appears to me, while that was a business loan experience, that allowed me or afforded me the opportunity to get a mortgage.

The fact is that we are, through this trying to synchronize and harmonize and standardize everything, we are going to eliminate those very opportunities for worthy individuals who may not fit into the cookie cutter box that we think we are building on their behalf to actually have access to loans. Has that been your experience in the field?

Mr. POLYCHRON. Well, what you did not know about me is that I was a bank president in another life, and, you know, a lot—I do not think this has been discussed enough today. We had Mr.

Cordray at a meeting with NAR earlier last year and one of the things that I kept hearing was underwriting, and I will tell you that when I was a banker, Underwriting 101 was basically the ability to repay. And, I do not think what we are doing enough of is good underwriting, and I still think that was the primary cause of the bubble. It was not necessarily some of the rules and regulations that have come forward, but truly the fact that, you are right, we need more opportunity for the millennials, *et cetera,* who are the primary borrowers, or buyers of homes right now. We have to open that up, and I think good underwriting would take care of a lot of it.

Senator SCOTT. Mr. Motley, I see you shaking your head.

Mr. MOTLEY. Senator Scott, I would like to just follow up on that, and I gave an example earlier about the restrictive one-size-fits-all nature of the 43 percent back-end ratio. It does not fit for everybody and we should not rely on it as the only source of underwriting. Instead, we need to be able to make holistic changes to the QM rule that will allow us to exercise prudent judgment in making good, sound underwriting decisions. That does not mean that we go back to the days of stated income, stated asset type loans at all. It just means that we have a little bit more flexibility to evaluate the very situation that you discussed earlier.

Senator SCOTT. It appears our rush toward the one-size-fits-all for a State like South Carolina, which so much of my State being rural areas, where manufactured homes in the rural areas, or throughout, frankly, the State of South Carolina are consistent, and yet many of the rules that we are seeing promulgated would restrict access to capital. And, when you look at the challenge of growing wealth in this Nation, there is a great disparity, primarily because of the value of the home and the value of that home ends up on a calculation on your net worth. So, from my perspective, the rural communities are being impacted negatively by the direction that we are heading.

One final question before we get to the other witnesses. It seems to me that the impact on minorities and their ability to be a part of the qualified mortgage conversation is very strong. It is as if we prevent minorities from getting mortgages because of Dodd-Frank. Then the Government comes in to bankers and says, why are you not doing more lending? And then you get penalized for that, and then the Government creates another set of rules forcing you to do something that seems to be in great contradiction to the very Dodd-Frank standards that we are setting.

Mr. Woods.

Mr. WOODS. I think your comment is right on, and I think that is one of the cases where we look at the fact that the rules or the regulations are not in—in misalignment, if you will, the fact that there are a lot of unintended consequences. The rule itself was for a good reason——

Senator SCOTT. Yes.

Mr. WOODS.——but nobody looked beyond that to start to say, yes, but it will not work in these kind of communities, or it will not work under these kinds of loans.

You know, back to the community banker, and I have a great respect for them, one of the things that the community banker has

as an advantage, if he is a true community banker—be careful, there are a lot of people calling themselves community bankers that are not, OK—the true community banker knows his community. He is involved in the school board and the Chamber and he has a reason to have his bank be successful and the community be successful, because it is going to make his bank more successful.

And there is no—and there is nothing in all of these that allows for that insight. You cannot put that insight on a loan form, where he knows the individual.

Senator SCOTT. Exactly.

Mr. WOODS. He made that relationship loan.

Senator SCOTT. Hence the relationship lending experience that I have had.

I know my time is up, Mr. Chairman.

Chairman SHELBY. Thank you, Senator Scott. That is a good point.

Senator Donnelly, you have been very, very patient.

Senator DONNELLY. Thank you, Mr. Chairman. In this seat, you have to be.

[Laughter.]

Chairman SHELBY. I have been in that seat.

[Laughter.]

Senator DONNELLY. Before he leaves, I want to mention, Mr. Scott has real world experience working in small business and trying to make markets go.

I used to serve, Mr. Woods, on a school board, which can occasionally be a challenging endeavor, as they say. But, for the State I am from, Indiana, manufactured housing is really important. It is important in a number of ways, for the people who want to live there, and then we have over the years traditionally had a great history of being one of the producers of the product. I have toured the plants. I have been with the workers, spent time with them. And, the goal is, how do we provide affordable housing to families who, you know, they are not going to be building the McMansions on the Potomac River. These are our families who work hard every day and have the same American dreams, though, that everybody else has. And, so, access to credit in a responsible way is obviously a key.

I have been a sponsor of a bill, Preserving Access to Manufactured Housing, and so the question is, how do we do this in the most responsible way, that nobody wants to open up a can of worms again. I voted for Dodd-Frank, but I voted for it to provide safety and stability, not to make it impossible for certain markets to have loans.

You know, what we have seen, or what I have seen and what I have heard from folks, they are small—you know, the companies that I deal with in my home State are usually small, family-owned enterprises that are building these homes. There has been a dry-up of small dollar loans on these kind of things.

And, so, as we look at this, Mr. Polychron, I want to ask you, could you tell us why it is important to ensure consumers have more affordable access to manufactured housing, if you would?

Mr. POLYCHRON. And I would even suggest a way maybe we get there, if that is OK.

Senator DONNELLY. That would be terrific. We have no magic answers here. We are looking for——

Mr. POLYCHRON. Arkansas, too, is a lot like Indiana, and a large percentage, especially in our rural areas, depend on manufactured housing. I think Ms. Gordon mentioned earlier, we had a symposium on credit access recently at the National Association of REALTORS®, and one of the subjects we have touched on a little bit today were different credit scoring systems, such as FICO 09, VantageScore, which take into account rents paid, utilities paid, and can actually raise a person's credit score to where they could qualify for these type loans. I think it is an area we certainly need to research more and explore.

Senator DONNELLY. Because the thing we do not want to do is we do not want to put folks in a box with a payment that cannot be made. That does not help——

Mr. POLYCHRON. Good underwriting, again.

Senator DONNELLY. It does not help any families. It does not help the home companies. So, what we are trying to do is thread the needle of, in effect, how do we do this. And, I am not willing to say, and I know the Chairman is not, that small, you know, relatively small compared to some others, you know, loans of $30,000, $40,000, that they should not be made, because those people have the same hopes and dreams, and, then, so, how do we do this in an affordable way.

Mr. Woods, do you believe Congress can have lending restrictions that make sense on this while still protecting consumers and the economy from the dangerous practices we ran into?

Mr. WOODS. I think it is possible. I think—again, I do not know that much about that piece of it, but I can——

Senator DONNELLY. Well——

Mr. WOODS.——some of the comments before. The good rules can be made. They need to be made with common sense and they need a lot of input and we need to look at all the aspects.

Senator DONNELLY. Mr. Polychron, to that same question. Do you feel this needle can be threaded so that we have regulations that make sense, that provide appropriate restrictions and also make a profit for the people who have to write the papers?

Mr. POLYCHRON. My opening comments were about balance and finding that in the middle, and I think, with enough work, we can reach that balance. Yes, sir, I do.

Mr. MOTLEY. Senator, we agree. MBA would welcome the opportunity to figure out a way to thread that needle.

Senator DONNELLY. OK. And, Ms. Gordon, I know there are certain parts of the bill that you do not support, and I understand that from your written testimony. The FHFA, the Duty to Serve rule required by the Housing and Economic Recovery Act of 2008, can you talk a little bit about how the Duty to Serve will enhance accessibility and affordability of manufactured housing.

Ms. GORDON. Well, what I hope it will do is make sure that both Fannie and Freddie have an obligation to ramp up their work in this area so that there are more ways to access safe and affordable financing for manufactured homes and for community owners that run responsible communities.

I think what is important and what FHFA can do is they can sort of set a best practices standard, if you will, to ensure that where they are putting their backstop, their guarantee, is on the type of lending that has the features that people need to be successful, you know, security of land tenure, adequate notice before rent increases, the ability to sell their unit if they need to move. You know, there is a whole variety, and I would be happy to work with your office on the list that we have provided to FHFA on this.

You know, if I could wave my magic consumer protection wand, of course, I would make most of these loans titled as real estate. But, for some reason, not everybody seems to be planning to listen to me on that, and so I think it is extremely important that we not just completely write chattel loans out of this rule, but that we use the market power that Fannie and Freddie have to establish this safer standard of those loans so that people in this situation are able to access responsible credit.

And the reason—the dispute I have with some of the provisions of the proposed legislation really just has to do with not wanting to strip consumer protections from people who may have very, very high rate loans, because those can be dangerous and can be abusive and can put families in a situation that they do not expect. But, I would be very happy to work with you and your other colleagues on ways that we can open up that credit in a responsible way.

Senator DONNELLY. Thank you very much.

Thank you, Mr. Chairman.

Chairman SHELBY. Thank you.

Senator Rounds.

Senator ROUNDS. Thank you, Mr. Chairman.

When I first purchased my home in Fort Pierre, South Dakota, it was just after I had left working as Governor for 8 years. We were told that in the area that I purchased my home, there were no comps. The bank would have to hold my loan on their books. As a result, I had to pay a higher interest rate. Now, I suspect it might also have not helped that I was now seen as not having a stable job history, having just left one job and picking up another job.

[Laughter.]

Senator ROUNDS. I have heard that same story, though, from other South Dakotans. If you live in a rural area and you do not have comps, odds are that if you can get a mortgage, you will face higher mortgage interest rates.

Another South Dakotan told me that he is also facing a similar situation. Because his loan cannot be sold into the secondary market, he is also paying a 1 to 2 percent interest rate premium for a loan with a 6-year term and a balloon payment. This is essentially a tax on living in rural America and another example of the red tape that is making it harder for people to own homes.

Another example—and I thank my colleague, Senator Heller, for his leadership on this particular issue—residents in rural communities like South Dakota that I have mentioned often use balloon payments to finance home purchases. CFPB says this type of loan is abusive, but they have made an exception for parts of the country that the CFPB defines as rural in nature.

The CFPB took two attempts, but even after their second try, the CFPB still does not define towns like Lead, South Dakota, population 3,109, or Sturgis, South Dakota, population 6,683—other than during the Sturgis Motorcycle Rally when it goes to 600,000 for a period of 2 weeks—they consider both of those as not being rural. That is thousands of people who will have severe difficulties getting a loan.

This rule makes no sense and the practical result is that if your bank has to hold a mortgage on its books and you need a balloon payment, you will not be able to get a mortgage in towns like Lead or in Sturgis.

In South Dakota, the community bankers rely on relationships and knowing their customers. Another effect of these new rules is that it does not matter how well you know your customer.

Another example is a constituent was looking to buy a home and went to a community bank where they had done business in the past. His father had passed away and he was due to inherit several thousand acres without a mortgage. Because at the moment he applied for the loan this individual's debt-to-equity ratio was not acceptable, he could not get a loan and that community bank lost his business and he had to go looking elsewhere.

We need to take a look at all of these rules, all of these regulations, and, well, and ask the question, do they make common sense?

I want to thank all of our witnesses here today. I want to ask them, aside from the fact of if you really had the opportunity to start out by eliminating the CFPB and starting over again, which rules do you think are the most egregious and which rules do you think constrain access to mortgage credit the most?

Mr. MOTLEY. I would be happy to start with that. I think that the QM rules are too prescriptive. They incorporate a one-size-fits-all debt-to-income ratio. They restrict points and fees to too great an extent and lenders need to have more flexibility to accommodate the kind of loans that you are talking about.

Senator ROUNDS. Yes.

Ms. GORDON. Well, this may not be the answer you are looking for, but I actually think that by turning the qualified mortgage definition, which was never meant to be the box that everybody had to fit in—when CFPB, at the mortgage industry's request, turned that into a safe harbor, it had the unintended consequence of having all of these loans feel like they had to fit in that box. The purpose of the Ability to Repay rule was to provide exactly the kind of flexibility that you are talking about, to know your customer, and as long as you are documenting that what the customer, in fact, is saying to you is true, that you would be able to make loans that did not at all look like that QM definition.

And, I know nobody here is asking to roll back that safe harbor. But, the answer is not to give everything a safe harbor, because then you will go back to irresponsible lending, and that might not happen in your community banks, but it will happen in other institutions that do not have those same community ties as yours do. So, that is really important.

I will add, since I did not get an opportunity to say this before, I completely agree that just the 43 percent bright line is a problem

and that compensating factors are really important. And, I will note again, when CFPB was implementing—Congress did not put that 43 percent in the Dodd-Frank statute. That was something that CFPB did when it was implementing the rule at the request of industry groups that went in and said, bright lines. We need bright lines. We cannot do this unless we have bright lines. And then they got a bunch of bright lines——

Senator ROUNDS. For fear——

Ms. GORDON.——and now folks are saying, oh, well, you know——

Senator ROUNDS. For fear of litigation.

Ms. GORDON. Well, for fear of litigation, which, by the way, I would be interested if anybody can show me any kind of onslaught of litigation under Dodd-Frank on the consumer side——

Senator ROUNDS. If I could——

Ms. GORDON.——because I have not seen that.

Senator ROUNDS.——and I know my time has expired, but, sir, would you care to——

Mr. MOTLEY. I would just point out that the safe harbor allows more security and less potential for litigation, not a rebuttal of presumption. Lenders are subjected to a defense of foreclosure, private right of action, punitive actions. It is—a safe harbor loan is far safer and it is marketable. A rebuttable presumption—there is no market for a rebuttable presumption loan in today's world. So, there is a reason that we want to have safe harbor protections, because it is a more marketable loan. It allows banks to sell that loan into the secondary market, which they cannot do right now.

Chairman SHELBY. Go ahead, Senator.

Senator ROUNDS. Thank you. I did not know whether anyone else wanted to comment on that or not, but I am over my time, but with your generous accommodation——

Chairman SHELBY. Go ahead.

Mr. POLYCHRON. The only thing I would comment on, A, about your appraisal process earlier, I concur with you 100 percent. Appraisals still cause a huge problem in our State and we would like to see that process strengthened.

I think I would still go back to credit scores. The average credit score, you know, in 2013 was over 750. Last year, it was over 740. I still think going back to using a different method of scoring, credit scores, could certainly help more than almost any other thing.

Senator ROUNDS. Thank you.

Thank you, Mr. Chairman.

Chairman SHELBY. Thank you, Senator Rounds.

Senator Heitkamp.

Senator HEITKAMP. Thank you, Mr. Chairman.

A lot has been covered, obviously, and I have been listening to this discussion of rural, and we have been able to work this through with Consumer Finance, and so we now have our definition that works, so give them a call. Maybe they will, a Governor, maybe they will work it out with you.

One of the things that I want to point out, because we have been talking a lot about manufactured housing, and we are talking about real estate versus chattel lending. The difference that is hugely important to the consumer is the nonrecourse nature of a

mortgage versus chattel lending. And, so, you could, in fact, if you overburden or put too much debt on a borrower who is financing a manufactured home, you could be indenturing them for a long time. They cannot simply walk away from that debt. In most States, they cannot. And, so, we just need to be really careful as we pursue the manufactured housing, understanding that it does not have the same kind of characterization that mortgage lending does. So, I just want to kind of put that down.

I am concerned about creditworthiness, and manufactured housing plays into this, as you have said, Chris, about that—or, I think it might have been you, Tom—that we begin with that lower level and then work up. We are looking at twin homes, condos, you know, apartment buildings, small first-time homeowner kind of operations that then move up. That is true for manufactured housing. Some of my folks live there for 50 years, but many transition out to a regular mortgage and a regular home.

Going back to credit scoring, one of the things that is happening now is in the world of big data looking at algorithms and looking at not whether you paid your bill or whether you have a bank account or, you know, what did you buy yesterday? Where do you shop? And, so, I want you to comment a little bit about this trend to try and analyze creditworthiness looking at big data and algorithms and different kinds of inputs and whether you have seen any movement in that direction or if this is a 10-year-out problem.

And, Mr. Woods, maybe start with you.

Mr. WOODS. I think it may be the 10-year-out problem. I am intrigued by that kind of data. I think it plays into, as I say, the community banker. You know, those relationship loans that were first made in many cases were made because that banker knows the granddad and the dad and the uncles and they are a hard-working family and they pay their bills and it is just built into their nature. But, that young person that walks in there certainly does not have the credit and all the other things that he would need to have a 750 credit score.

One of the other things I thought interesting that we passed over, they would allow loans at 660, but nobody is making them, you know. They are making them at 750 and above. I defend the fact that I came from some pretty humble beginnings. I would fight the fact that there are a lot of people in those lower scores that pay their bills. They pay them on time——

Senator HEITKAMP. Yes.

Mr. WOODS.——and that is their genetic——

Senator HEITKAMP. And an independent community banker who has been in that community, who has a relationship that goes way back, knows which family. I say this all the time in North Dakota. You could have a banker, a client or customer comes in and you look at the financial statement. It checks all the boxes. There is no way you are going to give them a loan. The guy who owns the body shop down the street who you know has always paid his bills, because you know his community reputation, you want to give him the loan and you do not want to be dinged for it in an examination, or you want to be able to do what you have always done in your communities, and so I do not think anyone is more sympathetic,

coming from a town of 90 people, than I am about what that means for relationship banking.

But, I am concerned about creditworthiness. We hear this over and over again, and it is not just student debt. It is depressed wages. It is the whole nine yards that challenged millennials and young people.

And, then, it is a change in consumptive behaviors. Are they really looking for those loans? Are they looking to the shared economy? And, how do we reach out to those folks, because we know that is also a way that they can build equity, that they can build a future. And, this is a big part of solving our retirement problem, as well.

And, so, we—I am going to associate myself with Senator Corker. I was on that effort last time and urge the Committee Chairman to give us another go at the great work that we did last Congress. I think it will help solve and analyze a lot of these problems.

And, so, I want to thank you all. I am going to submit some questions for the record, with the Chairman's appreciation and approval, and thank you for the work that you do in your communities and thank you for the work that you do on behalf of consumers.

Chairman SHELBY. Senator Merkley, do you have any other questions?

Senator MERKLEY. Mr. Chair, I think the points have been quite well explored and it is very important to American families, this challenge. Home ownership is just an incredibly important part of families moving into the middle class, and getting it right in a fashion which empowers families and does not prey on families is what this conversation is all about, and thank you for bringing your insights to bear.

Chairman SHELBY. I want to, on behalf of the Committee, I want to thank all of you. We have had, I think, a very good hearing, a lot of participation. We appreciate your input and your willingness to come to share, and let us try to solve some of these problems that you pointed out here.

The Committee is adjourned.

[Whereupon, at 12:07 p.m., the hearing was adjourned.]

[Prepared statements, responses to written questions, and additional material supplied for the record follow:]

PREPARED STATEMENT OF TOM WOODS

PRESIDENT, WOODS CUSTOM HOMES
ON BEHALF OF THE NATIONAL ASSOCIATION OF HOME BUILDERS

APRIL 16, 2015

Introduction

Chairman Shelby, Ranking Member Brown, and Members of the Committee, I am pleased to appear before you today on behalf of the National Association of Home Builders (NAHB) to share our views on regulatory burdens to obtaining mortgage credit. My name is Tom Woods, and I am a home builder from Blue Springs, Missouri and NAHB's 2015 Chairman of the Board. We appreciate the invitation to appear before the Committee on this important issue.

NAHB represents over 140,000 members who are involved in building single family and multifamily housing, remodeling, and other aspects of residential and light commercial construction. Each year, NAHB's builder members construct approximately 80 percent of all new housing in America.

The ability of the home building industry to meet the demand for housing, including addressing affordable housing needs, and contribute significantly to the Nation's economic growth is dependent on an efficiently operating housing finance system that provides adequate and reliable credit to home buyers and home builders at reasonable interest rates through all business conditions. At present, home buyers and builders continue to confront challenging credit conditions weighed down by a zealous regulatory response to the Great Recession. In addition, the ongoing uncertainty over the future structure of the housing finance system has intensified these challenges. This statement will examine several cases where Government regulation and other developments have impeded the ability of the housing sector to recover from the historically steep downturn and meet the credit needs of home buyers and home builders.

The housing finance system is governed by statutes and regulation overseen by a myriad of Federal agencies. In response to the recent financial crisis, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank) mandated significant mortgage finance reforms and created the Consumer Financial Protection Bureau (CFPB) to supervise and monitor many of the new requirements. Additionally, the Federal Housing Finance Agency (FHFA), the Federal Housing Administration (FHA) and the Federal banking regulators all have taken steps to ensure the U.S. economy will never again be as vulnerable to "risky" mortgage lending. The collective force of the actions taken by these agencies, along with the lingering doubts and uncertainty of market participants, has resulted in an undue restriction on the availability of mortgage credit to many creditworthy borrowers.

While there have been some actions taken by the individual agencies to mitigate the overly tight lending conditions, the housing sector is still struggling to return to normal. NAHB believes there are additional steps that can be taken to eliminate some of the barriers to credit availability and support a stronger, more robust recovery of the housing and mortgage markets while still employing balanced reforms to protect the housing market from another crisis.

Factors Constraining Availability of Mortgage Credit

While mortgage rates remain near historically low levels, access to mortgage credit is limited to home buyers and homeowners with pristine credit histories who can qualify for Government-backed programs. Presently, FHA, the Department of Veteran's Affairs (VA), Fannie Mae and Freddie Mac (the Enterprises) account for an overwhelming majority of mortgage originations.

Today's tight lending conditions are keeping more buyers on the sidelines even as the housing market strengthens. As discussed below, significant new regulations, lender credit overlays, high fees and other factors continue to impact the availability of mortgage credit. At a time when housing affordability has been at record favorable levels, more buyers should be entering the housing market. However, many creditworthy borrowers are not able to take advantage of these opportunities. As more new rules are implemented, consideration should be given to how the cumulative impact of this imposing regulatory environment will adversely affect the availability of mortgage credit and housing market and economic activity.

Regulatory Constraints

The regulatory environment for mortgage lending is undergoing significant changes as regulators implement new rules mandated by Dodd-Frank. Uncertainty about the eventual impact of these regulations and the cost of compliance are key factors in tightened access to mortgage credit.

Total loan production costs continue to escalate and NAHB is concerned about the effect of the additional regulatory cost to originate loans in today's environment, particularly for smaller banks and independent mortgage bankers. Many of these smaller originators serve rural communities, first-time home buyers and other underserved market segments. NAHB members are hearing that many smaller banks and independent mortgage bankers are choosing to depart the residential mortgage business, and in some cases, closing or merging their banks. This exodus will cause less competition and provide consumers with fewer choices.

Ability to Repay Rule

The implementation of the final Ability to Repay (ATR) standard by CFPB, which took effect on January 10, 2014, defined new lender underwriting requirements for mortgage loans and liabilities. However, the rule has created new hurdles for borrowers, especially low- to moderate-income buyers and self employed borrowers that are under increased scrutiny due to the debt-to-income calculation and more stringent documentation requirements.

The ATR rule establishes standards for complying with the ability-to-repay requirement by defining a "qualified mortgage" (QM). The QM standard is intended to balance protecting consumers from unduly risky mortgages and providing lenders more certainty about potential liability. Lending outside the QM box still is allowed, and in fact, the CFPB is encouraging lenders to make non-QM loans. Lenders, however, must balance being exposed to increased litigation risk with expanding their non-QM product offerings. To the extent that lenders will remain cautious during the transition and beyond, creditworthy borrowers may not have access to affordable mortgage credit, or may be left out of the credit box all together. According to a Fannie Mae survey released in August 2014, 80 percent of lenders said they do not plan to pursue non-QM loans or prefer to wait and see.

As required by Dodd-Frank, FHA and VA released separate QM definitions for loans insured or guaranteed by these agencies. As the HUD and VA QM definitions allow for lenders to follow current FHA and VA underwriting criteria, this has helped keep credit flowing.

The final ATR rule included a 7-year window in which loans that are eligible for purchase by Fannie Mae and Freddie Mac are considered qualified mortgages. This provision will expire in 2021, or when the conservatorships of the Enterprises end. This provision of the ATR rule also has aided the continued flow of conventional mortgage credit through this transition period. With the Enterprises still purchasing a large percentage of mortgage originations, the market may not experience the full effect of the ATR rule until 2021 or when the conservatorships of the Enterprises has ended.

Since issuing the final ATR rule, the CFPB has made several amendments to the rule to address the practical implementation of the rule. Most recently, CFPB proposed beneficial amendments relating to small creditors and rural underserved areas.

An area that continues to be of concern to NAHB is how the final ATR rule requires lenders to calculate the 3 percent cap on points and fees. The final ATR rule includes closing charges paid to affiliated settlement service providers in the 3 percent cap on points and fees, while the points and fees charged by unaffiliated companies are not included. NAHB strongly objects to this disparity and has urged CFPB to exclude points and fees paid to affiliated firms when calculating the limit. Many home builders and lenders have established settlement service affiliates such as mortgage and title companies to facilitate home purchases for consumers. Requiring affiliate fees and points to be included in the 3 percent cap creates disincentives to establish these beneficial relationships. Affiliated and non-affiliated settlement services should be treated equally. NAHB adamantly believes that fees and points from affiliated firms should be excluded in the 3 percent cap, thereby giving equal treatment to affiliated and non-affiliated settlement service providers. We strongly urge the CFPB to implement such an exclusion.

H.R. 685, the *Mortgage Choice Act,* introduced in February, and passed by the House on April, 14, 2015, would amend the Truth-in-Lending regulation to clarify the final QM rule's definition of points and fees. The specific adjustments provided in the bill would clarify that title insurance charges by a title insurance provider affiliated with the lender and a homeowner's escrowed insurance premiums do not count toward the 3 percent cap on the points and fees limit for a QM loan. The bill is intended to help more sound loans pass the QM test and ensure that consumers can choose the lender and title provider best suited to their needs.

Representative Andy Barr (R–KY) recently introduced H.R. 1210, the *Portfolio Lending and Mortgage Access Act.* The legislation is intended to ease the ATR requirements for community lenders who may be fearful to originate non-QM loans

and, therefore, may limit access to credit for home buyers in their communities they believe to be creditworthy. This bill would amend the Truth-in-Lending regulation to provide that a loan satisfies the ATR requirement if the loan remains in the originating lender's portfolio. Banking regulators would be required to treat such a loan as a QM, if the lender has, since the loan's origination, held it on its balance sheet and all prepayment penalties with respect to the loan comply with specified limitations.

NAHB believes the concepts behind each of these bills have merit and should be passed by both the House and Senate as methods to ease the components of the ATR rule with the most potential to restrict mortgage credit.

Qualified Residential Mortgages

The implementation of the Credit Risk Retention rule, also mandated by Dodd-Frank, was finalized in 2014 and aligns the definition of a qualified residential mortgage (QRM) with the QM. Though the rule is not effective until December 2015, NAHB believes aligning the QRM with the QM has many benefits. Establishing one streamlined regulation, instead of having two separate sets of underwriting criteria, will alleviate confusion in the marketplace and will help provide clarity and transparency for home buyers, lenders, investors and other housing market participants. Aligning QRM with QM levels the playing field, promotes liquidity in the mortgage market and allows access to credit for a diverse range of home buyers, particularly first-time and low- to moderate-income home buyers. Additionally, the underwriting criteria and product limitations contained in the QM will promote more prudent lending and will provide investors with an assurance that the loans are sustainable.

Integrated Mortgage Disclosures under the Real Estate Settlement Procedures Act and the Truth in Lending Act Proposal—"Know before you owe"

In December 2013, the CFPB finalized new mortgage disclosure forms that are intended to help consumers make informed decisions when shopping for a mortgage and avoid costly surprises at the closing table. The new forms will become effective August 1, 2015. The rule applies to most closed-end mortgages but does not apply to home-equity lines of credit, reverse mortgages or mortgages not attached to real property. The rule also does not apply to loans made by a creditor who makes five or fewer mortgages in a year.

For over 30 years, Federal law has required lenders to provide consumers with a Good Faith Estimate of closing costs and a Truth-in-Lending disclosure of the loan's annual percentage rate, total finance charges and total loan payments within 3 days of applying for a mortgage loan. The law also required the two different forms to be re-disclosed shortly before closing on the loan. The information on these forms was determined to be overlapping and the language inconsistent. As directed by Dodd-Frank, the CFPB updated and integrated the forms based on extensive consumer and industry research.

The new combined forms are called the "Loan Estimate" which is provided at application and the "Closing Disclosure" which must be provided at least three business days before the consumer closes on the loan. Any change to the information provided on the form that is made during that 3-day period will restart the 3-day waiting period (with limited exceptions). NAHB and other housing industry stakeholders are concerned with the practical outcome of transitioning to the new forms, particularly that there is no opportunity under this regulation to comply early, which means that industry will not be able to test systems, in real-time, in real circumstances, until after August 1. NAHB joined with other industry groups and recently wrote CFPB Director Cordray to encourage the agency to announce and implement a "restrained enforcement and liability" or "grace period" for those seeking to comply in good faith with the provision after August 1 through the end of 2015.

NAHB members depend on the certainty of a smooth closing process and NAHB is concerned that any confusion related to the new rules, compounded by the fear of aggressive enforcement activities, will negatively impact the ability to close on a home in a timely manner.

Lender Credit Overlays and Buy Back Risk

Lender overlays in the mortgage credit process have been a major factor in the greater difficulty potential home buyers are having in obtaining financing as lenders impose credit underwriting standards that are more restrictive than those required by FHA, VA, Fannie Mae and Freddie Mac. These credit overlays are employed due to heightened lender concerns over forced loan buy-backs on mortgages sold to Fannie Mae and Freddie Mac and/or greater required indemnifications on FHA-insured and VA-guaranteed loans.

When lenders sell loans to entities, such as Fannie Mae and Freddie Mac, and through the FHA/VA/Ginnie Mae securities process, they are required to make as-

surances that they have performed the appropriate level of due diligence on the loan application, and the lenders agree to buy back a loan if it is discovered that they were at fault in their underwriting process. These representations and warranties ("reps and warrants") have been a standard practice in mortgage lending.

In the aftermath of the collapse in the housing market, the underwriting of delinquent loans was alleged not to have met the established criteria of FHA, the Enterprises, and other secondary market entities. As a result, lenders have faced a protracted struggle with these agencies about the buy back of loans that have been deemed ineligible for Enterprise guarantees or Government insurance based on the finding of faulty due diligence practices. Lenders complain that the criteria triggering buy-back demands by Fannie Mae and Freddie Mac and insurance claims rejections by FHA and VA are unclear and inconsistent. The resulting uncertainty has caused lenders to employ underwriting standards that are more restrictive than those required by FHA, VA, Fannie Mae and Freddie Mac. These lender "overlays" have closed the credit window to many aspiring home buyers who actually meet the loan qualification requirements established for these programs.

The recent sharp increase in borrower credit scores since 2001 is an indication of how lenders have responded to concerns about how the Federal agencies will implement repurchases and indemnifications. A recent report from the Urban Institute (UI)[1] found that credit has become much less available to borrowers with lower credit scores. From 2001 to 2013, the share of new purchase borrowers with FICO credit scores below 660 declined from 28 percent to 11 percent; those with FICO scores between 660 and 720 remained at 28 percent of the total. Meanwhile the share of borrowers with FICOs above 720 increased from 44 percent to 62 percent of the total. The UI report estimates that as many as 1.25 million fewer mortgage purchases were made in 2013 than would have been made had credit availability been the same as in 2001. For 2009–13, UI estimates that 4 million more loans would have been made based on 2001 credit standards.

The weighted average credit score for loans purchased by Fannie Mae and Freddie Mac in 2014 was 744, while in fact, both Fannie Mae and Freddie Mac have a minimum credit score requirement of 620 for most purchased mortgage loans.

FHA will insure mortgage loans with credit scores as low as 500 under certain scenarios. However, according to the 2013 State of the Nation's Housing Report,[2] in 2007, borrowers with credit scores below 620 accounted for 45 percent of FHA loans. By the end of 2012, that share was under 5 percent.

Similar trends are evidenced in the share of first-time home buyers which accounted for only 28 percent of home sales in February 2015, well below the historical average of about 40 percent. In the new home market, NAHB survey data indicate the current share of first-time buyers is only 16 percent compared to an historic average of 30 percent.

In 2014, the Enterprises' regulator, FHFA, and FHA announced efforts to clarify and, in some cases, ease, the reps and warrants and identification of loan defects that will trigger enforcement actions against lenders. NAHB anticipates positive results from these modifications and is hopeful to see lenders originating to the underwriting specifications of the agencies rather than implementing their own, more strict, standards.

Alternative Credit Scores

It is possible that the use of alternative credit scores could offer lending opportunities to borrowers currently lacking access to mortgage credit due to a low or inaccurate FICO credit score. Fannie Mae and Freddie Mac have been directed by FHFA to assess the feasibility of using alternative credit score models in their automated loan-decision models. The Enterprises are planning to study the costs and benefits associated with VantageScore 3.0 and FICO Score 9.

To generate a traditional credit score, a borrower must have one trade line that is at least 6 months old, with a balance on it. Fair Isaac Credit Services, Inc. estimates that 50 million U.S. consumers have credit histories that do not meet that requirement. These potential borrowers are disproportionately Hispanic (24 percent), African American (14.6 percent), and recent immigrants. However, it is estimated these 50 million people have a history of paying regular bills such as rent, utilities, insurance, and telecommunications.

FICO Score 9's primary enhancement is its separation of medical debt collection from other unresolved debts. As a result, Fair Isaac estimates that a consumer with

[1] *The Impact of Tight Credit Standards on 2009–13 Lending. http://www.urban.org/research/publication/impact-tight-credit-standards-2009-13-lending.*

[2] The State of the Nation's Housing 2013. *www.jchs.harvard.edu/sites/jchs.harvard.edu/files/son2013.pdf.*

the median credit score of 711 whose only negative collection issue is medical-related will see his or her credit score increase by 25 points. FICO also recently announced a new credit score based on a consumer's payment history with telecommunications and utility bills. The new score could help applicants who don't use credit often but are responsible with other monthly payments.

VantageScore 3.0 claims the ability to calculate a score for 30 to 35 million previously *"unscoreable,"* or "thin file," consumers. VantageScore requires just 1 month of credit history and less frequent updates than the current FICO score used by the Enterprises. Credit scores can now be made available to consumers who are brand new to credit, those who only use credit occasionally and people who have not used credit at all recently. The VantageScore 3.0 credit score also ignores all paid collections, as well as any collections, paid or unpaid, under $250.

HUD Secretary Castro also has stated that FHA is exploring the use of new credit scoring models that use nontraditional factors, such as rent and utility payments, to determine creditworthiness. The potential use of alternative credit scoring models by FHA and the Enterprises could help to open the credit box.

Fees

Fees for Government-backed mortgages continue to be at an increased level, even though the credit quality of the underlying loans has increased significantly, as evidenced by the high FICO scores referenced earlier. These higher fees are usually passed on to consumers, making it more expensive for borrowers to obtain a home loan or, in some cases, even preventing them from qualifying for a loan.

In the wake of the housing downturn, FHA steadily and significantly increased its upfront and annual mortgage insurance premiums (MIP). The annual MIP on a typical 30-year FHA loan (LTV less than 95 percent and loan amount below $625,500) was raised six times in 5 years and had reached 130 basis points by April 2013 compared to 50 basis points in April 2010. Further, FHA also terminated the policy that allowed borrowers to stop paying mortgage insurance premiums after their loan reaches 78 percent of its original value. As a result, the cost of an FHA loan over the life of the loan had become higher than that of a conventional loan with private mortgage insurance, which borrowers can stop paying when the LTV reaches 78 percent of original value.

NAHB strongly supports FHA's announcement in January that, effective with case numbers dated on and after January 26, 2015, it would reduce its annual upfront MIP by 50 basis points to 80 basis points on FHA loans with LTVs less than 95 percent and loan amounts of $625,500 and below.

At the direction of the FHFA, Fannie Mae and Freddie Mac have been increasing their guarantee fees (g-fees) that are charged to lenders to protect against credit-related losses. G-fees charged by Fannie Mae averaged 62.9 basis points on new single-family originations in Q4 2014. This is a significant increase over 2012 in which the average was 39.9 basis points.

In addition to the g-fees, Fannie Mae and Freddie Mac continue to charge adverse market fees and loan level pricing adjustments. Fannie Mae and Freddie Mac have charged a 25 basis point adverse market fee since March 2008 for whole loans and mortgage loans delivered into MBS. The loan level price adjustments, which have been charged since 2009, add delivery fees to mortgages purchased by the Enterprises. The delivery fees which vary based on credit score and loan-to-value ratio range from 25 to 325 basis points. This translates into a 6 to 80 basis point increase in mortgage financing costs.

In June 2014, FHFA requested input on setting the g-fees. NAHB's comments to FHFA opposed a further increase in g-fees and urged that affordability should be a significant consideration in setting g-fees. NAHB's comments also included a recommendation for the Enterprises to eliminate the upfront adverse market charge and loan level price adjustments. Current market conditions in which defaults and foreclosures are declining and housing markets nationwide are improving have rendered these charges obsolete.

Though FHFA still is in the process of reviewing and considering comments received on the g-fee request for input, NAHB is hopeful that Director Watt will make an announcement soon that will provide for lower fees to lenders and, ultimately, home buyers.

Downpayments

In an acknowledgement that high downpayments are a significant impediment to some borrowers, especially first-time home buyers, last October FHFA Director Mel Watt directed the Enterprises to begin purchasing 3 percent downpayment mortgages from creditworthy borrowers. Fannie Mae began purchasing 97 percent LTV mortgages in December and Freddie Mac's purchase program began in March.

NAHB agrees with Director Watt's assessment that 3-percent downpayment mortgages can be made safely by imposing strict credit and underwriting standards that ensure borrowers have strong credit and meet income, asset and employment requirements. Also, a recent Urban Institute analysis found that the default rates on 3 to 5 percent downpayment loans and 5 to 10 percent downpayment loans purchased by the Enterprises are similar.[3]

Appraisals

The housing recovery also has been impeded by ongoing problems in the U.S. residential appraisal system. While lenders, Federal banking regulators and federally related housing agencies implemented corrective measures in response to valuation breakdowns that came to light in the wake of the Great Recession, and Congress mandated additional measures in the Dodd-Frank Act, these steps did not address fundamental flaws and shortcomings of the U.S. residential appraisal framework. Improper appraisal practices, a shortage of experienced appraisers and inadequate oversight of the appraisal system continue to restrict the flow of mortgage credit and retard the housing recovery. NAHB is not advocating that appraisals should be higher than the real market. Rather, our goal is to establish an appraisal system that produces accurate values through all phases of the housing cycle.

The principal focus of reforms to-date has been on eliminating undue influence on appraisers to produce inflated valuations that facilitate transactions. However, when home prices began declining, improper appraisal practices exacerbated the slide in values. Some appraisers used distressed sales—many of which involved properties that were neglected and in poor physical condition—as comparables in assessing the value of brand new homes, without accounting for major differences in condition and quality. Without such adjustments, the two housing types are not comparable. The inappropriate manner in which distressed sales were utilized distorted home valuations. Use of the cost and income approaches in conjunction with the comparable sales approach could mitigate such distortions.

The dramatic increase in the use of Appraisal Management Companies (AMCs) is another factor contributing to inaccurate appraisals. Some AMCs have reduced appraiser compensation, which has led to more activity by appraisers with less training and experience, and shortened turnaround times for valuations to as little as 48 hours. These changes have had a significant adverse effect on appraisal quality.

Other challenges facing the appraisal industry include shortcomings in appraiser training and experience in dealing with new construction and green building. Additionally there is insufficient new construction, energy efficient and green building data available to appraisers and current valuation practices do not provide a process for expedited appeals of inaccurate or faulty appraisals. Oversight of appraiser qualifications and appraisal practices falls to the individual states, and many jurisdictions have inadequate resources to adequately perform this function. In some states, fees collected for appraiser licensing and certification are swept into a general fund and are not utilized in appraisal/appraiser oversight and enforcement.

NAHB has been a leading advocate for correcting the valuation process and has undertaken a number of actions to raise awareness and address the adverse impacts inaccurate appraisals are having on the housing sector. NAHB has conducted five Appraisal Summits to provide opportunities for the agencies and organizations that establish appraisal standards and guidelines to join housing stakeholders in a constructive dialog on major appraisal topics of concern.

Through the Appraisal Summits and feedback from builders and others in the field, NAHB has identified the following key areas of focus to improve current appraisal requirements and practices, which are presented in a white paper entitled *A Comprehensive Blueprint for Residential Appraisal Reform,* which contains the following recommendations:

Strengthen Education, Training and Experience Requirements for Appraisers of New Home Construction, including:

- The establishment of greater education, training and experience requirements for those who are assigned appraisals of new construction to ensure that lot values and building costs, including those for energy efficient, green building and other evolving new construction techniques and mortgage products, are fully considered in valuation of new home construction.

[3] Urban Institute, *Why the GSEs' Support of Low-Downpayment Loans Again is No Big Deal. http://www.urban.org/urban-wire/why-government-sponsored-enterprises-support-low-down-payment-loans-again-no-big-deal.*

- The incorporation of the qualifications for appraisers of new construction into appraisal regulations and guidelines of the bank regulatory agencies, Fannie Mae, Freddie Mac, FHA, VA, and USDA.

Improve the Quantity and Quality of Data for New Construction through:

- Establishment of an appraisal database system for new construction.
- Standardization of loan level valuation data by Fannie Mae, Freddie Mac, FHA, VA and
- USDA in their Uniform Appraisal Dataset (UAD).
- Expansion of the UAD to include new construction, energy efficient and green building data standards. Develop New Appraisal Standards and Best Practices for Conducting Appraisals in Distressed Markets by:
- Modifying current appraisal practices and procedures to consider all three approaches to value—cost, income and sales comparison—in appraisals of residential properties to mitigate distortions and volatility.
- Giving greater weight in distressed markets to alternative means of valuation, such as the cost-based approach to value.
- Revising banking agency guidelines to require the appraisal entities used by financial institutions to avoid the use of distressed sales as comparables for new construction sales and, if distressed sales are the only comparables available, to make adjustments to accurately reflect possible condition and stigma issues associated with distressed properties.

Develop Processes for Expedited Appeals of Inaccurate or Faulty Appraisals through:

- Federal agency adoption of an appeals structure similar in design to that of the Department of Veterans Affairs Loan Guaranty Service Home Loan Program.
- The establishment of more efficient, timely and effective processes for State and local appraisal oversight.
- The establishment of a timely value dispute resolution process that is fair, balanced and appropriate to allow interested parties to appeal appraisal values when appraisal techniques and/or assumptions are incorrect.

Strengthen Oversight of Appraisal Activities through:

- Streamlining and coordinating the current regulatory framework to devote adequate resources and ensure effective oversight and enforcement.
- Full implementation of appraisal mandates in recent Federal legislation addressing:
  - Appraisal independence
  - Customary and reasonable fees
  - Mandatory reporting of appraisal standards violations
  - Strengthening of State appraisal oversight and enforcement of regulations
  - Dispute resolution
- Establishment of best practices for effective and consistent appraisal practices, policies and procedures.

NAHB stands ready to work with appraisal, housing and financial stakeholders to address the real challenges we face in restoring the public trust in how we build, transfer, value and finance the American consumer's most valuable asset. Solving these issues, in the short and long term, is a critical step toward establishing an efficient and sustainable housing finance system.

Regulatory Constraints to Housing Production Credit

Despite signs of improvement in recent months, many home builders continue to deal with a significant adverse shift in terms and availability of land acquisition, land development and home construction (AD&C) loans. Lenders are reluctant to extend new AD&C credit citing regulatory requirements or examiner pressure on banks to shrink their AD&C loan portfolios as reasons for their actions. While Federal bank regulators maintain that they are not encouraging institutions to stop making loans or to indiscriminately shrink their portfolios, reports from NAHB members in a number of different geographies continue to suggest that bank examiners in the field are maintaining a more aggressive posture.

According to data from the FDIC and NAHB analysis, the outstanding stock of 1–4 unit residential AD&C loans made by FDIC-insured institutions to residential

construction businesses rose by $1.158 billion during the fourth quarter of 2014, a quarterly increase of 2.32 percent. On a year-over-year basis, the stock of residential AD&C loans is up 17 percent from the final quarter of 2013. Despite these gains, AD&C lending remains much reduced from years past.

The current stock of existing residential AD&C loans of $51.2 billion now stands 74.9 percent lower than the peak level of AD&C lending of $203.8 billion reached during the first quarter of 2008. However, the count of single-family homes under construction is down only 33 percent from the first quarter of 2008 compared to today. Thus, there exists a lending gap between home building demand and available credit. This gap is being made up with other sources of capital, including equity, investments from non-FDIC insured institutions and lending from other private sources, which may in some cases offer less favorable terms for home builders than traditional AD&C loans.

Concentrations in Commercial Real Estate Lending

In general, the Federal banking regulators have been reminding financial institutions to adhere to the December 2006 bank regulatory guidance Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices issued by the Office of the Comptroller of the Currency (OCC); the Board of Governors of the Federal Reserve System (Federal Reserve); and the Federal Deposit Insurance Corporation (FDIC) (collectively "the Agencies") in which the Agencies specified criteria they would review to determine when a bank was exposed to potential CRE concentration risk. A financial institution is considered to have a high CRE concentration, and thus subject to the Guidance, if it exceeds or is rapidly approaching the following thresholds:

- If loans for construction, land development, and other land loans equal 100 percent or more of total capital, the institution would be considered to have a CRE concentration and should have heightened risk management practices.
- If loans for construction, land development, and other land loans secured by multifamily and non farm nonresidential property (excluding loans secured by owner-occupied properties) equal 300 percent or more of total capital, the institution would be considered to have a CRE concentration and should employ heightened risk management practices.

The guidance emphasized that the 100 percent and 300 percent thresholds are not to be considered as limits or caps on bank CRE lending but rather are intended as guidelines for banks and their examiners in determining appropriate loan underwriting and review systems, risk management practices and levels of reserves and capital.

NAHB continues to raise awareness in Congress about the lack of AD&C financing and the possible adverse economic impacts of this situation.

Basel III

In mid-2013, the U.S. Federal banking agencies approved a new regulatory capital regime for all federally insured banking institutions. Referred to as Basel III, the new requirements increase the quantity and quality of capital for all federally insured banking institutions and will impose additional capital thresholds for the largest banking organizations. Basel III was effective for the largest banks beginning January 2014; compliance for community banks was mandatory beginning January 2015.

Basel III revised the definition of High Volatility Commercial Real Estate (HVCRE) and required HVCRE financings to be risk-weighted at 150 percent up from 100 percent. AD&C loans considered HVCRE financings which generally will include commercial real estate projects with an LTV greater than 80 percent and borrower-contributed capital of less than 15 percent of the project's "as completed" value.

HVCRE loans do not include:

(1) One-to-four residential property; or
(2) Commercial real estate projects that meet certain prudential criteria, including with respect to the LTV ratio and capital contributions or expense contributions of the borrower.

The new HVCRE capital requirement is affecting the ability of community banks to provide financing for AD&C loans using traditional methods and will impede the ability of banks to make high quality AD&C loans to builders and developers. As AD&C lending finally begins to recover, NAHB is extremely concerned that this rule introduces a significant new impediment to further improvement.

Cost of Regulation

NAHB appreciates the Committee's focus on regulatory activities that are adversely impacting the housing credit availability. Along with the challenges faced by home buyers and home builders in securing financing, regulatory burdens impose costs on the development of land and the construction/remodeling of homes, both multifamily and single-family, that are passed along to home buyers/homeowners and renters through higher costs for housing, both in terms of prices and rents. New regulations are being developed that impact all aspects of home building. For instance, the housing and construction industry is actively engaged with OSHA, EPA, FEMA and other agencies on new regulations which could drive up the cost of housing further.

NAHB survey data of builders has demonstrated that, on average, regulation imposed during development accounts for 16.4 percent of the price of a home built for sale; regulation imposed during construction accounts for 8.6 percent of the price. Thus, in total, 25 percent of the price of an average single-family home built for sale is attributable to regulation imposed by all units of government at various points along the development/construction process. Most of these burdens are associated with permitting, land use, and construction codes, however, other financial burdens impose costs on the construction process and contribute to an increased cost of housing.

In turn, higher housing costs "price out" households from home ownership. For example, according to 2014 estimates from NAHB, on a national basis, a $1,000 increase in home prices leads to pricing out just slightly more than 206,000 individuals from a home purchase. The size of this impact does vary widely across States and metro areas, depending on population, income distributions and new home prices.

Housing is an important source of economic growth and job creation; and regulations are limiting home builders' ability to grow and contribute positively to the economy. As of the final quarter of 2014, housing's share of gross domestic product (GDP) was 15.2 percent, with home building yielding 3.1 percentage points of that total. Historically, residential investment has averaged roughly 5 percent of GDP while housing services have averaged between 12 percent and 13 percent, for a combined 17 percent to 18 percent of GDP. While these shares tend to vary over the business cycle, clearly housing is an important factor in a healthy economy. Job creation is one of the important ways that housing contributes to GDP. NAHB estimates that building an average new single family home creates 3.05 jobs; building an average new multifamily rental unit creates 1.16 jobs; and every $100,000 spent on residential remodeling creates 1.11 jobs. Therefore, the cost and availability of credit for builders and home buyers has a direct impact on the ability of housing to contribute to economic growth.

All of these issues must be factored into the cost of housing. As the cost of housing increases and the credit box remains tight, home buyers and renters will have fewer safe, decent and affordable housing options.

Conclusion

NAHB supports steps to ensure that mortgage lending occurs in a safe and sound manner, with appropriate underwriting, prudent risk management and sound consumer safeguards and disclosure. NAHB continues to advocate for comprehensive mortgage finance system reform. While we believe regulatory barriers can be alleviated to some degree by the various regulators of the system as well as by specific legislative reforms, comprehensive legislation would ensure that components of reform are not in contradiction, but will work together to offer the hoped-for result; minimum disruptions to the mortgage markets while ensuring consumer protections.

PREPARED STATEMENT OF CHRIS POLYCHRON

2015 PRESIDENT, NATIONAL ASSOCIATION OF REALTORS®

APRIL 16, 2015

INTRODUCTION

Thank you for the opportunity to testify today. My name is Chris Polychron. I am the 2015 President of the National Association of REALTORS® (NAR). A REALTOR® for 27 years, I am an executive broker with 1st Choice Realty in Hot Springs, specializing in residential and commercial brokerage.

While we have seen great progress in our economic recovery, access to affordable mortgage credit remains a problematic obstacle for prospective home buyers. The

number of first-time buyers entering the market is at the lowest point since 1987, despite historically low mortgage rates. The Nation's home ownership rate has fallen almost to levels last seen in 1990. Today, the number of homes purchased annually remains less than 70 percent of what was purchased prior to the real estate bubble and subsequent collapse.

Credit remains tight as lenders remain leery of taking on risk. NAR has long supported strong underwriting standards that require all mortgage originators to verify the borrower's ability to repay the loan based on all its terms, including taxes and insurance. However, there remain some unnecessary regulatory burdens that are preventing qualified, credit-worthy borrowers from obtaining the American dream of home ownership. These fall into four specific areas:

- Consumer Financial Protection Bureau Issues
- Specialty Markets Challenges
- Short Sales and Foreclosure Matters
- Lending Policies

CONSUMER FINANCIAL PROTECTION BUREAU (CFPB) ISSUES

NAR appreciates the CFPB's approach in proposing regulations that recognize the balance between access to credit and responsible lending. We support regulations such as the Qualified Mortgage (QM) rule to ensure that borrowers can repay their mortgage. We generally believe that these rules have created certainty in the mortgage market and have encouraged increased mortgage liquidity and availability, while ensuring consumers are afforded necessary protections. However, we believe there are certain changes that can be made to existing rules that will promote a safe, but more robust housing market.

3 PERCENT CAP ON POINTS & FEES NEEDS TO BE FIXED

This year, the U.S. House Financial Services Committee passed H.R. 685, "The Mortgage Choice Act." This bill is identical to legislation that passed the House last year. This legislation is a bipartisan compromise that reduces discrimination against mortgage firms with affiliates in the calculation of fees and points in the Dodd-Frank Ability to Repay/Qualified Mortgage rule. The QM rule sets the standard for mortgages by providing significant compliance certainty to QM loans that do not have risky features and meet certain requirements. A key requirement is that points and fees for a QM may not exceed 3 percent of the loan amount. The inherent discrimination in this rule arises from the fact that under current law and rules, what constitutes a "fee" or a "point" varies greatly depending upon who is making the loan and what arrangements are made by consumers to obtain closing services. As a result of these definitions, many loan originators affiliated with other settlement service providers are not be able to make QM loans to a significant segment of otherwise qualified borrowers.

The discrimination in the calculation of fees and points is being felt by consumers who are seeing reduced choices and added obstacles in their transactions. A Spring 2014 NAR survey of affiliated mortgage lenders revealed almost half experienced problems due to the ATR/QM rule. When the 3 percent cap was cited as the cause, a significant number had certain services outsourced or were not able to complete the transaction. Where services were outsourced and charges known to the lender, nearly half of loans (43.8 percent) included higher fees. NAR strongly urges the Senate to introduce companion legislation and work to pass the bill this year.

RESPA/TILA REFORM MUST BE ENFORCED SLOWLY

On August 1, 2015, significant Real Estate Settlement Procedures Act (RESPA) and Truth in Lending (TILA) changes go into effect during the busiest transaction time of the year. There will no longer be a Good Faith Estimate (GFEs) or Truth in Lending disclosures. Those two forms have been combined into a single "Loan Estimate" or "LE." While NAR is supportive of this harmonization, there will be unanticipated problems and issues uncovered in the implementation. NAR, as well as other industry groups, have urged CFPB to provide for a restrained enforcement period on the RESPA–TILA integration regulation, and have asked them to clarify TILA and RESPA liabilities under the regulation.

COMMUNITY BANK LENDING SHOULD BE ENCOURAGED

Ensuring community banks can continue to maintain good relationships and provide mortgage credit to their customers without being overloaded with regulations intended for more complex financial institutions is an important goal.

NAR supports strong underwriting standards and believes that all mortgage originators should act in "good faith and with fair dealings" in a mortgage transaction and treat all parties honestly. This idea is at the core of community banks which

base their reputations on a relationship-lending model. These standards had been the basis for offering mortgage credit for decades until the mid-2000s which saw a proliferation of lenders offering mortgage products that were unstainable for most borrowers.

In May 2005, NAR adopted principles that warned that consumers were being taken advantage of by intemperate, and often predatory, lending. We acknowledged then too that, in a credit-driven economy, the legislative and regulatory response to lending abuses could go too far and inadvertently limit the availability of reasonable credit for borrowers. Unfortunately, this restriction of credit was exactly what the market experienced. As a result of lenders and regulators over-correcting in response to the abuses in the middle of the previous decade, NAR called on the credit and lending communities and Federal regulators to reassess the entire credit structure and look for ways to increase the availability of credit to qualified borrowers who are good credit risks.

Noting the importance of both of these principles, NAR supported the balance that the January 2013 mortgage rules achieved including strong consumer protections, the promotion of mortgage liquidity, and important ability-to-repay standards. One compliance option allows the creditor to make a reasonable and good faith determination that the borrower has a reasonable ability to repay the loan and related obligations, based on verified and documented information based on all its terms, including taxes and insurance.

The CFPB's proposed amendments recognize that community banks have a long history of this common sense approach to underwriting and that the relationship-lending model is one that should be maintained. Of course, any exception to the general rule must be limited and not become the general rule; moderating regulatory burdens for small lenders needs to be balanced with maintaining principles of strong underwriting based on a borrower's ability-to-repay.

SPECIALTY MARKETS SHOULD HAVE SPECIAL CONSIDERATION

As stated, we believe that exceptions to the CFPB rules must be made on a very limited and specific basis. Certain markets may warrant that type of consideration. Rural communities and manufactured housing loans fall into this category.

RURAL COMMUNITIES

Rural citizens face unique challenges finding access to credit. Almost 20 percent of the U.S. population lives in rural areas or small towns and nearly all of the counties with the highest poverty rates in America are rural. NAR recognizes the uniqueness of rural communities and the key role that housing plays in building strong communities. REALTORS® who live in and serve these communities also understand the need for specialized programs to meet the needs of Americans living in rural areas.

The CFPB has updated its own definition of a rural community for lending policies. NAR supports the recent changes they have made, but also believe communities should be able to petition the CFPB to be considered rural. To this end, NAR supports S. 871, the "Helping Expand Lending Practices in (HELP) Rural Communities Act", introduced by Majority Leader McConnell (R–KY), along with Senators Heller (R–NV), Capito (R–WV) and Paul (R–KY). This bill will allow communities to apply for a designation as a rural community. There are a number of factors to be considered when determining if a community warrants a rural designation—and some factors commonly used can be misleading. For example, the population determined by the census is a common tool used to determine a communities' rural nature. But institutions like prisons and colleges can distort the actual population of a community. This legislation does not require the CFPB to grant a rural designation, but simply allows communities to apply for reconsideration.

The Association also support changes to the process by which loans are approved under the Rural Housing Service (RHS) of the Department of Agriculture. Today, every RHS loan must be reviewed and approved by staff of the Rural Housing Service. In recent years, RHS staffing has been dramatically reduced, and borrowers have experienced significant delays in loan approval. Both the Veterans Affairs loan guaranty and the FHA mortgage insurance program utilize private lenders for direct endorsement. Providing RHS with the authority to approve direct endorsed lenders would create great efficiencies for the Service and for home buyers. RHS, in turn, would have additional staff time needed to focus on a strengthened lender monitoring process and risk management. NAR strongly urges Congress to provide RHS with direct endorsement authority to ease burdens on the agency and accelerate loan processing for borrowers.

MANUFACTURED HOUSING LOANS

Nearly 20 million Americans live in manufactured homes. These homes are often a more accessible and affordable way for many people to buy their own home. Manufactured housing has come a long way with respect to the features and quality of life it provides homeowners. Today, manufactured homes blend seamlessly into many markets or neighborhoods. In many areas of the country, particularly rural communities, manufactured homes are the only type of quality affordable housing available.

The Dodd-Frank Act regulations have mistakenly resulted in manufactured homes becoming less available as an affordable housing option. We support S. 682, the "Preserving Access to Manufactured Housing Act", introduced by Senators Donnelly (D–IN), Toomey (R–PA), Manchin (D–WV), and Cotton (R–AR). This legislation will preserve manufactured housing as an affordable housing option without reducing important consumer protections.

S. 682 clarifies the difference between manufactured housing manufacturers and loan originators, and ensures that low-dollar manufactured housing loans are exempt from Home Ownership and Equity Protection Act (HOEPA) standards. The costs of originating and servicing a manufactured loan are not much different than those of a more traditionally built home, even though the loan itself is often much smaller. Therefore, the closing costs of a manufactured loan as a percentage of the loan are much higher than the percentage on a more expensive home. This can cause manufactured housing loans to violate caps in Dodd-Frank and be categorized as "High-Cost," or predatory. S. 682 will exempt manufactured loans from this label.

FORECLOSURES AND SHORT SALES REMAIN PROBLEMATIC

Too often, short sales are still a story of delay and unrealistic views of current home values, resulting in the potential buyer canceling the contract and the property going into foreclosure. Enormous amounts of time are spent on potential short sales that ultimately result in foreclosures. Even if successful, the process usually takes many months and countless hours and often requires re-marketing because buyers lose patience and terminate the contract.

CERTAINTY IS NEEDED TO MAKE THE SYSTEM WORK

NAR believes that the short sale process would significantly improve with the passage of S. 361, "The Prompt Notification of Short Sale Act," introduced by Senators Brown (D–OH) and Murkowski (R–AK) last year. This legislation requires servicers to decide whether to approve a short sale within 30 days of completion of the file. The bill attempts to prod servicers to make the short sales process more efficient by setting standards and penalizing them for inadequate performance. Streamlining short sales will reduce the amount of time it takes to sell the property, improve the likelihood the transaction will close, and reduce the number of foreclosures. This will benefit the lender, the seller, the buyer, the community.

TAXPAYERS NEED RELIEF

Today, more than 5 million families remain in a home that is "under water." While Congress provided relief in recent years, uncertainty exists for these homeowners today. For many of these homeowners, a short sale or workout is the most viable option. However, the income tax exemption on mortgage debt forgiven in a short sale or a workout for principal residences was extended late last year retroactively, but expired at the end of 2014. Not having this relief, many families will simply walk away and accept a foreclosure on their home. This is contrary to the goal of every policy designed to keep people in their homes and prevent foreclosures.

Unless remedied, homeowners who participate in a workout or short sale will have to pay tax on "phantom income" from forgiven debt. This is not only unfair but harms families, neighborhoods and communities. NAR urges all Members to extend this provision of the tax code. Without this provision, distressed homeowners will decide to take a pass on opportunities for workouts with the lender or short sales, opting instead for continued delinquency or possible default until foreclosure, or simply to walk away from the property. This will destabilize the communities where such homes are located.

LENDING POLICIES CONTINUE TO CONSTRAIN ACCESS TO CREDIT

Loan pricing and lending restrictions also are making it more difficult for creditworthy borrowers to purchase a home. We believe that these types of rules should be directly commensurate with actual risk. Borrowers should not be subject to higher fees or burdens that are unnecessary.

CONDO RESTRICTIONS PREVENTING HOMEOWNERSHIP OPPORTUNITIES

Condominiums often represent the most affordable options for first-time home buyers, including minorities. However, the Federal Housing Administration (FHA) and the Government-Sponsored Enterprises (GSEs) have significant restrictions on the purchase of condominiums. However, NAR supports developing policies that will give current homeowners and potential buyers of condos access to more flexible and affordable financing opportunities as well as a wider choice of approved condo developments. Specifically, we have five areas of concern.

1. Owner Occupancy—FHA requires that a condominium property be at least 50 percent owner occupied. FHA's ratio greatly limits the number of condominium buildings available to credit-worthy borrowers. This policy is also self-fulfilling. If a building has less than the 50 percent owner-occupancy ratio, sellers of units have fewer buyers who are eligible, leading them to rent out their unit rather than sell. This makes it difficult for many buildings to achieve the 50 percent requirement. By way of contrast, the GSEs do not place limits on the owner-occupancy of a condominium project if the borrower is buying it as a primary residence. NAR strongly urges FHA to eliminate this requirement to open up more properties for FHA-eligible buyers.
2. Project Approval Process—FHA requires the entire condominium project to be approved prior to a buyer purchasing a unit. This certification process is costly and time-consuming, and difficult for the often volunteer boards of condominium buildings. Less than 20 percent of all condominium properties nationwide have FHA approval.[1] NAR strongly urges FHA to reduce the burdens associated with project certification. NAR also recommends that the spot loan approval process be reinstated to allow purchases in some buildings that do not have FHA certification.
3. Delinquent Dues—Following the housing crisis, a number of condominium and homeowner associations have units that are behind in paying their dues. Both FHA and the GSEs restrict approval of properties where more than 15 percent of the units have delinquent dues. While NAR appreciates the need to make sure properties are properly capitalized with appropriate reserves; dues payment should not be a sole determinant. Some associations may have compensated for delinquencies by building reserves or taking other steps to ensure that delinquencies are not impacting their financial stability. This requirement should NOT be a determining factor, but instead be a part of an overall review of a property's finances.
4. Commercial Space—Multi-use properties and new "town center" developments are very popular, and lauded by HUD as creating benefits for communities in providing easy access to amenities and transportation. Yet, condominium associations with commercial space are restricted from approval by both the GSEs and FHA. The GSEs limit commercial space to 20 percent, but provide waivers. FHA's limit is 25 percent, also with allowable waivers. The current policy hinders efforts to build neighborhoods that have a mix of residential housing and businesses with access to public transit. The Association urges FHA and the GSEs to lift these restrictions.
5. Transfer Fees—FHA has a policy that prohibits FHA mortgage insurance on any property that has a transfer fee covenant. Fees that increase the costs of housing can disenfranchise those who wish to obtain the American dream; however, fees that provide a direct benefit to homeowners and improve the property are legitimate and should be permitted. The blanket policy used by FHA can greatly disadvantage the millions of homeowners living in community associations, making it much harder for them to sell their homes. FHFA has previously dealt with this issue, following a thoughtful and lengthy rulemaking. FHFA's final rule on transfer fee covenants establishes a clear, national standard to protect homeowners from equity-stripping private transfer fees while preserving the preeminence of State and local governments over land use standards.

FHA should accept a mortgagee's compliance with FHFA's transfer fee covenant regulation as compliance with relevant FHA mortgage insurance program rules, guidelines and requirements. Any additional and potentially conflicting Federal standard on transfer fee covenants by FHA will cause confusion in the housing market and require community associations to amend governing documents. Amend-

[1] Based on estimates derived from FHA's condo lookup tool as of 2/24/15.

ments to community association covenants, conditions, and restrictions can be difficult to execute and by statute generally require legal counsel and the approval of at least a supermajority of owners. We urge FHA to mirror FHFA's rule, and prohibit only those fees that don't benefit the homeowner and association where they live.

There are additional concerns related to condo rules including investor ownership, concentration limits, and pre-sale requirements that also should be changed. REALTORS® were pleased to see a recent notice by Fannie Mae, loosening some restrictions. We look forward to the publishing of FHA's upcoming condo rule and are hopeful that it will loosen many of the current restrictions.

Condominium unit mortgages are among the strongest performing in the FHA portfolio. According to FHA data from 2014, the national serious delinquency rate for condominium projects is 0.89 percent versus 1.17 for single-family homes.[2] Condominiums are often the most affordable option for first-time home buyers, or older homeowners who wish to downsize. We strongly believe that qualified home buyers should not be prevented from this option, simply due to mortgage restrictions.

HIGH G–FEES STILL HURTING CONSUMERS

High guarantee fees (g-fees) and loan level pricing adjustments (LLPAs) charged by the GSEs are negatively impacting the housing recovery. These Enterprises buy single-family mortgages from mortgage companies, commercial banks, credit unions, and other financial institutions. A key revenue component for the GSEs is a g-fee received for guaranteeing the payment of principal and interest on their mortgage backed securities (MBS). The g-fee is a significant factor in determining profits earned from this credit guarantee. The g-fee covers projected credit losses from borrower defaults over the life of the loans, administrative costs, and a return on capital.

Continued increases in g-fees and upfront borrower costs will extend a trend of reduced access to mortgage credit, which is counter to a principal duty of the FHFA Director under the Housing and Economic Recovery Act of 2008 (HERA). Continuing to increase the fee will mean that larger numbers of consumers, many of them first-time home buyers, will be forced to pay substantially higher mortgage rates, or be left with limited housing finance options. NAR believes borrowers who are either purchasing a home or refinancing their existing mortgage using conventional financing are being charged excessive fees due to policy goals that go beyond protecting taxpayers from GSE losses.

NAR is especially concerned with the disparate impact the changes will have on first-time home buyers and other traditionally underserved borrowers. These families are more likely to bear the brunt of these fees, either because they have thin credit files and traditional credit models do not reflect payments toward housing expenses and utilities; or because they often make smaller down payments than do other borrowers.

FHFA seems to believe that by raising costs for loans purchased or guaranteed by the GSEs, they can lure private sector capital back to the mortgage market. However, we believe this policy does not account for the aversion to, and lack of trust in, issuers of private mortgage backed securities that many investors still harbor since suffering tremendous losses during the recent housing crisis. This lack of trust remains and is hard to quantify. When increasing fees, the GSEs must include performance measures to ensure they are meeting the goal of increasing private sector participation. In addition, the Agency should examine other factors that are holding back the private market in conjunction with the Treasury Department. The National Association of REALTORS® believes that future data will show that the effect of raising fees will simply be increased costs to home buying taxpayers who can afford to become homeowners, and that the true effect will be redirection of more mortgage loans to FHA without a robust private sector return.

CONCLUSION

The Urban Institute recently reported that "If credit standards had been similar to those of 2001, more than 4 million additional loans would have been made between 2009 and 2013. The missing loans grew from 500,000 in 2009 to 1.25 million in 2013."[3] While we generally support recent regulations such as QM, policies still exist that unnecessarily constrain lending to credit-worthy borrowers. While no one

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[2] Serious Delinquent Rates, Retrieved April 13, 2015, from Neighborhood Watch, Early Warning System. *https://entp.hud.gov/sfnw/public/*.

[3] *http://blog.metrotrends.org/2015/04/million-mortgage-loans-missing-2009-2013-due-tight-credit-standards/?utm_source=iContact&utm_medium=email&utm_campaign=Housing%20Finance%20Policy%20Center&utm_content=HFPC+newsletter+4%2F8%2F2015.*

wants to see a return to the unscrupulous, predatory lending practices that caused the Great Recession, some modifications of existing regulations may be necessary to ensure a robust housing market.

Adjustments to rules issued by the CFPB including 3 percent cap on points and fees, enactment of RESPA/TILA harmonization, and encouraging responsible community bank lending will help provide consumers with valuable protections and safe access to affordable credit. Small market areas such as rural and manufactured housing must also be provided with flexibility appropriate to their market conditions. Americans who continue to struggle with underwater mortgages or mortgages they simply cannot afford should be provide protections and given certainty so they can make decisions appropriate for their families. Last, loans must be priced to reflect actual risk, and unnecessary restrictions must be removed to allow families to achieve the American Dream of home ownership.

Thank you for allowing me to share the view of the National Association of REALTORS®, and we look forward to working with you.

Statement of J. David Motley
President of Banking and Mortgage Operations
Colonial Savings, F.A.

On behalf of the
Mortgage Bankers Association

Before
The U.S. Senate Committee on Banking, Housing, & Urban Affairs

"Regulatory Burdens to Obtaining Mortgage Credit"

April 16, 2015

1919 M STREET NW, 5TH FLOOR • WASHINGTON, DC 20036 • MBA.ORG • (202) 557-2700

Chairman Shelby, Ranking Member Brown and members of the committee, my name is David Motley and I appreciate the opportunity to testify before this committee today on the topic at hand, one of critical importance to consumers.

I currently serve as President of Colonial Savings, F.A., a community bank headquartered in Fort Worth, Texas. I also serve as a member of the Board of Governors of the Mortgage Bankers Association (MBA), and have twice served as Chairman of MBA's Residential Board of Governors. Currently, I serve on the Community Bank Advisory Council for the Consumer Financial Protection Bureau (CFPB).

The Mortgage Bankers Association (MBA)[1] uniquely represents mortgage lenders of all sizes and business models: from small independent mortgage bankers, community banks, and credit unions to the nation's largest financial institutions. All of MBA's members have their own unique role in serving the mortgage financing needs of families across the country.

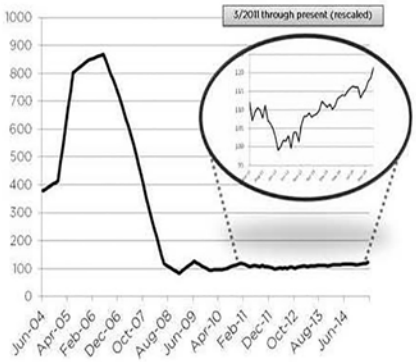
Similarly, my community bank, Colonial Savings, serves consumers in all 50 states, originating $1.7 billion in mortgages in 2014 through retail branches for both the bank's portfolio and for sale to the secondary market, and buying loans from smaller institutions that no longer maintain the capacity or desire to engage in mortgage banking themselves. Colonial today services more than $24 billion in single-family mortgages.

As a four-decade veteran of the mortgage banking industry, I can tell you that the regulatory demands under the Dodd-Frank Wall Street Reform and Consumer Protection Act and other statutes have made the market safer. I can also tell you that the industry is more focused on regulatory compliance than ever before. However, the new regulatory regime is also quite costly and many aspects of the Dodd Frank rules have an unnecessarily detrimental effect on the availability and affordability of mortgage credit for too many creditworthy families.

MBA data show that mortgage credit availability remains far below the levels seen prior to the mortgage crisis. Although credit has begun to loosen somewhat in recent months, particularly for jumbo borrowers, many borrowers continue to have difficulty qualifying for credit, or would pay much more for credit than was true before the crisis. No one would advocate going back to the weak credit standards that contributed to the boom

[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,200 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, REITs, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mba.org.

and bust. However, the pendulum has swung too far, and credit standards could safely be changed to enable loans to additional qualified borrowers.



MBA has consistently supported reasonable requirements that will prevent a reemergence of any past excesses. While we believe that the Consumer Financial Protection Bureau ("CFPB" or "the Bureau") did commendable work in developing the Ability to Repay (ATR) rule including the Qualified Mortgage definition, we also believe the ATR rule, and other aspects of Dodd Frank, warrant strong oversight and adjustment when they unnecessarily raise costs or limit access for creditworthy consumers. We believe such changes must be made judiciously to retain appropriate consumer protections while ensuring access to safe sustainable mortgage credit in a competitive market.

As explained here, we believe other changes to the Bureau's operations and requirements beyond the Bureau's purview also are warranted to facilitate the availability of credit.

I. ATR and QM Background

The ATR rule requires lenders to determine that a borrower has a reasonable ability to repay a mortgage before the loan is consummated. Dodd-Frank and this rule establish significant penalties and liability for failing to meet this requirement. The ATR rule provides a presumption of compliance with its requirements for loans that are originated as Qualified Mortgages (QMs), which provides greater certainty to lenders and mortgage investors regarding potential liability should a loan later default.

In order for a mortgage loan to qualify as a QM it cannot contain higher-risk features such as negative amortization or interest-only periods, and the sources of repayment must be fully documented. A QM must also meet specified underwriting standards including that the borrower's debt-to-income (DTI) ratio must not exceed 43 percent or,

in the alternative, the loan must be eligible for Fannie Mae and Freddie Mac (the GSEs) purchase or Federal Housing Administration (FHA) or other government programs. This alternative is commonly referred to as the "QM patch." In today's market the patch is essential since it offers and weighs a broader array of relevant underwriting factors than the alternative 43 DTI approach. However, the patch effectively hides the full impact of the QM rule by making all agency loans qualified mortgages.

Further, for loans to qualify as QM, borrowers also may not be charged points and fees that exceed three percent of the loan amount for loans in excess of $101,953 (in 2015). Loans below that amount are permitted to have fees in excess of three percent, based on a sliding scale; the lower the loan amount below the $101,953 threshold, the greater the points and fees permitted.

The rule establishes a compliance "safe harbor" for QMs if the Annual Percentage Rate (APR) of the loan does not exceed the average prime offer rate (APOR) for that mortgage by 150 basis points (bps) or more and the loan meets the other QM requirements. A safe harbor is a well-tested means of ensuring compliance with legal requirements. In that model, regulated entities are provided specific requirements and if they meet them, they are assured that any legal inquiry will be concerned only with whether the requirements were in fact met.

Loans to borrowers whose APRs exceed the APOR by more than 150 bps are not offered a safe harbor and instead receive a rebuttable presumption of compliance if their loans otherwise qualify as QMs. The level of additional risk under this standard versus the safe harbor has not yet been tested in litigation under Dodd-Frank.

Considering the significant potential liability and litigation expenses for an ATR violation, QM safe harbor loans currently comprise nearly all of the mortgage loans available in today's market. Few lenders are making either non-QM loans or rebuttable presumption QMs loans.

Moreover, the secondary market for non-QM loans remains extremely limited, and rate sheets from non-QM investors indicate a substantial risk premium exists for these loans. To date, affordable non-QM loans have generally been available only to higher wealth borrowers with broad financial relationships with institutions.

The CFPB recently proposed to amend its mortgage rules to facilitate lending by small and rural lenders by expanding the number of small creditors who receive QM status for loans held in their own portfolios when a consumer's DTI ratio exceeds 43 percent. Also, under the proposal an increased number of small creditors in rural or underserved areas would be able to originate QMs with balloon payments, even though loans with balloon payments are generally not permitted to qualify as QM loans.

II. Recommended Changes to QM

A. Framework for QM Changes

MBA believes it is time to consider changes in the QM definition to mitigate the adverse impact the initial rule has had on access to credit for some borrowers. We strongly believe these changes should be made holistically to the QM definition, and not limited to certain lenders based on charter types or business model. Consumers should not be forced to discern which institutions offer particular types of loans; their choices should not be limited to particular providers. Stratification of the market by establishing different underwriting standards for some lenders and not others only causes unnecessary consumer confusion and will lessen competition. A holistic approach to revising the QM will ensure a competitive market for all types of QM loans, and does not shift the burden to the consumer to figure out which lenders offer which QM products.

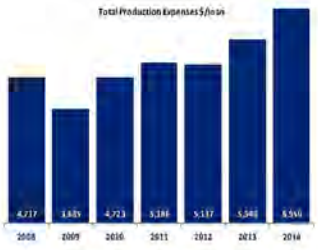
B. Expand the QM Safe Harbor

Because of certain flaws in the definition of the Average Prime Offer Rate, the calculation is biased low as a measure of the typical prime mortgage in the market. In addition, the rate is pegged only weekly and therefore lags the market. In a volatile interest rate environment where interest rates can move up 50 basis points or more in few days, the 150 basis spread over the APOR may inadvertently knock many borrowers out of the QM safe harbor. MBA recommends that the spread over the APOR for defining a safe harbor QM be expanded to 200 basis points. This step alone would broaden the availability of credit by extending safe, sustainable QM loans to a greater number of creditworthy borrowers, particularly in a rising interest rate environment.

C. Increase the Small Loan Definition

The current definition of a smaller loan under the ATR rule — where points and fees may exceed three percent and still qualify as a QM — is set at $101,953 for 2015. This definition is far too limited considering the costs of originating a loan.

Origination Production Costs – Also Up



Moreover, the average loan size today is approximately $260,000. Because of the current definition, too many smaller loans do not qualify as QMs. MBA recommends that the Bureau raise the definition to loans under $200,000, with a sliding scale that permits progressively higher points and fees caps for smaller loans. This change – which MBA would assert the Bureau has the authority to make by rule – would do much to serve the credit needs of low- and moderate-income borrowers who have smaller loan balances.

2015 QM Points and Fees Caps		Recommended QM Points and Fees Caps	
Loan Amount	Points and Fees Cap	Loan Amount	Points and Fees Cap
		$200,000 and up	3%
		$150,000 to $199,999	$6,000
$101,953 and up	3%	$100,000 to $149,000	4%
$61,172 to $101,952	$3,059	$80,000 to $99,999	$4,000
$20,391 to $61,171	5%	$20,391 to $79,999	5%
$12,744 to $20,390	$1,020	$12,744 to $20,390	$1,020
Less than $12,744	8%	Less than $12,744	8%
		New tiers/caps	

D. Broaden Right to Cure for DTI and other technical errors

MBA strongly advocated for an amendment to the QM rule to permit the cure or correction of errors where the three percent points and fees limit is inadvertently exceeded. We appreciate that the Bureau made this important amendment; such a change helped ameliorate any understandable conservatism that limits credit availability to borrowers. To encourage lending to the full extent of the QM credit box, MBA also urges that the right to cure or correct inadvertent errors be extended to DTI miscalculations and typographical and technical errors and omissions.

E. Revise the "Points and Fees" Definition

MBA strongly supports the passage of legislation that would exclude title insurance fees paid to lender-affiliated companies from the calculation of "points and fees" under QM. Currently, the CFPB's ATR/QM rule points and fees calculation includes fees paid to lender-affiliated settlement service providers — but not to unaffiliated settlement service providers. Many MBA members use affiliated settlement service providers to deliver a more reliable consumer experience. This is particularly important as we transition to the new integrated TILA-RESPA disclosures where lenders are held accountable to meet narrow fee tolerances and tight disclosure timeframes. Furthermore, title insurance premiums are regulated in most states and the premium is the same whether or not the title company is an affiliate of the lender.

MBA believes that the rule should not discriminate against lenders that use affiliated settlement providers. Requiring that the affiliate's title premium be included in lender origination charges, but not those of non-affiliated title companies does a disservice to the consumer as well as lenders with affiliate providers. Such discrimination works to lessen choice and decrease competition for consumers. Most importantly, for many lenders it makes low balance loans serving low- and moderate-income borrowers much costlier to originate and consequently less available to consumers.

F. QM for Portfolio Loans

While we prefer a holistic fix for QM, certain aspects of the QM could be modified to recognize the alignment of lender-borrower interests in portfolio lending. MBA could support proposals for QM treatment of loans that do not meet the 43 percent DTI limit, and for certain balloon loans if they are held in portfolio for three years. The fact that a loan is to be held in portfolio can be an important check against originating unsustainable loans. However, we believe some of the other parameters of the QM should be retained for portfolio loans to protect against the re-emergence of loans with risky features such as pay option ARMs, stated-income underwriting, and short-term balloon terms.

Importantly, MBA also believes that the portfolio exemptions from the QM should be extended to originators that process, fund and sell these loans to a bank (or REIT) that

will retain the loans in portfolio for the required holding period. This could be particularly important for many community banks that are finding the costs and compliance burdens of maintaining a mortgage origination operation to be excessively burdensome, but wish to offer the portfolio products to their customers.

MBA believes that independent mortgage bankers who specialize and excel in mortgage origination should be permitted to originate portfolio QMs for sale to community banks. The community banks would maintain control over the credit and underwriting standards, and would retain the ability to enforce these standards through repurchase requirements should a loan not meet the required parameters. This approach expands the availability of portfolio QMs for community banks that cannot sustain the high costs of maintaining an origination platform in today's high compliance cost environment.

G. Long-term Work on QM: Replace the Patch and the Default QM

Unlike the 43 DTI test and the cumbersome guidelines set forth in Appendix Q, the QM patch provides compensating factors to better qualify consumers for affordable credit. While the QM patch is an essential feature of the ATR/QM rule at this time, it is intended to expire after seven years or when the GSEs leave conservatorship. Considering the importance of an alternative to the DTI formulation, MBA urges the CFPB to begin a process of working with stakeholders to develop a transparent set of criteria, including the use of compensating factors, to define a QM, replacing both the patch and the 43 percent DTI standard. Such a standard must provide workable, flexible underwriting standards that are consistent with Dodd-Frank but do not inject undue complexity or uncertainty into the process of serving consumers credit needs. A simpler approach would be to classify all loans for which the lender has determined the borrower's ability to repay as qualified mortgages.

III. Other Impediments to Credit Access for Consumers

In addition to changes to the ATR/QM rule, there are several other areas which we believe should be addressed to facilitate access to credit.

A. Need for Authoritative Written Guidance Accompanying Rules

Notwithstanding the Bureau's preeminent role in consumer regulation, the Bureau has, with limited exceptions, followed a policy of only offering authoritative guidance in the form of formal rules and commentary. Most other guidance in the form of webinars, handbooks or other oral statements is prefaced with the caveat that only formal commentary and rules can be relied upon. While MBA believes that rules and commentary with an opportunity for public comment must remain the primary means of implementing the myriad laws for which the Bureau is responsible, the agency's reluctance to also offer authoritative written guidance – through FAQs or supervisory memoranda -- as questions arise has made lenders excessively cautious and defensive in their approach to lending.

The final RESPA/TILA rule, comprising 1,888 pages, was issued on November 20, 2013, with an implementation date of August 1, 2015. The rule requires new, integrated disclosure forms to be provided to consumers at the time of mortgage application and settlement, known as the Loan Estimate and the Closing Disclosure, respectively. Most importantly, the rule brings major changes not just in the mortgage process, but also in the real estate transaction process. Under the new rule, both lenders and assignees face significant liability for failures to comply.

While the Bureau has produced several webinars and helpful issuances, and participated in a numerous conferences and forums, many questions regarding this uniquely detailed and complex rule have arisen and remain unanswered, and many more questions can be counted on before August 1. Notwithstanding, the Bureau has steadfastly refused to offer timely, accessible Frequently Asked Questions (FAQs) or other authoritative guidance to regulated entities as other regulators do, except for on a handful of technical amendments and commentary to address a small set of issues. The absence of timely, authoritative written guidance from CFPB has resulted in confusion and has complicated the implementation process. Most importantly, the lack of such guidance in some areas threatens to make borrower beneficial features of transactions such as lender credits toward closing costs far more difficult to sustain.

Considering the extensive liability that can arise from TILA violations, there is considerable concern that the new disclosures will open lenders to new liability. The CFPB has taken the position that the question of the nature of liability under the rule will be settled by the courts. In the meantime, however, such uncertainty can be expected to spawn litigation and ultimately increase costs for consumers.

Because of the lack of guidance on key issues and the need to review and amend parts of the rule, we have urged that the Bureau establish a reasonable grace period for enforcement and liability during the first six months of the rule's implementation. Such action would facilitate the provision of needed guidance, compliance in good faith and allow any impediments to implementation to be addressed.

B. <u>The Bureau Should Issue Guidance Prior to Enforcement</u>

Since the Bureau was established it has moved forcefully to enforce the laws it is charged with and publicly announced numerous and costly settlements. While MBA does not question the appropriateness of these efforts, we are concerned about an over-reliance on enforcement actions to drive industry compliance with the Bureau's new rules. Instead of issuing supervisory guidance, many of the Bureau's positions have been articulated through settlements rather than through guidance or rules. This approach – particularly regarding difficult and often subjective areas such as RESPA or unfair, deceptive, or abusive acts or practices (UDAAP) actions – opens up activities not previously believed prohibited to potential challenge by state regulators, plaintiffs' attorneys, as well as the government.

Most importantly, while both enforcement and clear rules of the road protect consumers, offering guidance upfront casts a wider net and protects borrowers against harm before it occurs by ensuring the compliance of the vast majority of lenders that want to comply. With no public rulemaking or supervisory guidance, even industry counsel becomes hesitant to provide lenders with reliable compliance advice. In this environment, fear of enforcement too frequently becomes the dominant driver of lender behavior, discouraging even meritorious interpretations of the rules to serve borrowers.

MBA supports Bureau or, if necessary, Congressional action to develop an appropriate framework for the issuance of rules, policies and supervisory guidance. This would include issuing Supervisory Memoranda or Compliance Bulletins to put industry on notice regarding supervisory expectations on specific problematic practices, along with suggested compliance practices. This is especially important in connection with CFPB's UDAAP authority. Such action will ensure that access to credit for consumers will not be harmed by unnecessary confusion or fear.

C. Improvements Needed in CFPB Consumer Education Initiatives

While MBA appreciates the Bureau's work to create several valuable education resources to improve consumers' choices, its recently posted "rate checker" tool and its recently announced policy to begin posting unverified consumer narratives to its complaint database threaten to mislead consumers, undermining the Bureau's other efforts.

The Rate Checker

In January of this year, the Bureau posted on its website a "rate checker" tool so borrowers could determine the interest rate for a mortgage loan in the state where the property is located. The tool was posted without any notice and opportunity to comment and notably does not include loan costs in its calculations.

Online rate checkers or trackers are inherently problematic because they tend to simplify markets and the collateral, borrower, and other factors that determine interest rates. The CFPB's rate checker is no different but raises even a greater risk of borrower confusion because it comes with the imprimatur of a government agency.

Although, the CFPB has made some minor revisions to the tool, significant problems remain, including:

- a flawed sampling methodology, which excludes independent mortgage bankers and community banks that today account for about 50 percent of the market for home purchases;
- a lack of specific data on discount points or origination fees associated with quoted rates;
- the failure to collect key data on the occupancy, property type (single family/condo), and use of proceeds (refi or purchase)

- the absence of an APR disclosure required in lender rate advertisements;
- exclusion of certain products such as the 20-year mortgage and the 5/5 ARM;
- lack of data collected about the borrower's income; and
- the absence of estimates made about a borrower's monthly principal and income payments.

Complaint Database

Similar problems are presented by the CFPB's recently announced decision to expand its consumer complaint database to include unsubstantiated consumer narratives to accompany complaints about lenders. Because the vast majority of consumer complaints lodged through the Bureau's complaints portal do not require remedial action, MBA urged in its comment on this change that CPFB narrow its postings to include only those narratives where the accuracy of the complaint has been verified. MBA also urged the Bureau to treat this undertaking as necessitating rulemaking so that the effects on small business and the economy were appropriately taken into account. The CFPB moved forward nonetheless and the final policy makes no provision for ensuring that complaint narratives are valid or accurate. Moreover, the database does not allow financial institutions to provide a detailed response; instead, companies are limited to a single selection from a drop down menu. Nor is there any process for removing complaints that are inaccurate or resolved with a simple explanation.

Like the "rate checker," rather than ensuring consumers are provided accurate information, the CFPB has chosen to put the Government's imprimatur on information that can mislead consumers and result in ill-informed choices. MBA has urged Bureau to reconsider these recent "consumer education" initiatives that are doing more to confuse than enlighten American consumers. With the rate checker and the posting of unsubstantiated narratives, the Government provides information that is incomplete, undermining borrowers' choices at a time when the mortgage industry has never been safer or more transparent.

IV. Other Barriers to an Efficient Housing Finance Market

A. <u>SAFE Act Disparities</u>

MBA has long supported the establishment of a sound qualification framework for all mortgage originators serving consumers, regardless of where they work. Unfortunately, while the Secure and Fair Enforcement for Mortgage Licensing (SAFE) Act seeks that objective, in its current form the Act does not provide consumers the necessary assurance that all Mortgage Loan Officers (MLOs) have met minimum standards of competency through an objective test.

The SAFE Act requires MLOs employed by non-bank lenders to be licensed, pass a comprehensive test, undergo criminal and financial background reviews, and register in the National Mortgage Licensing System and Registry. By contrast, under SAFE, MLOs employed by federally-insured depositories or their affiliates are registered in the NMLS

but do not have to pass an objective test administered by a third party. Although most banks, including Colonial Savings, employ extensive training curriculums, a testing requirement would provide consumers assurance that their LO meets minimum standards of competency and knowledge. In addition, the different standards under the SAFE Act makes it difficult for MLOs to transition efficiently between employers of different charter types.

MBA urges Congress to amend the SAFE Act to require states to issue transitional licenses to individuals who are registered loan originators employed by a depository institution (or an affiliate). Similarly, a state-licensed loan originator in one state who takes a similar position in another state would have a transitional grace period to obtain a license in the new state. These individuals would be able to continue originating loans for a transitional period after being employed by a state-licensed non-depository entity willing to take responsibility for their activities during the transitional period.

In the long term, it is important to move toward a universal testing requirement that creates a level playing field for all MLOs. In the interim, this narrow and simple solution creating transitional licenses would allow all qualified individuals to satisfy borrowers' credit needs and maximize consumer choice while ensuring workforce mobility.

B. FHFA Should Direct the GSEs to Use Updated Credit Scoring Models

Another impediment to consumer access to credit is the use of outdated credit scoring models by the GSEs. The major consumer credit score model developers have announced changes to their credit scoring models with an eye toward making those models more accurate for today's borrowers in light of lifestyle changes and the post-recessionary risk environment. While the GSEs, in consultation with industry, have begun the process of analyzing and incorporating these new models, the continued required use of the outdated models harms today's borrowers. Among many factors, outdated credit scoring models may not accurately reflect the credit-worthiness of a borrower; for instance, medical debt and rent payment histories may not be given proper weight. The new models help to score borrowers with limited credit experience, i.e. "thin files".

MBA believes that the Federal Housing Finance Agency (FHFA) should expedite the GSEs' validation and adoption of the latest validated credit scoring models. Furthermore, the GSEs' delay in including the new scoring models into their automated underwriting systems may also cause lenders to hesitate to use them in their other lending products, as it could be viewed as an unfair practice to use different scoring models for different products.

C. New Regulations Have Driven Up the Cost to Service Loans

New servicing rules have dramatically driven up the cost to service loans and driven down efficiency in servicing operations. On the efficiency front, loans serviced per full-time equivalent employees have decreased from 1,638 in 2008 to 790 in 2014. Total

cost to service loans has increased from $173 per loan in 2008 to $309 in 2014. Direct costs have increased from $55 per loan to $170 per loan during the same timeframe. Costs to service loans in default have risen from $423 per loan in 2008 to $2,214 in 2014. These additional costs ultimately get passed through to consumers on new loans. Likewise, these costs directly impact consumer access because defaulted loans cost so much more to service, and lenders reduce their exposure to lower FICO borrowers as a result.

D. Basel III Limits Banks' Involvement in Mortgage Finance

The U.S. bank regulators put in place the Basel III framework in recent years. Basel III reduces a bank's potential investment in mortgage servicing assets from 50 percent of Tier 1 capital to 10 percent of the common equity component of Tier 1 capital before they must be deducted directly from capital. Regulators also raised the risk-weighting of mortgage servicing rights from 100 percent to 250 percent. Thus banks that are close to these limits will be forced to sell the servicing on incremental mortgage production, making new mortgage production less attractive. That is why MBA would support bicameral efforts to move legislation that would mandate a study into the impact of

Basel III on mortgage servicing assets owned by community banks and credit unions (a bipartisan bill, H.R. 1408 has already been introduced in the House). A moderation of Basel III's treatment of mortgage servicing assets would allow these smaller institutions to maintain responsible credit access for consumers, i.e., selling the loan asset to replenish lendable funds, while still maintaining the loan servicing relationship with the consumer.

V. Conclusion

We commend the efforts of the committee to examine the regulatory hurdles preventing consumers from accessing credit. No matter how well-intentioned they may be, we are concerned that key federal rules and practices are unduly restricting credit opportunities for qualified borrowers.

We look forward to working closely with this committee and with regulatory policymakers to improve the availability of sound mortgage credit for American families.

Center for American Progress

Regulatory Obstacles to Mortgage Credit

Testimony before the Senate Committee on Banking, Housing, and Urban Affairs

By Julia Gordon
Senior Director of Housing and Consumer Finance
Center for American Progress
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Good morning, Chairman Shelby, Ranking Member Brown, and members of the committee. My name is Julia Gordon, and I direct the Housing and Consumer Finance team at the Center for American Progress, a nonpartisan think tank dedicated to improving the lives of Americans through progressive ideas and action. Thank you so much for convening this hearing on the critical topic of access to mortgage credit.

Historically, the housing sector has led recoveries following economic downturns. Recovery from the Great Recession, however, has played out differently – in significant part because unlike most downturns, this recession was triggered by the housing sector itself. Driven by a highly leveraged, largely unregulated superstructure in the private capital markets, risky and abusive mortgages replaced previously stable, well-underwritten, long-term, fixed rate products and created a precipitous asset bubble. This system was driven by misaligned incentives up and down the securitization chain and abetted by regulators asleep at the wheel. Predictably,[1] as soon as housing prices started to level off, these new loans began to fail *en masse*, causing failures throughout the private securitization market that ultimately threatened the global financial system and required the largest taxpayer bailout in America's history.

Fallout from the mortgage crisis has been extensive throughout the system and continues to hamstring the housing market. Foreclosures due to toxic mortgage products damaged the real economy, spiking unemployment and causing massive home price declines, the combination of which then triggered a new wave of foreclosures even on homes with properly underwritten mortgages. Tens of millions of families suffered job loss, foreclosure, or other financial insecurity, in many cases ending up with damaged credit and ravaged savings and retirement accounts. Much of the American public lost confidence in the financial system, especially banks and mortgage lenders.

On the business side, hundreds of banks and mortgage companies failed,[2] and those that survived pulled back from the mortgage business or limited their lending to households with very high credit scores and ample wealth. Today, access to credit is tighter than it was pre-housing boom, mortgage

volumes are down precipitously, homeownership shares have fallen to their lowest level in two decades, and rental costs are soaring relative to incomes. Many neighborhoods have not yet turned around and continue to struggle with foreclosures, vacant homes, and blight, especially communities of color.

In the wake of the crisis, Congress and the American public supported comprehensive financial reform legislation to help realign incentives and strengthen oversight to prevent future crashes of this nature and size. That legislation, the Dodd-Frank Act, addressed a slew of issues, including but not limited to new rules of the road for the mortgage market, and also established a new independent regulator, the Consumer Financial Protection Bureau. This legislation makes it extremely unlikely that we will once again see a proliferation of the dangerous, poorly underwritten mortgages that led us to this pass.

Yet today, just a few years after the crisis, the mortgage industry has returned to Congress to ask for a rollback of these crucial financial reforms. Lenders blame Dodd-Frank for tight access to credit, and they promise that if only Congress would undo financial reform, the doors would swing open. The problem, however, is that this route to opening the doors would open them to the same pernicious, predatory practices that brought the economy to its knees less than seven years ago. Above all, removing these reforms would undermine the most critical component of recovery, which is to restore public trust in the system.

The truth is that there are likely many reasons for tight lending practices. The same voices asking for regulatory rollbacks have previously told both Congress and regulatory agencies that access to credit will open if a variety of other factors are addressed: aggressive buyback policies and steep risk-based pricing pursued by Fannie Mae and Freddie Mac in the wake of the crisis; FHA's insufficiently nuanced "Compare Ratio"; the Basel III capital requirements; and the high cost and complex requirements of servicing troubled mortgages. Fortunately, these problems lend themselves to policy changes that can help both mortgage lenders and homebuyers in a "win-win" situation, in contrast to the regulatory rollbacks that trade away consumer protection for lender profits.

In this testimony, I first provide a reminder of the problems in the pre-crisis mortgage market and then sketch out the dimensions of the current credit crunch. Next, I examine some of the proposed regulatory reforms and demonstrate how they could hurt rather than help today's homebuyers.

- The CLEAR Relief Act would undermine core lending rules for more than half of all mortgage originations and restore incentives to make "exploding" adjustable rate mortgages.
- The Mortgage Choice Act would make mortgages more expensive by re-opening the door to upselling practices driven by kickbacks and commissions.
- The Preserving Access to Manufactured Housing Act would sanction offering a largely lower-wealth and rural population more expensive mortgages with fewer consumer protections than are available to households purchasing site-built homes.

Finally, I provide a set of alternate, effective recommendations to increase access to responsible, sustainable mortgage credit.

I. Background: A trip down memory lane to the pre-crisis mortgage market

A misalignment of incentives lies at the heart of the foreclosure crisis. A toxic combination of Wall Street appetite for risk and stakeholders up the entire mortgage origination chain making more money for originating worse loans drove home prices to unsustainable levels. In the capital markets, investors aggressively poured money into the mortgage-backed-securitization machine in search of yield, while "financial innovations" aimed at managing risk actually spread that risk throughout the system. Subprime mortgage products proliferated and were sold to consumers who could have qualified for more stable and affordable products. Homeowners lost existing equity to aggressive lenders and brokers milking these transactions for fees. So-called "Alt-A" mortgages with features previously used judiciously in a narrow market were broadly marketed and layered with increasing numbers of risk factors, virtually assuring their failure.

At the height of the housing bubble, independent mortgage brokers originated the vast majority of subprime loans, receiving their compensation from lenders immediately upon brokering the loan. Those lenders then sold the loan into the secondary market within weeks, where it was bundled together with other mortgages and sliced and diced into mortgage-backed securities (MBS). The facilitators of this process – the investment bankers, lawyers, and ratings agencies involved – were all paid their fees regardless of the performance of the MBS. Those securities were then sold to investors. At the same time, even more derivative products were layered on top of them, with credit default swaps at the top of the pyramid – what Warren Buffet identified as early as 2003 as "financial weapons of mass destruction."[3]

Most of the subprime and so-called Alt-A mortgage products layered a variety of risks to create loans that were essentially designed to fail. One of the worst products, the hybrid adjustable rate mortgages also known as 2-28s or 3-27s because they would have 2 or 3 years of a fixed rate before the rate would explode, would often be locked in by prepayment penalties as high as four percent of the mortgage amount, so to refinance, these penalties would be paid from the proceeds of the new loan, and the loan balance would grow with each refinancing. Other mortgages, the "pay option" variety, offered consumers an opportunity to pay even less per month than their interest payments alone, which resulted in loan balances that rose rather than declined over time. While these designed-to-fail products stripped away much of the economic benefit of homeownership, it was at least possible – and extremely lucrative for brokers, lenders and investors – to continue refinancing as long as home prices kept rising. Once home prices declined, however, failure was virtually inevitable.

In addition to the exploding rates and prepayment penalties, other risky features included a failure to escrow for taxes and insurance (which often was a part of deceptively marketing a "lower monthly payment"), little or no documentation of income, and underwriting only to the very low initial teaser rates. In many cases, mortgage brokers were paid more to steer borrowers into higher-rate loans with riskier features through lender-paid yield-spread premiums, and they generally received the highest lender payment when that increased rate was locked in with a prepayment penalty.[4]

The predatory lending practices and toxic products characteristic of that period had only one function: to enrich mortgage brokers, lenders, and investors. These were not true "affordability" products

designed to help renters become homeowners; in fact, the overwhelming majority of subprime mortgages made from 1998 through 2006 went to borrowers who already owned their own homes – 60 percent were refinances, and 30 percent were for families who were moving from one home to another.[5] Far from expanding homeownership to people who otherwise could not afford it, subprime lending actually resulted in a net reduction in homeownership.[6] Homeownership rates in the US peaked in 2004, well before the housing bubble had fully inflated or burst.[7]

Similarly, the damage to the market was largely wreaked by the mortgages themselves and the system for selling them, not by borrowers who were overreaching or not ready for homeownership. The average subprime loan amount (which includes loans made in high-priced housing markets like California) was a modest $205,700.[8] What's more, most borrowers who received predatory loans qualified for better, more sustainable loans. A study for the Wall Street Journal found that of the subprime loans originated in 2006 that were packaged into securities and sold to investors, 61 percent "went to people with credit scores high enough to often qualify for conventional [i.e., prime] loans with far better terms."[9] Even those borrowers who did not qualify for prime loans could have received sustainable, thirty-year fixed-rate loans, for at most 50 to 80 basis points above the introductory rate on the unsustainable exploding ARM loans they were given.[10]

When the music stopped, the market crashed quickly, and the foreclosures began. At that point, it became clear that mortgage servicers had no ability or capacity to assist troubled borrowers. Congress blocked the most effective solution, which would have been to permit judicial loan modifications, and subsequently various executive and regulatory agencies worked for years on programs such as Making Home Affordable and on new servicing rules and regulations. Yet servicers to this day are unable to effectively handle a large quantity of failing mortgages.

Not surprisingly, the huge number of foreclosures triggered a much larger economic event – the Great Recession, where high unemployment rates combined with huge numbers of underwater mortgages decimated many neighborhoods and communities along with household balance sheets.

II. Why today's mortgage market needs fixing

In the wake of the financial reforms enacted after the crisis, mortgage lending is much safer than it was, and many predatory practices have either disappeared or at least are far more limited. At the same time, the national mortgage market is significantly smaller than it was, both in terms of overall volume and home sales.[11] The national homeownership rate has dropped from close to 70 percent to 64 percent. Cash investors made 29 percent of all purchases in 2013, way above their historic norm of 10 percent to 12 percent.[12] Housing starts remain depressed, and even optimistic projections for 2015 remain well below levels seen before the housing boom.[13]

A big reason for the change in the size of the market is that access to credit remains historically tight. For a conventional home purchase mortgage, the average FICO score is 754. While Federal Housing Administration credit is easier to obtain, with average credit scores for purchase-money mortgages around 680, it is still tighter than historical norms.[14] The Urban Institute estimates that approximately 1.25 million fewer purchase mortgages were made in 2013 than would have been the case had credit availability remained at pre-housing-bubble 2001 levels.[15] Consequently, more than 4 million loans have

been "missing" from the market over the last 5 years. This tight credit has disproportionately affected African American and Latino borrowers.[16]

A particularly troubling dimension of this problem is that homeownership rates for people of color have dropped particularly dramatically, with the Latino homeownership rate falling by 6 percent from its peak and the African American rate falling by 8 percent.[17] This decline in homeownership plays a significant role in the ever-increasing wealth disparities between whites and people of color.[18] Specifically, whites lost about 26 percent of their net worth during this period, while African Americans lost 50 percent and Hispanics lost 61 percent.[19]

Because the majority of families formed in America going forward will be families of color, a steep reduction in the numbers of Latinos and African Americans buying homes spells trouble for the housing market for decades to come.[20] It is also a problem that even as home prices became more affordable than they had been in years, the lack of affordable credit means many communities that lost significant wealth due to foreclosures have failed to rebuild that wealth through homeownership; as more people rent, and especially as more formerly owner-occupied homes transition to long-term rental, payments that could be contributing to rebuilding family balance sheets instead flow to investors, many of whom live outside the community.

Additionally, weakness in the housing market deprives our economy of the economic multiplier effects of a strong housing market, including additional construction jobs, consumer demand for household-related items, and local and state tax revenue. Moody's Analytics estimates that if home construction were at a more typical level, the economy would be at full employment.[21] The stubborn persistence of negative equity also continues to depress aggregate consumer demand for all goods and services, with significant macroeconomic consequences. Homeowners with high levels of debt relative to the value of their assets have experienced larger declines in consumption than less highly leveraged homeowners, even after taking into account declines in net worth.[22]

III. Current proposals to roll back regulatory reforms will leave consumers vulnerable without increasing access to high-quality, affordable credit

Some mortgage industry players are using the tight credit environment described above as a reason to call for rolling back Dodd-Frank. In the Senate, several bills are now pending that would reverse some of the important protections of this landmark financial reform legislation. However, a time when policymakers agree that increasing homeownership is a good idea is the worst possible time to remove underlying consumer protections. In fact, the only reason that many individuals and organizations support increasing access to credit is because they are counting on the Dodd-Frank framework to keep guardrails on the market. If those guardrails are removed, the likelihood of seeing a return to predatory and unsustainable lending is extremely high.

The truth is that the Consumer Financial Protection Bureau and other agencies charged with implementing the Dodd-Frank mortgage provisions have worked hard to accommodate the needs of industry stakeholders, holding literally hundreds of meetings and using their exception authority liberally. For example, the six regulators charged with establishing "risk retention" rules made significant changes to the qualified residential mortgage definition in response to industry concerns.[23]

Indeed, mortgage trade associations have noted that the Consumer Financial Protection Bureau in particular has done a good job taking industry concerns into account.[24] In numerous rulemakings, CFPB has provided special rules taking into account all sorts of variables, including loan size, lender size, originator type, and liability concerns. A quick review demonstrates the extent to which CFPB has been responsive to these concerns. CFPB has taken the following actions, among others:

- Established a "true" safe harbor for loans meeting the qualified mortgage definition, although the statute only calls for a rebuttable presumption liability standard.[25]
- Permitted exceptions to limitations on loan originator compensation for bank loan officers as opposed to independent mortgage brokers.[26]
- Tailored the qualified mortgage points and fees cap to accommodate smaller loan sizes, allowing up to 8 percent in fees for very low balance loans.[27]
- Allowed cure periods for lenders who make unintentional clerical errors in DTI and Points/Fees calculation[28]

Nowhere has Dodd-Frank and CFPB provided more accommodation than to smaller financial institutions. Congress and the CFPB have both recognized the unique and important role that small banks play in communities across the country, and as a result, the majority of these institutions already have access to a variety of exemptions and special provisions to ensure that they have the flexibility to do high quality lending that meets the needs of their communities:

- Small banks have greater underwriting flexibility when making mortgages that are eligible for safe harbor protection, including mortgages with APRs 200 basis points higher than larger banks.[29]
- Those serving rural or underserved areas may make loans that are eligible for the qualified mortgage designation even if the loan requires a balloon payment, which is otherwise prohibited under that designation.[30]
- Community development financial institutions, housing finance agencies, small rural lenders, CHDOs and some non-profits have special carve-outs from the Ability-to-Repay rule.[31]
- Small institutions serving rural or underserved areas are exempted from maintaining escrow accounts for higher cost loans.[32]
- Small creditors who service fewer than 5,000 loans are exempt from most mortgage servicing rules.[33]
- CFPB has supervision, examination, and enforcement authority over only those financial institutions with more than $10 billion in assets.[34]
- CFPB has not yet pursued any enforcement actions against community banks.[35]
- Small businesses have the opportunity to submit early comments to the CFPB under the Small Business Regulatory Enforcement Fairness Act.[36]
- CFPB has recently proposed expanding the definition of small creditor so that roughly three quarters of creditors with less than $1 billion in assets would qualify for a variety of mortgage rule exemptions. It also proposed expanding the rural definition to be more inclusive of rural pockets in urban areas.[37]

In short, while lobbyists looking to roll back financial reform claim the rules make it impossible for smaller institutions to compete and point to the declining number of small banks in America as evidence for their case, it is clear that these institutions already benefit from special treatment across a wide

range of rules. In fact, the decline of the small banking sector predates financial reform by decades. FDIC data show that for the last twenty years, the number of small banks has declined at a rate of about 300 per year. This rate has remained essentially unchanged in the years since Dodd-Frank was passed.[38]

Nor has reform destroyed the profitability of small banks. In the fourth quarter of 2014, profits at community banks increased 27 percent compared to the previous year, despite the fact that they had to comply with the new CFPB mortgage rules.[39] FDIC data also demonstrates that by many measures, including net interest income, community banks are performing better other institutions.[40]

A primary problem for small banks is that the complexity of today's market means size matters. Large banks can benefit from the economies of scale that make markets such as residential mortgage lending more efficient, while small banks cannot.[41] A 2012 FDIC study of community banks shows that over 80 percent of the banks that exited the industry between 1984 and 2011 left to become larger banks, either through a merger with an unaffiliated bank or consolidation with another chartered bank within the same organization.[42] Only 17 percent of the banks that left the industry did so because they failed.[43]

Also, while it's inarguable that compliance costs can be more of a burden for a small institution than a large one, all banks operate under myriad rules, with Dodd-Frank being only one part of that picture, and rolling back consumer protections is not a solution to challenges posed by capacity problems. Instead, regulators and policymakers should proactively support small lenders' ability to adapt new technology and processes so that they can meet their regulatory requirements as efficiently and affordably as possible.

The CFPB's mortgage rules also appear to be having little effect on the profitability of mortgage lending more broadly. The Mortgage Banker Association's most recent survey of loan profitability among independent mortgage banks and mortgage subsidiaries of chartered banks shows that mortgage loan origination profitability has increased dramatically since the quarter *before* CFPB's mortgage rules took effect.[44] Additionally, a larger proportion of these companies are profitable than before the mortgage rules took effect, and personnel or total loan production expenses have increased only minimally during this time.[45]

Finally, some have seized on the recent interest in community bank regulatory relief to suggest that non-depository institutions should receive similar exemptions.[46] However, the business model of non-depository institutions bears little resemblance to that of small banks with known customers and strong community ties. To the contrary, non-depositories tend to have single rather than repeated interactions with customers, and many of those customers live in locations where the non-depository likely has no presence. Additionally, non-bank mortgage lenders were responsible for some of the most pernicious practices during the housing bubble. We should not return to the days when these lenders were able to avoid regulatory scrutiny or oversight, especially under the guise of helping community lenders.

Below, I take a closer look at several specific proposals pending in the Senate, examining what impact each would have on consumer protection, mortgage sustainability, and access to credit.

A. S. 812: The CLEAR Relief Act

The CLEAR Relief Act, recently introduced in the Senate, would deem any mortgage made by any bank with assets under $10 billion to qualify for "qualified mortgage" safe harbor status as long as the bank holds the mortgage in portfolio for at least 3 years.[47] This unusually broad exemption would blow a hole

through the heart of the Dodd-Frank Ability to Repay rules and shield those banks from any accountability to customers. The result of the three-year portfolio exception could easily be a new brand of hybrid adjustable rate mortgages (or "3-27s") that would be designed to fail only after the financial institution was no longer holding them in portfolio.

To understand this proposal, it is important to understand the interplay between Dodd-Frank's core Ability to Repay requirement and the subset of loans that fit into the "qualified mortgage" (QM) definition. Ability to Repay codifies a basic principle that should be common business sense but which was largely ignored during the run-up to the crisis: a lender should not make a loan unless it has reasonably determined that the borrower can afford to pay the entire loan back. To do this thorough underwriting, a lender will need "verified and documented information."[48] If a lender makes a loan that does not meet these standards, the borrower would have the basis to take legal action against the lender for a period of three years. A borrower can also assert violation of this rule as a defense to foreclosure at any time, but damages would be limited to three years' worth of finance charges and fees.

The "qualified mortgage" definition was intended to designate a category of "super-safe" mortgages – mortgages that have so few potential risks that lenders making this type of loan would receive extra protection from any potential lawsuit. While the Dodd-Frank statute established a higher threshold for legal action, the CFPB used its authority to go further than the statute to give lenders a true "safe harbor" for QM loans that are not higher-cost, which makes lenders virtually impervious to liability if they make QM loans. The QM definition excludes certain types of riskier products, such as negatively amortizing, interest-only, and balloon mortgages, requires underwriting to the maximum possible payments in the first five years of the loan, places a limit on fees that lenders can charge, since high fees generally make mortgages riskier, and excludes borrowers whose total debt-to-income exceeds a certain threshold.

As noted in the previous section of this testimony, CFPB allows loans made by small banks to qualify for the QM safe harbor even if the borrower has a higher debt-to-income ratio than specified, and for certain institutions, even if the mortgage has a balloon feature. While these banks are still subject to other components of the QM definition, because the responsible community banks were already largely engaged in safe lending, they have not had to change their practices very much at all.

The CLEAR Relief Act would expand the balloon loan exemption to much larger banks, and – even more concerning – convey safe harbor status or legal immunity on loans with virtually *any* terms or features as long as they are held in portfolio for three years by a bank with less than $10 billion in assets.

Proponents of this bill argue that because loans are held on portfolio, lenders have an incentive to insure a borrower will succeed. But history has shown otherwise. Some of the most egregious predatory lenders such as Countrywide and Washington Mutual kept a considerable number of their failed loans on their portfolios, leading to their severe financial distress.[49] And nothing prevents a portfolio loan from being predatory by charging borrowers high fees or significantly higher interest rates than they could otherwise qualify for. Furthermore, the CLEAR Relief Act's automatic granting of QM status to portfolio loans after three years gives lenders an opportunity to create loans whose price or other risk features dramatically increase after the three-year deadline.

The CLEAR Relief Act proposal also would exempt all these banks from the requirement that they require escrow accounts for borrowers in higher-cost loans. The failure to escrow was also a large contributor to bad lending, as many borrowers will fail to budget properly for large tax and insurance bills at the end of the year, and may think that their monthly payment is just "PI" (principal and interest) rather than PITI (principal, interest, taxes and insurance).

Finally, exempting institutions under $10 billion is not targeted at what anyone would think of as their local community bank. *In fact, this definition would include all but the largest 110 depository institutions in America and well over half of all mortgage loans.*[50] According to the FDIC, the average community bank has approximately $340 million in assets and fits comfortably under the current $2 billion asset threshold established for the small creditor QM definition.[51]

B. The Mortgage Choice Act

The so-called "Mortgage Choice Act" would exempt title insurance sold by a title insurance company affiliated with a lender from the "points and fees" cap in the QM definition. By permitting lenders to use affiliates to evade the fee cap, this legislation makes mortgages more expensive, which narrows rather than expands access to credit, and can easily lead to the kind of equity-stripping that harmed so many consumers in the 90s and early 2000s.

The points and fees cap in the QM definition excludes certain bona fide third party charges, including title insurance offered by non-affiliated insurance companies. However, because abuses related to affiliates abounded during the run-up to the crisis, with kickbacks and upselling rampant throughout the system, the fee cap does not exempt charges for affiliate companies, which removes the incentive for these arrangements. If this protection were removed, lenders would once again have an incentive to steer borrowers toward higher-cost insurance plans offered by affiliate companies that compensate the lender. Because borrowers rarely understand the relationship between corporate affiliates, they cannot protect themselves against inappropriate upselling based on those corporate relationships.

In testimony yesterday before the House Financial Services Committee on the same topic, Mitria Wilson from the Center for Responsible Lending observed that "anti-competitive practices put companies at a significant disadvantage if they market directly to consumers and can offer lower rates."[52] For example, one company, Entitle Direct, has only 0.1% of the market even though it offers rates that are 35 percent lower than competitors.[53] Consumers already have little choice in the title insurance market, and the Mortgage Choice Act would only constrain consumer choice by giving lenders more incentives to steer consumers to affiliated insurers.

While some states adequately regulate title insurance premiums, many states either do not regulate title insurance rates or allow insurers to set their rates and essentially notify state regulators.[54] And while the Real Estate Settlements Procedures Act, or RESPA, prohibits paying kickbacks among third-party title insurers, it does not prohibit payments to affiliated title firms.[55]

While the industry forces calling for the passage of the Mortgage Choice Act claim that the QM cap on points and fees is making it impossible for them to originate loans profitably, we know that the data indicates otherwise. As shown above, measures indicate that mortgage lending is more profitable today than it was before the CFPB's mortgage rules took effect.

Relatedly, some groups have advocated for raising the points and fees caps for all loans with a balance of less than $200,000. This change would mean that a substantial share of the mortgages would not subject to the 3% cap on points and fees to which Congress intended qualified mortgages to be subject. Responding to industry concerns, the CFPB has already used its authority to increase the allowable points and fees on smaller balance mortgages. Given what we know about the current profitability of mortgage originators, we believe this proposal is unnecessary. Rather than increase access to credit, expanding the universe of loans not subject to the 3% cap would primarily result in consumers paying more for mortgage credit.

C. S. 682: The Preserving Access to Manufactured Housing Act

The Preserving Access to Manufactured Housing Act would dramatically scale back the protections available to a consumer who takes out a loan to buy a manufactured home.[56] Specifically, it would strip away critical protections for buyers of manufactured homes, who are among the nation's most financially vulnerable consumers, by rolling back updated high-cost loan thresholds. If this proposal were to become law, a lender could charge nearly 10 percentage points higher than a prime mortgage rate without the borrower obtaining the same heightened protections that would apply in the case of a high-cost mortgage on a site-built home.

Note that while manufactured housing owners have only about one quarter of the wealth of homeowners as a whole, they typically pay far more for their home loans: more than two-thirds of manufactured home loans are currently categorized as high priced loans compared to 3 percent of site-built homes.[57] Additionally, the bill would make it easier for a manufactured home salesperson to steer a consumer into a higher cost mortgage, even when they might qualify for a more affordable loan. Earlier this month, the Center for Public Integrity and the Seattle Times reported on consumer abuses in manufactured housing finance, detailing how borrowers were misled into taking out expensive loans and how retail salespeople were encouraged to steer borrowers into affiliated loans.[58] The last thing this vulnerable population needs is cutbacks to the sorely needed protections in Dodd-Frank.

It is absolutely true that manufactured housing plays a crucial role in providing families with affordable housing, especially outside of metropolitan areas, and that affordable credit for manufactured housing is currently constrained. However, legislation that erodes consumer protections and paves the way to more expensive mortgages will harm the very consumers it is purported to help. An alternative, safer way to support the development of a robust, responsible mortgage market for manufactured housing loans is described in section "IV. B." below.

IV. Effective ways to help increase access to high-quality credit

As explained above, the proposed rollbacks of Dodd-Frank are both overly broad and insufficiently targeted to the real problems, and therefore will increase risk without necessarily increasing access to appropriate products. Increasing access to safe and sustainable credit is a critically important goal. But it is equally critical to ensure that any expansion of access not lead to the same predatory and abusive market practices that led to the crisis.

There are a number of other, safer policy changes that can increase access to credit without compromising consumer protection. In fact, there is much agreement among the many stakeholders in this system on the dials and levers that can help increase access to safe and sustainable mortgages. The following is a suggested agenda for such actions, although it is by no means exhaustive.

A. Congress should complete comprehensive reform of the housing finance system

One thread that runs throughout most policy recommendations about easing tight credit is the need to provide as much certainty as possible to market participants and stakeholders. Perhaps the largest of such uncertainties is the fate of mortgage giants Fannie Mae and Freddie Mac, which have now been under conservatorship for more than six years.

Some advocate for simply returning to the system we had before the crisis, in which Fannie and Freddie's private shareholders profited from an implicit government guarantee with minimal capital requirements. While we agree the conservatorship should not last forever, before it ends, we need to fix the misaligned incentives that led the mortgage giants to need a taxpayer bailout and we must create an explicit, priced, and paid-for government guarantee to support the long-term, fixed rate mortgage product while protecting taxpayers.

The legislation passed last year by the Senate Banking Committee, S. 1217, provided a good framework for discussion, but lacked a number of essential elements that we have recommended, particularly with respect to the access to and affordability of credit.[59] Placing the goal of access to affordable, sustainable credit at the center of the new system's purpose will provide the greatest benefit in the long run not only to families but also to lenders and investors and will also protect taxpayers from future bailouts.

We look forward to working with Congress to craft a housing finance system that can take this country into the future smoothly and successfully.

B. The Federal Housing Finance Agency should encourage Fannie and Freddie to serve more borrowers and make other changes to increase safe access to affordable credit

While comprehensive housing finance reform proceeds through the legislative process, we urge the Federal Housing Finance Agency to use its extraordinary powers of conservatorship to promote a robust, inclusive mortgage market that provides liquidity for the broadest possible range of credit needs. Given the GSEs' dominance in the secondary market, their appetite for mortgages essentially determines whether the mortgages will be made at all by the primary market.

FHFA has already taken two very important steps: providing more certainty to lenders around repurchase policies – also known as "rep and warrant" relief – and allowing the Enterprises to offer mortgages with three percent down payments as long as the borrower has private mortgage insurance. Early indications suggest these changes are making a positive difference in the marketplace. Additional steps the agency should take are the following:

- **Finalize a stronger housing goals rule:** In recent years, whole segments of the market have moved to the Federal Housing Administration or have not been served at all. In 2012, for example, the enterprises financed only 16 percent of home purchase loans that originated in

low-income and minority Census tracts, one-quarter of home purchase loans to African Americans, and under one-third of home purchase loans to Latinos.[60] Today, there are no housing goals in force at all, as FHFA has not yet issued a final rule setting goals for 2015-2017. As the agency prepares to issue this rule, we urge it to set strong single- and multifamily benchmarks, including a 27 percent goal for low-income home purchase lending; take enforcement actions that considers the performance of the overall market when the enterprises fail to meet the housing goals; establish subgoals for small multifamily properties; and create reporting requirements for single-family rental.[61]

- **Complete the long-overdue "duty to serve" rulemaking:** FHFA can use the implementation of the "duty to serve" rule required by the Housing and Economic Recovery Act of 2008 to encourage responsible innovation and give the enterprises strong incentives to serve broadly and to lead the market.[62] In particular, FHFA can make a significant contribution to greater affordability in the manufactured housing area by using the duty-to-serve rule to push the market toward more responsible practices in the area of chattel lending. The majority of manufactured housing is titled as chattel rather than real property, meaning that buyers often lack basic consumer protections.[63] Borrowers who receive chattel financing are even more vulnerable than typical manufactured housing owners, facing more expensive loans, fewer rights upon default, and legal uncertainties if they do not own the land beneath their properties.[64] In the affordable housing preservation and rural markets, we similarly believe that the enterprises can actively support these markets through new products, flexible underwriting, affirmative outreach, and other activities, including grants to and partnerships with high-performing nonprofits devoted to this work.

- **Use g-fee policies to make housing affordable to all populations in all geographies:** FHFA should return to a pricing structure that is transparent, countercyclical—or, at the very least, not pro-cyclical—and take full advantage of the enterprises' unique ability to pool risk. As we recommended in our comment letter to FHFA,[65] we think FHFA should price based on what is needed to cover expected losses and costs—including a justifiable level of capital and revenue to support its cost—and to protect the taxpayer in the event of stress scenarios, rather than on pursuing particular market shares for non-GSE entities or sectors. This means removing the adverse market fee, eliminating loan-level pricing adjustments, and keeping the base g-fee at its current level.

- **Update credit score models to include more creditworthy borrowers:** Currently, the enterprises require the use of a FICO 04 credit score in their automated underwriting systems.[66] However, newer scoring models, including both FICO 09 and VantageScore, have made some critical changes that will improve the reliability of scores and/or allow the scoring of tens of millions of consumers. These newer models no longer consider paid collection items, including medical debt collections, and give less weight to unpaid medical debts. In addition, these newer models are better able to deal with consumers with limited credit history, or thin-file consumers. For example, FICO 09 has enhancements to better assess thin-file consumers, and VantageScore claims to be able to score an additional 30 million to 35 million thin-file consumers.[67] We urge FHFA and the Enterprises to move quickly to modernize their systems.

C. As a provider of credit to so many underserved populations, FHA should continue to improve access to and affordability of credit

The Federal Housing Administration has played a crucial role in supporting our economic recovery, preventing not only even more catastrophic home price declines but also a double-dip recession. While this support came at a cost to the agency's capital ratio, a combination of strong management and improvement in the economy has put the agency on track to fully replenish its reserves over the next couple of years. Particularly, FHA has supported first-time homebuyers and buyers of color, who are poorly served by the conventional market.

Recently, FHA took a major step in increasing access to affordable credit when it reduced annual mortgage premiums, which had gotten too high in the wake of the crisis. Now, FHA should complete efforts underway to provide clarity to lenders and reduce overlays. To address lender concerns about indemnification, FHA has proposed a new system for detecting defects in loan quality and holding lenders accountable for such defects. In this proposal, FHA more clearly identifies and classifies defects in loan applications, establishes severity levels of such defects, and provides a more objective approach to analyzing appropriate cures for defects.

FHA should also complete its work on the so-called Supplemental Ratio. Right now, FHA uses the Compare Ratio tool to identify risky lenders for further scrutiny. The ratio compares the performance of loans originated by a given lender to loans originated by other lenders in the same geographic location. However, the ratio makes no allowance for the loan characteristics of a lender's book of business, and thus incents lenders to originate loans primarily to pristine borrowers. Since FHA is statutorily bound to retain the Compare Ratio, adding additional dimensions through a Supplemental Ratio will help provide a more useful and robust comparison tool that allows for lenders who desire to lend to more underserved populations or geographies.

Additionally, we believe it would be sensible for FHA to work closely with FHFA to align its policies to protect lenders, such as providing a three-year window of clean payment history for indemnification, with exceptions for fraud, data inaccuracies, and compliance with responsible lending practices.

Finally, FHA should continue to work to improve its servicing policies, both to improve loss mitigation as well as to align better with other servicing schemes to reduce unnecessary complexity and cost.

D. Housing agencies should fix servicer compensation policies to ensure that incentives are correctly aligned

The CFPB's servicing rules, along with the FHFA servicing alignment effort, provide essential procedural protections that promote better servicing outcomes for homeowners, investors, and communities. The recent proposed amendments to the CFPB rules make substantial improvements in crucial areas including transfers of servicing, bankruptcy, and access to the loss-mitigation system for subsequent hardships. They also make important strides in protecting homeowners who seek assistance following the death or divorce of a co-homeowner.

However, there are still some basic building blocks to servicing reform that are not yet in place. First, servicer compensation reform has been sidetracked and must be revived. As long as servicers profit at the expense of homeowners and investors, the system will not reliably produce healthy outcomes for the housing market and communities regardless of the rules or enforcement thereof. Regulators must come together to develop a framework to modernize and rationalize servicer compensation.

Second, with the eventual sunset of HAMP, policymakers need to find a way to require loss mitigation and to require sustainable modifications for homeowners that also benefit investors. Loss mitigation before HAMP did not always happen, and when it did, it did not always promote long-term home retention. Without rules in place, it is possible—perhaps even likely—that the system will soon forget the lessons of the crisis. To the extent that the CFPB does not or cannot mandate loss mitigation and a substantive requirement for loan modifications, Congress and other regulators should step in to ensure that such a requirement is developed.

E. Regulators should monitor Basel III implementation

Regulators must continue to monitor the implementation of the new standards to ensure that the transition does not negatively impact consumers. In particular, under the new standards, higher risk-weights are assigned to mortgage servicing rights, which may be prompting some banks to sell their mortgage servicing rights to smaller, non-bank mortgage servicers.[68] As this shift occurs, regulators must improve oversight of non-bank mortgage servicers to ensure they have the servicing capacity to handle an increased number of loans and consider whether additional changes to the standards are necessary to prevent disruption in the mortgage servicing industry.

F. Congress and regulators should support alternative mortgage channels and innovative products to reach underserved borrowers

Many communities hardest hit by the housing crisis and the economic downturn have long been either underserved or not served by traditional financial institutions that could provide safe and affordable credit. Similarly, for many borrowers, the most popular mainstream products will always be difficult to access. For this reason, we recommend taking steps to strengthen alternative mortgage channels and to experiment with safe but innovative products to reach more borrowers.

The strong need for alternative lenders in underserved communities can be attributed to years of discrimination, redlining, and market failures in which mainstream financial institutions lacked incentives to lend to projects where the aggregate social return was positive. CDFIs and HFAs, which combine deep knowledge of local communities' needs with safe, targeted products, can identify and assist potential homeowners, and CDFIs can also provide business and consumer loans, investments, and retail banking services to neighborhoods that need critical economic catalysts to overcome years of disinvestment.

Congress and regulators should consider whether there are changes to regulations such as the Community Reinvestment Act, or CRA, that can be used to strengthen these institutions. For example, changing the way that financial institutions subject to the CRA receive credit for investing in CDFIs could provide a win-win solution for banks unwilling to take risks on certain populations, especially since CDFIs and nonprofits receive special treatment in the Dodd-Frank mortgage rules to enable them to better

serve lower-income families. Similarly, sources of funding such as recent settlements between government agencies and large banks could be directed to helping alternative mortgage channels scale their operations.

Additionally, a typical mortgage product is not always accessible to some households due to the down-payment requirements or fear of placing assets in a first-loss position. Shared-equity or shared-appreciation approaches can provide a middle ground between renting and traditional homeownership. In general, these products share certain common features: owner occupancy of residential properties, initial affordability, and sharing of risk and equity or appreciation. These strategies can potentially support modest individual asset accumulation while protecting consumers against home price declines and providing more stability to the macroeconomy in times of market disruption.[69] Congress and regulators should consider how to encourage safe experimentation with alternative products.

G. Congress and agencies should support housing and credit counseling for a wide range of potential homebuyers

Whether counseling a first-time homebuyer to avoid predatory loans, negotiating a modification that will allow a distressed homeowner to stay in their home, helping a low-income family find affordable rental housing, or helping a homeless person find emergency shelter, nonprofit housing counselors are advocates for housing consumers, especially those from traditionally underserved communities such as communities of color, low- and moderate-income communities, and the elderly. A growing body of research demonstrates that those who receive housing counseling realize better outcomes than similarly situated people who do not.[70]

Recently, Congress killed a proposed FHA entitled Homeowners Armed with Knowledge, or HAWK, that would have offered reductions on the upfront and annual mortgage insurance premiums, or MIPs, to FHA borrowers who participate in a specified housing counseling curriculum. Congress should immediately restore FHA's ability to pursue this idea. Other government agencies such as the U.S. Department of Veterans Affairs and the U.S. Department of Agriculture could create the same type of program, and FHFA could work with Fannie and Freddie to create a similar incentive structure in the secondary market through preferential pricing for counseled mortgages. Borrowers could yield additional incentives if they committed to post-purchase counseling as well. Bonus points could be awarded under the goals that would incent this kind of proven, safe, and sustainable lending. Additionally, Congress should grant the Department of Housing and Urban Development's, or HUD's, Office of Housing Counseling the authority to accept funds from private entities to be distributed and used for housing counseling activities.

H. Congress should extend the Mortgage Forgiveness Debt Relief Act

When a lender forgives mortgage debt through a short sale or a principal reduction modification or even after a foreclosure, the amount that the borrower no longer owes counts as taxable income to the borrower unless it fits into an exemption in the tax code. Given the deep inappropriateness of this result for those losing their homes, Congress created a tax code exemption in 2007 entitled the Mortgage Forgiveness Debt Relief Act, or MDRA. The MDRA has been crucial to virtually every effort to assist troubled homeowners and restore the housing market to health. However, the MDRA expired in 2012, and has only been extended piecemeal by Congress – last year, it was not extended until the very last

moments of the tax year. Without this legislation, homeowners are often unwilling to do short sales, which harms the overall housing market. Plus, principal reduction is less valuable to homeowners if they must pay tax on the forgiven debt, which hampers loss-mitigation efforts. Congress must extend the MDRA at least until the end of 2016 to provide the market with some certainty, and ideally, this exemption would become permanent.[71]

I. Congress should convert the mortgage interest deduction to a credit

The federal government spends $70 billion per year on the mortgage interest deduction—more than $1 trillion over a 10-year period and more than the entire HUD budget for a year.[72] Yet the benefit of the mortgage interest deduction is heavily skewed to households in upper-income tax brackets. As taxpayers' income increases, their tax rate increases and so does the value of the deduction. In addition, the mortgage interest deduction is only available to those who are able to itemize deductions rather than take the standard deduction. According to the Tax Policy Center's analysis of 2010 data, less than one-third of taxpayers itemize their deductions, and the majority of those who itemize fall in the top income tax brackets.[73]

As part of comprehensive tax reform, we recommend replacing the current mortgage interest deduction with a tax credit. Our proposal would gradually phase out the current deduction and replace it with an 18 percent nonrefundable tax credit.[74] The effect of this change would be to provide the same benefit to all taxpayers, rather than a much larger benefit to those with higher incomes. Increasing the value of the credit to low- and moderate-income taxpayers not only increases fairness and access to homeownership but also contributes to economic growth, since it puts more money in the hands of a large number of families who typically need to spend every dollar they earn just to get by.

J. Regulators should collect better mortgage data to help identify problems and potential solutions in the market

As a free and public database, the Home Mortgage Disclosure Act, or HMDA, provides critical data to housing market participants and stakeholders, especially to nonprofits and other entities without access to expensive proprietary databases. However, the HMDA database has long suffered from some key omissions, both in terms of who is reporting data and what data are reported.

Recently, the CFPB issued a set of proposed changes to the HMDA, including changes to definitions of covered institutions and transactions, as well as the addition of proposed new fields to improve the usefulness and quality of the HMDA data. We strongly support the CFPB's efforts. In addition to its proposals, we recommend additional data enhancements that would be of great benefit to researchers and community groups in the efforts to promote fair access to credit, while also helping equip regulatory and enforcement agencies with fair lending compliance. For example, we think the CFPB should take further steps to simplify the reporting requirement to one eligibility standard, add further fields on various topics such as denials and language and race, and collect information on loan modifications and housing counseling.[75]

Conclusion

As memories of the crisis fade, policymakers face some important choices in trying to strengthen the nation's housing market. We can open the doors to a new round of predatory, unsustainable lending, or we can work to create a healthier and more equitable housing market by promoting sustainable homeownership, affordable rental housing, and stronger neighborhoods. Choosing the latter will require action by a wide array of policymakers and market participants, which can be challenging. Ultimately, however, by working together, we can create a more robust, fairer housing market that drives economic growth and promotes opportunity for America's families.

Thank you again for inviting me to testify today. I look forward to continuing to engage with you on these and other issues.

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[72] See The White House, "Table 4.1: Outlays by Agency, 1962-2019," available at http://www.whitehouse.gov/sites/default/files/omb/budget/fy2015/assets/hist04z1.xls (last accessed December 2014); The White House, "Table 14-1: Estimates of Total Income Tax Expenditures For Fiscal Years 2013-2019," available at http://www.whitehouse.gov/sites/default/files/omb/budget/fy2015/assets/teb2015.xls (last accessed December 2014).

[73] Benjamin H. Harris and Daniel Baneman, "Who Itemizes Deductions?" (Washington: Tax Policy Center, 2011), available at http://www.taxpolicycenter.org/UploadedPDF/1001486-Who-Itemizes-Deductions.pdf.

[74] Roger Altman and others, "Reforming Our Tax System, Reducing Our Deficit" (Washington: Center for American Progress, 2012), available at https://www.americanprogress.org/issues/tax-reform/report/2012/12/04/46689/reforming-our-tax-system-reducing-our-deficit/.

[75] For more information, see Center for American Progress and others, "Re: Consumer Financial Protection Bureau's Amendments to Regulation C" (2014), available at http://www.responsiblelending.org/mortgage-lending/research-analysis/HMDA-Comment-Final-10-29-14.pdf.

RESPONSE TO WRITTEN QUESTION OF SENATOR HELLER FROM TOM WOODS

Q.1. A major issue for many potential home buyers and homeowners is flood insurance. Right now, homeowners essentially have no option but to buy Government-backed National Flood Insurance Program policies to meet mandatory purchase requirements. The Biggert-Waters flood insurance bill Congress passed had the unintended consequence of making it more difficult for private insurers to provide private flood insurance and for lenders to accept those policies. Right now lenders are being forced to reject many residential private flood policies. Senator Tester and I have introduced legislation in the past that would try to solve this problem.

I would like to know, Mr. Woods, if you support the development of a private flood insurance market that meet mandatory purchase requirements and could this help increase home ownership because consumers will have more insurance options?

A.1. Thank you Senator Heller for your question regarding NAHB's support of the development of a private flood insurance market that meets mandatory purchase requirements and if this could help increase home ownership because consumers would have more insurance options.

NAHB does not have policy on State-regulated insurance markets; however, we would welcome open competition and a vibrant private market.

In NAHB's experience, without the NFIP, many communities would be unable to provide affordable housing to many of their citizens. One of the leading causes of the housing affordability problem is the shortage of buildable land. By guaranteeing affordable flood insurance, the NFIP allows communities to use land that would otherwise be too costly due to high flood insurance premiums. Through the NFIP, flood insurance policies remain available and affordable, and residential structures can be constructed in floodplains as long as they are built to withstand flooding.

RESPONSE TO WRITTEN QUESTION OF SENATOR HEITKAMP FROM TOM WOODS

Q.1. Overlapping regulations in our mortgage markets have the potential to constrain credit and prevent otherwise worthy borrowers from qualifying for mortgages. That said, the Consumer Financial Protection Bureau (CFPB) has attempted to accommodate small and rural communities, institutions, and their customers during the rulemaking process by issuing a number of exceptions for these areas and revising rules when the existing regulations have proven unworkable or unduly burdensome. Below, find a list of regulatory accommodations that have been made by CFPB. How successful has each action been in providing relief, to what extent is each

measure deficient, and what steps can the CFPB take to improve each provision? Please provide any data or other information to support your position.

a. **Small Creditor QM:** Established a Qualified Mortgage (QM) Option that provides loans originated by small institutions—assets of less than $2 billion and make fewer than 2,000 loans annually—and held in portfolio for a minimum of 3 years a safe harbor.
b. **Balloon QM:** Created a QM option for mortgages with balloon payments that are originated by small creditors in rural or underserved areas.
    i. **Escrow:** Exempted small creditors who operate predominantly in rural or underserved areas from requirements to establish escrow accounts for higher priced mortgage loans.
c. **Rural Definition:** Incorporated industry feedback and expanded the definition of rural, using Census blocks. The revised definition would designate the entirety of North Dakota—except for the census blocks of three major towns—as rural.

A.1. Thank you Senator Heitkamp for your question on the Consumer Financial Protection Bureau's (CFPB) efforts to accommodate industry concerns through the rulemaking process. NAHB supports balancing mortgage lending standards and consumer protections and appreciates that the CFPB has made a concerted effort to solicit feedback from industry on the practical implementation of the 2013 mortgage rules. NAHB commends CFPB's efforts to monitor the impact of the new mortgage rules and appreciates that the CFPB is willing to adjust the rules in response to concerns in areas where improvements are needed.

NAHB supports the actions that CFPB has taken to provide relief to small financial institutions and those institutions lending in rural and underserved areas. NAHB believes that raising the loan origination limit for determining eligibility for small creditor status, along with the expanded definition of rural and the additional provisions, will provide small financial institutions with more flexibility in meeting the unique needs of the communities that they serve.

However, tight lending conditions continue to keep buyers on the sidelines even as the housing market recovers. At a time when housing is affordable and interest rates are low, more buyers should be able to enter the housing market. However, many creditworthy borrowers are not taking advantage of these opportunities. This impact is evidenced by the reduced participation rate of first-time home buyers that has dropped to 30 percent of the purchase market[1] from the historical rate of about 40 percent of sales.

NAHB believes that a healthy housing market includes broad participation from all population segments. NAHB has encouraged the CFPB to further investigate the impact of the new mortgage

[1] National Association of REALTORS® (NAR) Press Release. *Existing-Home Sales Lose Momentum in April.* May 21, 2015. Retrieved from: *http://www.realtor.org/news-releases/2015/05/existing-home-sales-lose-momentum-in-april.*

regulations, including the debt-to-income ratios and documentation requirements, on entry level buyers and other important market segments to ensure that creditworthy borrowers are able to access mortgage credit. Broader availability of safe and responsible credit increases home ownership opportunities and provides benefits to the housing market and the overall economy.

NAHB believes that the CFPB should take additional steps to address today's tight lending environment, such as adjusting the QM 3 percent cap on points and fees to exclude fees paid to affiliated businesses, and to provide a reasonable hold-harmless period for enforcement of the of the CFPB's TILA–RESPA Integrated Disclosures (TRID) regulation for those that make good-faith efforts to comply.

RESPONSE TO WRITTEN QUESTION OF CHAIRMAN SHELBY FROM J. DAVID MOTLEY

Q.1. You testified that loan officers employed by nonbank lenders are required to be licensed under the SAFE Act. Your testimony advocates for a transition period for new loan officers of nonbank lenders to work while they are earning their certification, so long as these employees were previously loan officers with another institution.

How could this particular proposal aid in the expansion of mortgage credit of the reduction in the cost of credit? Based on the average time period to complete this transition, how long should this transition period last?

A.1. The Secure and Fair Enforcement for Mortgage Licensing (SAFE) Act, enacted in 2008, mandates a nationwide licensing and registration system for residential mortgage loan originators (MLOs). Some of the objectives of the SAFE Act include creating increased accountability for MLOs, greater consumer protection, and providing home buyers with tools to help them select their loan officers. Unfortunately, in its current form, the SAFE Act creates a two-tiered licensing system that impedes the mobility of mortgage loan officers (notwithstanding the fact that Federal depositories are required to conduct regular job-specific training for their consumer-facing employees).

The SAFE Act requires MLOs employed by nonbank lenders to be licensed, which includes pre-licensing and annual continuing education requirements, passage of a comprehensive test, criminal and financial background reviews conducted by State regulators, and registration in the National Mortgage Licensing System and Registry. By contrast, MLOs employed by federally insured depositories or their affiliates must only be registered in the NMLS, and do not have to meet testing and specific education requirements.

This two-tiered structure creates a significant disincentive for loan officers to transition from a depository to a nondepository. These MLOs must wait for weeks, or even months, while they meet the SAFE Act's licensing and testing requirements—despite the fact that they have already been employed and registered as a loan officer at a depository.

Nonbank lenders or independent mortgage banks (IMBs) typically focus exclusively on mortgage lending. In recent years, large

depository-institutions have moved away from the home purchase business and toward other types of mortgage-related business, including refinancing, servicing portfolio retention, and making more jumbo and adjustable rate loans that can be held for investment. In contrast, from 2008 to 2013, the IMBs' share of the home purchase market grew from 25 percent to 40 percent with a particular focus on providing loan products for first-time home buyers and underserved borrowers.

A small amendment to the SAFE Act to require States to issue transitional licenses to registered loan officers seeking employment with nondepositories would help to eliminate the delays and hurdles in hiring highly qualified loan officers to work for IMBs and focus their efforts on providing home purchase mortgage credit. These individuals should be able to continue originating loans for 120 days after leaving their bank employer (and while beginning their work for an IMB). Similarly, a State-licensed loan originator in one State who takes a similar position in another State would have a 120-day grace period to obtain a license in the new State. This 120 period is based on the amount of time it typically takes for an MLO to receive a license and is also consistent with laws in States that have already passed legislation to permit transitional licensing.

This narrow and simple solution creating transitional licenses would eliminate a significant impediment to IMBs hiring highly qualified bank loan officers. IMBs have made the commitment to provide mortgage credit to a broad range of creditworthy borrowers. By increasing labor market mobility, loan originators could freely move to lenders that are best able to serve their clients through competitively priced products that will insure more qualified borrowers access to credit.

RESPONSE TO WRITTEN QUESTION OF SENATOR VITTER FROM J. DAVID MOTLEY

Q.1. Mr. Motley, In your statement you assert that "New servicing rules have dramatically driven up the cost to service loans and driven down efficiency in servicing operations" and cite that loans serviced per full-time employees have decreased from 1,638 in 2008 to 790 in 2014. Moreover, you cite that direct costs to service each loan have increased from $173 per loan in 2008 to $309 in 2014, and costs to service loans in default have risen from $423 per year in 2007 to $2,214 in 2014."

Which regulations have most directly increased the cost and amount of time to service these loans?

A.1. It is difficult to isolate one particular regulation as the direct driver of the significant increase in servicing costs, due to the sheer number of new regulations from Dodd-Frank as well as the increased costs associated with the volume of foreclosures following the 2008 financial crisis. Costs have increased across the board but particularly in the areas of collections, loss mitigation, recordkeeping, borrower communications, vendor management, servicing technology, and quality control and quality assurance.

There have also been large increases in compliance costs in this time period as servicers implement the myriad new Federal and

State requirements as well as the costs associated with the National Mortgage Servicing Settlement among the larger servicers. The CFPB's broad and prescriptive servicing rule necessitated costly system overhauls, training expenses, and ongoing compliance outlays and has certainly played a role in the increased costs of servicing.

The effect of implementing regulations is also demonstrated by the increase in costs of servicing performing loans as well as nonperforming loans, suggesting that the impact of the new regulatory paradigm will be continued to be felt well into the future.

RESPONSE TO WRITTEN QUESTION OF SENATOR HELLER FROM J. DAVID MOTLEY

Q.1. A major issue for many potential home buyers and homeowners is flood insurance. Right now, homeowners essentially have no option but to buy Government-backed National Flood Insurance Program policies to meet mandatory purchase requirements. The Biggert-Waters flood insurance bill Congress passed had the unintended consequence of making it more difficult for private insurers to provide private flood insurance and for lenders to accept those policies. Right now lenders are being forced to reject many residential private flood policies. Senator Tester and I have introduced legislation in the past that would try to solve this problem.

I would like to know, Mr. Motley, if you support the development of a private flood insurance market that meet mandatory purchase requirements and could this help increase home ownership because consumers will have more insurance options?

A.1. The Mortgage Bankers Association supports the development of a private flood insurance market that meets mandatory purchase requirements. A competitive and sustainable flood insurance market will expand available insurance options, lower costs, and increase the number of at-risk properties that are insured. Increased private sector involvement can also serve to shift some of the burden of post-disaster recovery and rebuilding from taxpayers to the private sector thereby limiting the Federal Government's exposure to flood loss.

RESPONSE TO WRITTEN QUESTION OF SENATOR HEITKAMP FROM J. DAVID MOTLEY

Q.1. Overlapping regulations in our mortgage markets have the potential to constrain credit and prevent otherwise worthy borrowers from qualifying for mortgages. That said, the Consumer Financial Protection Bureau (CFPB) has attempted to accommodate small and rural communities, institutions, and their customers during the rulemaking process by issuing a number of exceptions for these areas and revising rules when the existing regulations have proven unworkable or unduly burdensome. Below, find a list of regulatory accommodations that have been made by CFPB. How successful has each action been in providing relief, to what extent is each measure deficient, and what steps can the CFPB take to improve each provision? Please provide any data or other information to support your position.

a. **Small Creditor QM:** Established a Qualified Mortgage (QM) Option that provides loans originated by small institutions—assets of less than $2 billion and make fewer than 2,000 loans annually—and held in portfolio for a minimum of 3 years a safe harbor.
b. **Balloon QM:** Created a QM option for mortgages with balloon payments that are originated by small creditors in rural or underserved areas.
    i. **Escrow:** Exempted small creditors who operate predominantly in rural or underserved areas from requirements to establish escrow accounts for higher priced mortgage loans.
c. **Rural Definition:** Incorporated industry feedback and expanded the definition of rural, using Census blocks. The revised definition of would designate the entirety of North Dakota—except for the census blocks of three major towns—as rural.

A.1. MBA believes it is time to consider changes in the QM definition to mitigate the adverse impact the CFPB's Ability to Repay rule has had on access to credit for some borrowers. In this regard, MBA appreciates the CFPB's efforts regarding the Small Creditor and Balloon QM as well as the Rural Definition identified in your question. Nevertheless, MBA believes changes to the QM definition are better made holistically and not limited to certain lenders based on charter types or business models. Consumers should not be forced to discern which institutions offer particular types of loans and their choices should not be limited to particular providers. Stratification of the market by establishing different underwriting standards for some lenders and not others only causes unnecessary consumer confusion and will lessen competition. A holistic approach to revising the QM would ensure a competitive market for all types of QM loans, and would not burden the consumer with figuring out which lenders offer which QM products. Accordingly, as detailed in our testimony we believe: (1) in addition to adding certain protections against the re-emergence of loans with risky features such as pay option ARMs, stated-income underwriting, and short-term balloon terms, any new portfolio QM also should be made available to all originators that process, fund and sell these loans to a bank (or REIT) that will retain the loans in portfolio for the required holding period; (2) the spread over the APOR for defining a safe harbor QM should be expanded to 200 basis points; (3) the definition of smaller loans should be increased to $200,000, with adjustments for inflation and a sliding scale that permits progressively higher points and fees caps for these smaller loans; (4) the right to cure or correct inadvertent errors be extended to DTI miscalculations and typographical and technical errors and omissions; and (5) title insurance fees paid to lender-affiliated companies should be excluded from the calculation of "points and fees" under QM just as such fees to non-affiliated companies are excluded.

ADDITIONAL MATERIAL SUPPLIED FOR THE RECORD

Regulatory Burdens to Obtaining Mortgage Credit

United States Senate Committee on Banking, Housing & Urban Affairs

Thursday, April 16, 2015
10:00 a.m.

American Land Title Association Statement for the Record

AMERICAN
LAND TITLE
ASSOCIATION

www.alta.org

Chairman Shelby and Ranking Member Brown, my name is Diane Evans and I serve as president of the American Land Title Association (ALTA). In my day job, I am vice president at Land Title Guaranty Company, a title insurance agency in Colorado. ALTA is the national trade association founded in 1907 that represents the abstract, real estate settlement and land title insurance industry. Our more than 5,500 member companies include abstracters, title agents, real estate attorneys and title insurers, ranging from small, one-person operations to large publicly traded companies. The majority of our members are small businesses and the average title agency earns $156,000 in gross annual revenue and employs three or fewer people. Our members employ more than 108,000 professionals and our members have offices in every county in the country. We search, review and insure land titles to financially protect a homebuyer's largest investment and the primary and secondary market mortgage lenders who invest in real estate.

Thank you for including this statement in the record for today's hearing on regulatory burdens to obtaining mortgage credit. As the Senate considers regulatory reform, it is useful to note that title insurance is regulated at the state level and our settlement business is regulated at the federal level. Historically, this dual regulatory structure has been rather complimentary; however, with ever increasing regulation, our members must comply with regulations that overlap and contradict one another. This creates a complex compliance environment and increased costs for our members' businesses, additional liability for our mortgage lender clients and confusion and frustration at the closing table for homebuyers.

One of the largest regulatory burdens that impacts consumer's ability to obtain mortgage credit is regulatory uncertainty. As mortgage lenders work to refine their risk management practices to avoid a regulatory misstep, homebuyers and settlement agents are often required to provide documents multiple times signed and dated by the homebuyer. As you can imagine, this process is extremely frustrating and confusing for consumers.

I would like to share an example of how this uncertainty impacts homebuyers and ALTA members:

> On March 31 a Baltimore couple, Brian and Emina, bought rowhouse in for $245,000. The couple closed on the home right before heading to a hospital for an induced labor for their first child, a boy. Their settlement agent, Nancy McNealy with Consumer Real Estate Title, Inc in Beltsville, Maryland, knew about the labor date and wanted to be sure that she got everything to the lender in a timely fashion so that Brian and Emina could close and then go to the hospital to give birth. The settlement agent was able to get all of the closing documents together in time. Then, after closing, the settlement agent received another email from the lender that said that copies of tax returns were needed to be signed in order for the lender to fund the mortgage. Throughout the process of obtaining the loan, the couple was frustrated because they continually had to resubmit and resign and re-date every line—every request was repetitive and last minute.

Nancy, the settlement agent in this story, has been in the business since 1979 and employs one other person. She says, "A good month for us is about 12 closings," and her gross revenue runs right around the $156,000 industry average. Most of Nancy's business is from returning clients with whom she has worked for nearly 30 years – she is actually on her 2nd

generation of those clients. Nancy believes that small title companies are important to this industry because she has her client's needs in focus and are willing to spend more time and energy on them. Nancy is hands-on with every transaction and knows her customers personally since she lives in this community and sees them and their families at the grocery store. Nancy says, "My reputation is essential."

We urge the Senate to consider the following two issues as you seek to provide more certainty about regulations that impact mortgage credit. First, as our industry prepares to implement the Consumer Financial Protection Bureau's (CFPB or Bureau) TILA-RESPA Integrated Disclosures (TRID) regulation, there are commonsense modifications and clarifications that will reduce regulatory burdens imposed by the regulation. CFPB should develop and announce a plan to provide implementation support during a restrained enforcement period following the August 1 effective date of the regulation through the end of the year to reduce the impact of these regulatory burdens on consumers.

Second, the Senate should pass legislation to help improve the way that the Bureau works with small businesses while it protects consumers. Specifically, the Senate should introduce and pass legislation to create a permanent Small Business Advisory Board and an advisory opinion process at the CFPB.

Regulation of Title Insurance

ALTA members provide two primary services to homebuyers and financial institutions. The first service is the preparation and issuance of title insurance policies protecting both purchasers and mortgagor of real property. Insurance products, including title insurance, are regulated by the states and falls outside of federal regulation as part of the business of insurance. Additionally, title professionals act as third-party settlement agents in real estate and mortgage transactions. This service is subject to federal regulation pursuant to the Real Estate Settlement Procedures Act (RESPA), which is within the jurisdiction of the CFPB.

At the state level, title insurance regulation includes oversight of insurer and agent licensing, product regulation, financial regulation, market regulation and consumer protection. States oversee title insurance pricing through the promulgation of rates or reviewing and approving company rate filings. Most states approach rate regulation by prohibiting excessive, inadequate or unfairly discriminatory prices for title insurance.

At the federal level, when title professionals act as independent third-party settlement agents in real estate transactions, they are regulated by RESPA. This law was designed to protect homebuyers through defining and prohibiting kickbacks and increasing consumer understanding by requiring transparency about all of the costs of homeownership.

TILA-RESPA-Integrated-Disclosure Forms

In 1968, Congress passed the Truth in Lending Act (TILA) to "assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various

credit terms available to him and avoid the uninformed use of credit."[1] RESPA was then enacted by Congress six years later.

For nearly 50 years, these laws required lenders and settlement agents to provide consumers with similar but different disclosures at the beginning and end of their mortgage and real estate transactions. However, these laws changed when Congress adopted Section 1032 of the Dodd-Frank Act, which required the CFPB to "propose for public comment rules and model disclosures that combine the disclosures required under the Truth in Lending Act and sections 4 and 5 of the Real Estate Settlement Procedures Act of 1974, into a single, integrated disclosure." The Bureau started this rulemaking process in 2011, issuing a final rule in November 2013 and an implementation date of August 1, 2015, which is now just 107 days away.

This regulation is more than just two new disclosure forms. It represents a paradigm shift in the way real estate settlements occur in this country. Since finalizing this regulation, the title insurance and real estate settlement industry has focused on implementation of these new forms and regulations. Our industry and software developers have worked tirelessly since 2013 to update their software and business processes to comply with this regulation. These software programs are wrapping up their beta processes right now and are expected to deliver final software to customers between April and June of this year. All of our training and implementation will take place during what the National Association of Realtors has determined is the busiest time of the year for real estate closings.[2] Unfortunately, our industry's comprehensive preparation efforts may not ensure that real estate transactions will not be disrupted beginning August 1.

Nancy McNealy, the settlement agent from Beltsville, Maryland, who was mentioned in this introduction, says that "it is costing a small fortune for most title companies to re-tool to meet the new August requirements." Nancy needed to switch software providers in order to properly support the TILA/RESPA changes. With her new provider, the cost to retrieve old files and continue to access her old database is costing nearly $3,000.00. The cost of the new software and its installation on new computers is about an additional; $5,000.00. For Nancy, that $8,000 in expense for her roughly $156,000 in gross revenue represents a 5% increase in cost of doing business for one regulation in 2015 alone. These software updates ensure that Nancy's company is compliant with the regulation and can send information needed for the real estate transaction to mortgage lenders and other involved parties.

Need for Formal Hold Harmless Period from August 1 to December 31

We appreciate that the Bureau provided our industry with 21 months to reform our processes and train our staff to meet these new regulatory demands. However, we know from implementation of past regulations that there will be a learning curve and unforeseen issues once

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[1] 15 U.S.C. §1601.

[2] Hale, Danielle. "Part 1: EHS in 2014 by the Numbers – Popular Closing Dates." *Economist Commentaries: National Association of Realtors*, 12 Jan. 2014. http://economistsoutlook.blogs.realtor.org/2015/01/12/part-1-ehs-in-2014-by-the-numbers-popular-closing-dates/ (last accessed 09 Apr. 2015).

the new forms are used in actual transactions. Therefore, we request that the Bureau publicly commit to making August 1 through December 31 of this year a hold harmless period for enforcement.

A hold harmless period will allow industry to adapt their business processes to comply with this regulation without the fear of potential enforcement actions and class action lawsuits. When faced with some uncertainty surrounding this rule it will make it easier for business to work in good faith to find a solution that works for the consumer instead of taking an overly restrictive approach to risk management. In the absence of a hold harmless period, it is likely that some mortgage lenders and settlement service providers will initiate restrictive risk management tactics. This might include limiting access to financing and settlement services in small communities, especially considering many of the unanswered questions that exist regarding compliance with this regulation. For example, it is currently unclear how to properly issue a new closing disclosure if the settlement is delayed due to an unforeseen event like the basement flooding the day before the closing. Without more clarity, the result is likely to leave homebuyers with less flexibility to obtain the deal they bargained for and potentially fewer companies to work with.

To be truly effective, a hold harmless period needs to be accompanied by a commitment from the CFPB to work with industry to gather data about implementation. The Bureau should also provide written guidance to address common industry implementation hurdles that emerge between now and the end of the year. The Bureau's Official Interpretations, compliance guides and webinars on the regulation have been very helpful to industry but they are not comprehensive. Written guidance is needed in many areas to clarify the regulation. We urge the Bureau to recognize the value to consumers of providing this written guidance.

Fix Inaccurate Disclosure of Title Insurance Premiums

The new TRID forms prohibit our industry, by law, from disclosing the actual cost of title insurance policies the homebuyer will pay at closing. This is the only cost disclosed at closing that the CFPB prevents consumers from receiving their actual charge.

In the majority of states, when a homebuyer purchases a lender's title insurance policy concurrently with an owner's title insurance policy, the lender's policy is typically issued at a discounted rate (often called "simultaneous issue pricing"). This discount is offered because much of the title search, examination and underwriting that goes into preparing a lender's title insurance policy also supports the owner's policy.

However, in all transactions, TRID requires lenders and/or settlement agents to disclose on the Loan Estimate and Closing Disclosure the lender's title insurance premium at its full rate even though a discount exists that benefits the homebuyer. Conversely, TRID then requires the owner's title insurance premium to be inaccurately disclosed on the forms. As the example shows below, the result is that in most states, the Closing Disclosure will not provide consumers with accurate disclosures of their title insurance costs.

The Bureau could easily resolve this issue by requiring mortgage lenders and settlement

California

Here is how the rule works when applied to a transaction where the sales price is $200,000 and there is a $190,000 loan:

The Rule	vs.	Reality
OTP on Closing Disclosure = $676.00 (OTP Premium) $902.00 (LTP Simultaneous Premium) + $409.00 (Full LTP Premium) – $635.00		**OTP Actually Charged = $902.00** (OTP Premium)
LTP on Closing Disclosure =$635.00 (Full LTP Premium, with no discounts for Simultaneous Issue)		**LTP Actually Charged = $409.00** (LTP Simultaneous Premium)

Terminology Key:
OTP: Owner's Title Insurance Policy
LTP: Lender's Title Insurance Policy

LTP Simultaneous Premium: a discounted lender's title insurance premium that is issued in accordance to promulgated state rates or insurance company filed rates when both a lender's and owner's title insurance policies are simultaneously issued

agents to disclose the actual title insurance premium rates required in the state in which the real property is located. We are not proposing to change the regulation's requirements surrounding the disclosure of title premiums on the Loan Estimate, which would require an amendment to the regulation. Rather, the Bureau can modify a section of the Official Interpretation:

Comment 38(g)(4)-2:

> In a jurisdiction where simultaneous issuance title insurance rates are permitted, any owner's title insurance premium disclosed under **§ 1026.37(g)(4) or** § 1026.38(g)(4) is calculated by using the full owner's title insurance premium~~, adding any simultaneous issuance premium for issuance of lender's coverage,~~ and then deducting ~~the full premium for lender's coverage disclosed under § 1026.38(f)(2) or (f)(3)~~ **any policy cost differences due to the simultaneous purchase of a lender's title insurance policy**.

We appreciate that the Bureau is attempting to show consumers the marginal cost of purchasing on owner's title insurance policy; however, we are greatly concerned about the confusion this approach will cause consumers. In absence of a solution, the Bureau causes our industry to inaccurately disclose consumers' costs for title insurance. This exposes ALTA

members to potential class action lawsuits and state market conduct examination errors—not to mention actively dissuades homebuyers from purchasing financial protection for their largest financial investment.

Accurately disclosing the price of title insurance policy premiums will also help the title industry comply with state regulations. Under state insurance laws, title insurance companies are only allowed to charge the policy premium rates promulgated or filed with the state. If the Bureau declines to fix this problem, our industry is likely to address this legal requirement to knowingly disclose incorrect title insurance premiums by providing a second disclosure to the homebuyer showing the actual premium cost. Our industry will need this additional disclosure to prove to state insurance regulators and potential class action plaintiffs that they were charged the correct policy rates under state insurance law. These additional disclosure forms will likely contribute to homebuyer confusion about the actual costs of their title insurance policies, closing costs and homeownership in general.

We urge the Bureau to address this issue immediately. ALTA believes that the best way to reduce homebuyer confusion regarding the disclosure of title fees under the Rule is to modify the Official Interpretations to allow industry to disclose the actual title insurance premiums on the Closing Disclosure.

Improve the way the Bureau protects consumers and works with businesses

Congress can reduce regulatory burdens to obtaining mortgage credit by improving how CFPB and regulated institutions work together to determine how to apply guidance to specific situations. While ALTA members are not directly supervised by the Bureau, we are indirectly regulated through the Bureau's oversight of both depository and non-depository mortgage lenders. Our industry is most acutely feeling the impact of CFPB Bulletin 2012-03 on service providers.[3] This bulletin restated longstanding guidance from other federal regulators about the expectation that lenders should oversee their business relationships with service providers in a manner that ensures compliance with federal consumer financial law.

While other federal regulators have promulgated voluminous and helpful guidance to both depository and non-depository mortgage lenders on how to manage the risks affiliated with third-party service providers, the CFPB's bulletin only provided lenders with two and a half pages of general guidance. This lack of guidance from the Bureau, compared to the sixteen pages of guidance in from the Office of the Comptroller of the Currency (OCC) and fourteen pages of guidance from the Federal Reserve Board in 2013, has left lenders unsure of what kind of risk management the CFPB would require of lenders and how the CFPB would enforce its expectations. Lenders are left without a clear path, and many are still feeling their way through the risk management process.

This lack of guidance has consequences for homebuyers. Recently, a Wisconsin title company talked to ALTA about their customers, Kenneth and Danielle, who were scheduled to buy a $260,000 home in the Village of Caledonia, Wisconsin, on March 15. Two days before the

[3] http://files.consumerfinance.gov/f/201204_cfpb_bulletin_service-providers.pdf

scheduled closing, the title company's closing officer received an email from a loan processor at the mortgage company. The email directed the closing officer to the website of an unknown company requesting more information before the title company could continue conducting real estate settlements for this particular mortgage lender. The website asked the closing officer to provide personal information including her Social Security Number, authorization for a credit check, name of her personal banking institution, her personal bank account number and an authorization for her bank to speak with them. A letter accompanied this request from the mortgage lender that read:

"[Our company] has been hired to conduct vendor management services on behalf of the mortgage lender for whom you are handling funds and documents. All mortgage lenders and banks are required by regulation to conduct comprehensive checks and ongoing risk monitoring of settlement agents for consumer protection and data privacy and security purposes. We thank you for assisting lenders in meeting their legal requirements to protect consumers."

When the title company contacted the mortgage lender to say that the information requested was well beyond what would be required by title insurance and settlement industry best practices, our ALTA member reported, "the mortgage lender stated that use of this vetting company was required, and our title company declined to go forward. We assume that the mortgage lender then placed their title and closing order with a different company and we know that the homebuyer's closing was delayed for several days."

Kenneth and Danielle's closing was scheduled to occur on March 15th but was delayed until 5:00 p.m. on March 19. This delay did not protect Kenneth and Danielle from financial harm. Rather, the delay was simply because a mortgage lender hired a third-party vendor, who is unregulated, to request the Social Security Number and personal bank account information of another third-party vendor [the title company], who is regulated and licensed by states department of insurance. The unregulated vendor wanted authorization to check a regulated and licensed vendor's personal credit, the name and account number of her personal banking institution, and an authorization for her bank to speak with them. This is not commonsense consumer protection – this is a regulatory burden for Kenneth and Danielle to obtain mortgage credit.

A second example is from October of 2014 when a Missouri title company received a title order from a homebuyer, John, who was refinancing his home in Chesterfield, Missouri. In order to proceed, the mortgage lender required the staff of the state-regulated and state-licensed vendor, the title company, to provide the same non-public personal information to another vendor who is not regulated, in order to process the title order. It wasn't until the Missouri title company said that they, "would resign from the transaction and contact the borrower to let them know why before [the mortgage lender] agreed to remove the requirement and allow the title company to handle the transaction."

These two examples of consumers being affected by regulatory burdens to obtain mortgage credit was not the fault of either mortgage lender. These examples show that many lenders are still operating blindly with regard to their risk management process because of a lack of guidance from the CFPB.

In the absence of this guidance, and to assist our business partners' understanding of our industry, ALTA took the lead and developed a tool in 2012 to help the industry illustrate to homebuyers and lenders the industry's professionalism and best practice standard to help ensure a positive and compliant real estate settlement experience.

Today, ALTA's Title Insurance & Settlement Company Best Practices are becoming an industry standard of prudent business practices that lenders and settlement agents are adopting as the backbone of their service provider oversight program. These Best Practices are designed to meet market demands while being flexible enough to be adopted by all companies in the title and settlement industry, regardless of business size.

The Best Practices includes the following seven pillars:

1. Establish and maintain current license(s) as required to conduct the business of title insurance and settlement services
2. Adopt and maintain appropriate written procedures and controls for Escrow Trust Accounts allowing for electronic verification of reconciliation
3. Adopt and maintain a written privacy and information security program to protect Non-public Personal Information as required by local, state and federal law
4. Adopt standard real estate settlement procedures and policies that help ensure compliance with Federal and State Consumer Financial Laws as applicable to the settlement process
5. Adopt and maintain written procedures related to title policy production, delivery, reporting and premium remittance
6. Maintain appropriate professional liability insurance and fidelity coverage
7. Adopt and maintain written procedures for resolving consumer complaints

ALTA's Best Practices have gained the support of both large mortgage lenders (like Wells Fargo and SunTrust Bank) as well as community lenders (such as BancorpSouth Bank and FirstMerit Bank).

Regulatory Reform Proposals that Improve How the Bureau Interacts with and Regulates the Title Industry

While ALTA's Best Practices provide much needed guidance to the market, more should be done by the Bureau to fill this void. More certainty form the Bureau would help business understand their regulatory obligations so that they do not feel a need to take an overly cautious approach that limits consumer choice or access to credit. This is why ALTA supports three bipartisan legislative proposals to improve not only the way the CFPB receives feedback from industry about its regulatory proposals, but also the way the CFPB provides industry with much needed guidance about its expectations regarding compliance with federal consumer financial protection law.

First, we urge the Senate to introduce and pass companion legislation to H.R. 1195 as soon as possible. This bipartisan legislation introduced in the House by Rep. Robert Pittenger

and Rep. Denny Heck would establish a small business advisory board at CFPB, similar to those established for outreach to community banks and credit unions. This advisory board would give small businesses, like Nancy McNealy's in Beltsville, Maryland, a seat at the table when the Bureau is considers additional regulations that may negatively affect her business and customers. Advisory boards provide clear, formal and open channels of communication between Bureau staff and industry. Since the Bureau only supervises depository institutions with more than $10 billion in assets, the CFPB created an advisory board for community banks and credit unions to promote regular contact with these institutions. Creating a similar advisory organization for nonbanks will allow these smaller institutions to report, advise or consult with the Bureau on a regular basis.

Second, the Senate should introduce and pass legislation that directs the CFPB to establish procedures for issuing advisory opinions to the financial service providers it regulates. The best ways to protect consumers and produce good outcomes for their financial decisions are to discourage bad acts through enforcement while at the same time to also encourage good behavior. Today, the Bureau takes its enforcement role seriously, but we encourage it to take their ability to promote good practices seriously too. An advisory opinion provides certainty to those complying with federal consumer financial law in real-life situations.

Close to 20 other federal agencies issue advisory opinions. This type of guidance, issued in response to a specific request, would improve certainty about whether a proposed design, operation or maintenance of consumer financial product would be prohibited under federal consumer law.

These advisory opinions should be made available to the public through the CFPB website. However, before publication of any advisory opinion, the CFPB should redact specific information about the requesting individuals or entities, and about any individuals or entities associated with the requestor, to the extent that is reasonable to prevent release of any confidential business information or trade secrets.

ALTA members support bipartisan advisory opinion legislative efforts that include specific timeline triggers for the CFPB to respond officially to an advisory opinion request. In addition, we support a fee structure that could be levied on the advisory opinion requestor in order to offset the additional staff the CFPB would need to complete accurate advisory opinions.

Finally, the Senate should consider actions to improve CFPB transparency in the processes used to create bulletins, guidance documents and enforcement actions. In all three instances, the CFPB does not encourage public feedback to these performed actions. Substantive or legislative rules issued by federal agencies, like the CFPB, must undergo a public notice and comment rulemaking under the Administrative Procedures Act (APA). Comments are published in a public forum to promote transparency of rulemakings. Regulations issued by the CFPB benefit from public input and feedback. Receiving public input also makes regulations more effective, resulting in fewer unintended consequences on small businesses and consumers.

Whether a comment is provided to the CFPB through a bulletin, a guidance document or an enforcement action, this feedback should be made available to the public. In many cases,

soliciting transparent public comments on an issue promotes discussion that leads to better long-term policy outcomes. Members of the United States Senate employ these tactics when they receive and respond to constituent calls and letters each day.

As you continue to consider various regulatory reforms in the coming months, please remember the stories I have shared today from Maryland, Missouri and Wisconsin. Unfortunately, these complications are replicated in real estate transactions throughout the country as our members work to comply with new state and federal laws. Thank you for the opportunity to comment on regulatory burdens to obtaining mortgage credit. ALTA is eager to serve as a resource to this Committee.

Testimony of Mark A. Calabria, Ph.D.
Director, Financial Regulation Studies, Cato Institute
Submitted to the
U.S. Senate Committee on Banking, Housing and Urban Affairs

On "Regulatory Burdens to Obtaining Mortgage Credit"
April 16, 2015

Mark A. Calabria, Ph.D. is Director of Financial Regulation Studies at the Cato Institute. Before joining Cato in 2009, he spent seven years as a member of the senior professional staff of the U.S. Senate Committee on Banking, Housing and Urban Affairs. Prior to his service on Capitol Hill, Calabria served as Deputy Assistant Secretary for Regulatory Affairs at the U.S. Department of Housing and Urban Development, and also held a variety of positions at Harvard University's Joint Center for Housing Studies, the National Association of Home Builders and the National Association of Realtors. He has also been a Research Associate with the U.S. Census Bureau's Center for Economic Studies. He holds a doctorate in economics from George Mason University. http://www.cato.org/people/mark-calabria

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Chairman Shelby, Ranking Member Brown, and distinguished members of the Committee, I thank you for the invitation to submit testimony to today's important hearing. I am Mark Calabria, Director of Financial Regulation Studies at the Cato Institute, a nonprofit, non-partisan public policy research institute located here in Washington, DC. My comments are solely my own and do not represent any official policy positions of the Cato Institute. In addition, outside of my interest as a citizen, homeowner and taxpayer, I have no direct financial interest in the subject matter before the Committee today, nor do I represent any entities that do.

Mortgage Reform and the Financial Crisis

Many, if not most, accounts of the financial crisis of 2008 include a prominent role for the U.S. residential mortgage market. While other U.S. property markets, such as commercial and retail, exhibited similar boom and bust patterns, the elevated level of defaults and associated costs borne by the taxpayer have brought a particular emphasis on American single-family mortgage finance policies. It should be of little surprise that the Dodd-Frank Act contains multiple provisions related to mortgage finance. Any attempt to return to the mortgage lending standards of 2006 would be a grave public policy mistake.

We must, however, be clear about what particular standards contributed to the crisis and which did not. Fortunately the hard-working analysts at Congress' own Government Accountability Office (GAO) have provided some objective analysis of such[1], as well as examining the potential impact

[1] See United States Government Accountability Office. 2009. *Characteristics and Performance of Nonprime Mortgages.* Report to Congress GAO-09-848R, and United States Government Accountability Office. *Nonprime Mortgages: Analysis of Loan Performance, Factors Associated with Defaults, and Data Sources.* Report to Congress, August 2010. GAO-10-805.

of Dodd-Frank's mortgage provisions[2]. What should be clear from GAO's work, which is consistent with literally dozens of academic studies[3] on mortgage default, is that the main drivers of default are borrower credit quality and borrower equity. As the Committee is aware, both the Qualified Mortgage (QM) and Qualified Residential Mortgage (QRM) rules, as implemented, essentially "punt" on these issues. Based upon GAO's analysis, my estimate is that, all else equal, the QM/QRM rules as proposed would reduce default probabilities by around 1 percentage point.[4] The simple fact is that most of the loans features addressed by QM/QRM are **not** the primary drivers of default and essentially amount to little more than rounding errors.

That estimate assumes lenders discount the significant legal risk that accompanies QM/QRM loans. As the QRM is an amendment to the 1934 Securities Act, mortgage-backed securities issues that are later determined to be non-QRM would subject the issuer to liability under SEC Rule 10b-5. Given the subjectivity in some of the documentation requirements under QRM and potential Rule 10b-5 liability, lenders can expect increased documentation and verification costs. Issuers may not possess crystal balls, but what is clear to most potential MBS issues is that non-agency pools will generate significant class actions on the part of investors during the next downturn in the housing market. While this might be great for some lawyers, it is not so great for lenders or borrowers. Such provides a powerful incentive for lenders to avoid loans with any significant risk of default, unless those loans can be passed along to the Federal Housing Administration (FHA) or the government-sponsored enterprises (GSEs), Fannie Mae and Freddie Mac.

This is perhaps the most harmful aspect of current mortgage reform efforts. The worst loans, in terms of low down-payments and low FICOs, are being passed along to entities directly backed by the taxpayer. We have a perverse

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[2] United States Government Accountability Office. 2011. Mortgage Reform: Potential Impacts of Provisions in the Dodd-Frank Act on Homebuyers and the Mortgage Market. Report to Congress, July 2011. GAO-11-656.

[3] For instance see, Hatchondo, Juan Carlos, Leonardo Martinez, and Juan Sanchez. 2011. *Mortgage Defaults*. Working Paper 2011-019A. Federal Reserve Bank of St. Louis; Bajari, Patrick, Sean Chu, and Minjung Park. 2010. *An Empirical Model of Subprime Mortgage Default from 2000 to 2007*. Federal Reserve Board of Governors Working Paper; and Christopher Foote, Kristopher Gerardi, Lorenz Goette, and Paul Willen. *Subprime Facts: What (We Think) We Know about the Subprime Crisis and What We Don't*. Federal Reserve Bank of Boston. Public Policy Discussion Papers. May 20, 2008.

[4] See Mark Calabria, "Mortgage Reform Under the Dodd-Frank Act," in *Perspectives on Dodd-Frank and Finance*, edited by Paul Schultz, The MIT Press, 2014.

mortgage finance system where a lender can only make shoddy loans if the taxpayer is placed directly on the hook. Ideally we should want the opposite, where lenders bear the bulk of the risk and the taxpayer bears little, if any.

Additionally of concern is that Dodd-Frank's Section 1413 allows borrowers an additional delay to the foreclosure process. A longer foreclosure process increases the borrower's incentive to default, which of course should be obvious and reflects little more than basic economics. Keys, Piskorski, Seru and Vig (2012) document this increase in "strategic default" during the recent crisis.[5] Dodd-Frank's Section 1414(g) notice on anti-deficiency and the increased delays to foreclosure may well increase strategic defaults more than an amount to off-set reductions resulting from the QM/QRM provisions. As Gerardi, Lambie-Hanson, and Willen (2011) have demonstrated, delays in the foreclosure process largely extend the process, raising the overall level of loans in foreclosure at any one time, without significantly improving final outcomes for the borrower.[6] Dodd-Frank could very well result in an *increase* in the level of mortgage defaults during the next housing bust, relative to the recent crisis.

Let me emphasis at this point that I am ***not*** suggesting that we "turn back the clock" on mortgage reform. What I am suggesting is that so far Congress and regulators have made the wrong reforms and left the system (and taxpayers) at even greater risk than before the crisis. While I did not advocate then nor do I now advocate such, had policy-makers done nothing, we would have been better off. The key is to actually do the correct thing.

In order to assist policy-makers in choosing the appropriate reforms, I will first briefly note some longer term objectives and then offer a few modest proposals that can be addressed in the short run.

Long term reforms

If we wish to avoid or at least minimize financial crises that are associated with housing booms and busts, we must ultimately reduce the leverage in

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[5] Keys, Benjamin, Tomasz Piskorski, Amit Seru, and Vikrant Vig. 2012. *Mortgage Financing in the Housing Boom and Bust*. National Bureau for Economic Research.

[6] Gerardi, Kristopher, Lauren Lambie-Hanson, and Paul S. Willen. 2011. *Do Borrower Rights Improve Borrower Outcomes? Evidence from the Foreclosure Process*. Federal Reserve Bank of Boston Public Policy Discussion Paper Series, paper no. 11-9, (2011).

our mortgage finance system, both on the part of the lender and the borrower. We must, as importantly better align the incentives of all participants in our mortgage market. That implies that parties that reap the up-side of risk should also bear the down-side.

In order to accomplish the preceding all existing mortgage subsidies, including FHA and the GSEs, should be eventually eliminated. These subsidies have not added significantly to the homeownership rate, but have rated induced families to take on even greater leverage. As Senator Warren noted over a decade ago, our various mortgage subsidies largely result in families simply entering "bidding wars" for homes fueled by debt.[7] Our system of mortgage finance has not offered opportunity for long-term wealth building, but rather more opportunity for long-term debt building.

Other long term reforms should include if not an outright repeal of the Consumer Financial Protection Bureau, at least some increases in its accountability to Congress (who are after all elected by the American people). Such would include changing its structure to a board that is subject to the Congressional appropriations process (as intended by our Constitution). The CFPB should also be subject to cost-benefit analysis.

Short term reforms

Exempt QM for loans held in portfolio. Occasionally the correct insight that risk and reward should be align can be found in Dodd-Frank, hence the risk retention requirements under the QRM. There is no better alignment of risk for a lender than when a lender holds that loan. Since QM applies whether a loan is sold or not, it undermines this discipline. In fact it makes it worse by encouraging a lender to sell that loan to an exempt entity, like Fannie Mae or Freddie Mac. According, Congress should exempt all mortgages held in portfolio from QM as long as those loans are held in portfolio.

Allow QM as bar to foreclosure for only material defects. Lenders should not lose the ability to foreclosures simply because a "t" wasn't crossed or an "i" dotted. Nor should a borrower be able to evade their obligations because of clerical mistakes. QM should serve as a bar to foreclosure only when a borrower has suffered material harm that has arisen as a direct result of the

[7] See Elizabeth Warren and Amelia Warren Tyagi, 2003. *The Two-Income Trap*. Basic Books, specifically pages 132 to 133.

asserted error. Better yet, simply repeal Dodd-Frank's Section 1413. As the recent crisis proved, borrowers already possess plenty of opportunities to delay.

Increase QM small loan definition. While QM should be repealed, in the interim the definition for a small loan subject to the points and fees test is simply too low to cover the increased costs resulting from Dodd-Frank and other recent regulations. While the points and fees under the test should also be raised, as suggested by the House under HR 685, I would recommend raising the small loan exemption to match the GSE conforming loan limit, since that limit is supposed to be the dividing line between mortgages for the middle class and those for the wealthy.

Actions that should be rejected

While I have some sympathy with the concerns of both consumer advocates and lenders toward the reduction in mortgage access for high risk borrowers, the solution should **not** be to reduce underwriting or pricing standards for mortgages where the taxpayer is directly at risk. Congress would be wise to mandate a reversal of the recent reduction in FHA's premium, as well as bar the GSE from making loans with down-payments below 5%, if not permanently, then as long as those entities are in conservatorship. Let us not forget the very nature of a conservator is to reduce the risk of the entity under conservatorship, which of course found itself in conservatorship due to excessive risk-taking.

Conclusions

Despite years at attempted "reform" the taxpayer remains as exposed to the mortgage market as ever. Reforms have failed to protect the taxpayer, while also unduly increasing the costs of mortgage lending. In the 1970s, the spread of the 30 year mortgage over the 10 year treasury averaged about 130 basis points. Today that spread is closer to 170 basis points. That is a cost that is directly passed along to the consumer. And this is in an environment of record low interest rates. While considerable work remains left undone in reforming our nation's mortgage finance system, I commend the Committee for considering even modest steps in the right direction.

PRESERVING FAIR STANDARDS FOR COMMUNITY LENDERS

TESTIMONY

PAULINA MCGRATH

THE COMMUNITY MORTGAGE LENDERS OF AMERICA

U.S. SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

APRIL 16, 2015

As the Chairperson of the Community Lenders of America, I am pleased to submit testimony to the Senate Committee on Banking, Housing, and Urban Affairs in connection to its hearing on Regulatory Burdens to Providing Mortgage Credit. CMLA is a trade group representing both small mortgage bankers and community banks with mortgage lending expertise.

The CMLA is pleased Congress is moving forward with regulatory streamlining for community banks, and we support those measures. However, if Congress does not provide the same streamlining for community-based, non-depository mortgage lenders this effort will fail consumers and small businesses in every part of our country.

In 2014, non-depository lenders originated approximately 40 percent of all conventional loans and roughly 50 percent of all loans insured by the Federal Housing Administration and Department of Veterans. We are a key piece of the mortgage market, especially for consumers looking to get on the first rung of the economic ladder and for those borrowers looking for, or needing, more personalized service.

Unfortunately, the current regulatory burden is driving consolidation among small mortgage lenders. If this consolidation continues, the reduced competition will lead to higher costs for borrowers and consumers will have fewer choices. As a country, we need to find a way to serve – with careful and safe underwriting – more families in their homeownership needs, particularly first-time homebuyers. If we cannot, these families will continue to pay ever-increasing rents that are outstripping income gains.

Remember: Dodd-Frank's goal was certainly to make lending safer for consumers; however, as we were told in 2009, the law was intended to regulate most closely the largest lenders and the bad actors. Subsequent experience with this statute shows it lacks the flexibility to distinguish the level of regulation necessary for lenders of different sizes, business models, and performance records. Consequently, it levies the regulatory burden on everyone, including small lenders that operate in a prudent manner, and who simply cannot amortize large fixed costs onto a relatively modest volume of mortgage lending.

We think it is important for Congress to take reasonable steps to help preserve small lenders as an important segment of the mortgage lending industry. Without these steps being taken, we are extremely concerned that the consolidation we see today will continue and consumers will face fewer choices among lenders, higher costs, and the sort of impersonal, bureaucratic service so prevalent among many larger lending organizations. Such an outcome would not, in any way, advance consumer protection.

The CMLA would like to introduce a concept that will spur more community lending while not diminishing consumer protections: why not provide some targeted relief for small lenders, which have no recent enforcement actions, and which originate primarily loans that meet the Qualified Mortgage (QM) standard contained in the Truth-in-Lending statute? Why not streamline certain regulations for these lenders, which recognizes their unique role in the lending market and benefits the borrowers whose home financing needs they serve?

We propose that lenders would receive specified relief, so long as they remained (1) small, with (2) most of their annual loan origination volume composed of QM loans, and (3) only as long as they continue their excellent lending records. (If a lender grew too large, decided to pursue a non-QM market, or received an enforcement action, it would lose the streamlined regulation.)

If Congress adopted a framework like this, it would spur more community lending while maintaining the consumer focus intended by policymakers. The consolidation and shuttering of community mortgage lenders would subside, providing consumers more choices, better pricing, and better service. This is most crucial for our country's underserved areas and communities – from the rural areas to the inner city.

What sort of streamlined regulations would make sense? The CMLA is proposing a series of regulatory changes to preserve strong consumer protections while, at the same time, providing prudent and safe regulatory relief for small and mid-sized lenders.

The first is a very straightforward, common sense type of change. Current disclosure rules require new disclosures if there is a change – for good or bad -- in fees, costs or interest rates that cause the Annual Percentage Rate (APR) of a loan to change by more than a minimal amount (prior to the close of the loan). A new disclosure must be made to the borrower and a three-day period must elapse prior to the closing of

the loan following this revised disclosure. This is an appropriate consumer safeguard when the change results in a higher APR and therefore higher costs. However, it makes no sense when the change is resulting in a lower APR and therefore lower costs to the borrower. We recommend Congress mandate that the three-day waiting period be waived when a change results in a lower APR for the borrower than previously disclosed by the lender.

Second, vendor oversight requirements are another good example of the excessive regulatory burden faced by smaller mortgage lenders. Current rules do not differentiate between large and small lenders; instead, the rules levy the same vendor oversight duties and responsibilities on small mortgage lenders as they do on large banks.

Since oversight and review of vendors are costly and onerous, smaller lenders are more likely to choose large, national vendors. This decision provides smaller lenders with greater assurance of the vendor's integrity. Nevertheless, they must vet each of these national vendors on a regular basis, duplicating oversight that takes hundreds of staff-hours per year for each lender. Moreover, the impact of these necessary business decisions means that smaller, local vendors that traditionally provided these services are being shut out and job losses in these communities are meaningful.

Third, CFPB examinations are an important enforcement tool for the Bureau with large lenders and those lenders that may have broken the rules. However, the Dodd-Frank statute does not provide clarity or prioritization for the CFPB in the marketplace.

We suggest Congress establish a statutory priority for CFPB examinations, directing the Bureau to conduct examinations of small lenders only if there has been a referral by another regulator. Small lenders are routinely examined by a number of different regulators. Small banks are examined by state banking regulators and the FDIC at a minimum. Small non-depository lenders are examined by the regulator of each state in which they operate. In addition, many small non- depository lenders are approved FHA and VA lenders, as well as by Fannie Mae and Freddie Mac, and are examined by each of these organizations. Why not say that the disproportionate CFPB exam prep costs, including mock audits, together with the costs of the actual examination, will not fall on small lenders unless a referral came from one of the existing regulators and agencies overseeing these lenders? Remember: the CFPB will still be able to go where it is most needed; the provision will help it focus its resources where these resources will truly add to consumer protection.

Fourth, the current rules around servicing provide no relief for nonbank servicers doing a good job. Nonbank lenders typically contract with a subservicer for the servicing of their loans in order to keep costs reasonable and offer a high level of service to borrowers. The CMLA proposes that Congress statutorily define the definition of small servicer. We would further propose that relief granted to small servicers meeting this statutory definition not differentiate between small servicers that perform all servicing functions internally, and those small servicers that utilize

contract subservices to keep costs low and consumer service high. Again, this streamlining would be for lenders of small size, doing QM lending, with good track records. We should not penalize these lenders solely because they use subservicers.

Please note: on these policy recommendations above, the CMLA is working closely with the Community Home Lenders Association, an association exclusively representing nonbank mortgage lenders.

Fifth, CMLA suggest an amendment to the SAFE Act regarding the licensing of loan originators. Currently loan originators employed by non-depository lenders are licensed by state regulators. Those originators must take educational courses, pass an examination conducted by the state regulator and undergo a background check. Loan originators employed by depository lenders are registered in a database maintained by Federal banking regulators. Other employment requirements are left to the discretion of the depository employer, who will usually conduct a similar background check and utilize internal or external training courses to ensure the appropriate industry knowledge among their loan originators.

In every local community across the U.S., consumers interact on a daily basis with registered and state-licensed loan originators. These originators, – regardless of which Federal or State regulatory body has oversight of their employers – perform the same tasks, working with consumers to assess their home finance needs and then taking the steps necessary to qualify the consumer for the financing that will allow them to purchase the home of their choice.

As you can appreciate, in the employment marketplace, it is a difficult process for a non-depository lender to recruit and employ a loan originator from a depository lender despite the fact of nearly identical duties and consumer interaction. Once a loan originator employed by a depository lender leaves that job and takes an identical position with a non-depository lender, usually within the same geographical market, he or she cannot originate any loans until they take the courses, and pass the examination and background check required by state regulations. By contrast, a licensed loan originator employed by a non-depository or a depository, can resign their position on a Friday and begin working for a depository as a registered loan originator the following Monday.

The CMLA proposes that Congress amend the SAFE Act to direct state regulators to issue a 180-day transitional license to a loan originator registered with an insured depository who is hired by a non-depository lender. This transitional license would allow the loan originator to continue their employment for the period of time it takes them to satisfy the state licensing requirements.

Effect of Increasing Compliance Costs

We recently conducted a survey among our members to determine the impact of increasing compliance costs. We found that compliance costs on average had increased nearly 200 percent for small lenders since 2010 on an aggregate basis and approximately 125 percent on a per loan basis. Unfortunately, some of these

costs have been passed onto consumers. Lenders have also absorbed a portion of these costs. However, to the extent the increases in these costs have made it impossible for small lenders to continue to operate economically, these smaller lenders have been forced to sell or shut down their companies, thereby continuing the reduction in consumer choices.

Obviously, a very large bank can more easily absorb compliance costs. Moreover, given recent history, there appears to be a greater need and thus justification for stronger regulation of a large bank's mortgage lending. As we saw before and during the financial crisis, large institutional lenders can drive market behavior, and their failures can have devastating financial consequences for the market. Therefore, a tighter regulatory check on their activities is amply justified.

By contrast, most small mortgage banking companies are independently owned, do not retain a loan portfolio and have no access to bank deposits to fund operations and no access to the Federal Reserve window for liquidity. Instead, our lending operations are financed by warehouse lines of credit, which cost four to eight times more than insured deposits and overwhelmingly require personal guarantees by the company owners. In effect, our lenders risk their own capital in making mortgages and thus, our lending practices and quality control constitute the primary safety net should a loan fail.

Ask yourself: how did these community lenders survive the worst downturn since the Great Depression? Although some community banks received TARP money, not one of the mortgage bankers did--yet they are still here today. How could this be? The answer is we continually and routinely executed with higher underwriting standards--and did not take advantage of our borrowers with shoddy products that provided short-term payoffs and long-term pain.

The last few years have been a struggle to continue to serve our borrowers. We are hiring more compliance and non-consumer facing personnel than ever before. Given our higher cost of funding, mortgage banking companies are more vulnerable, not less, to the higher fixed costs of legal and compliance operations mandated by Dodd-Frank. The average independent mortgage banker with up to 250 employees has increased compliance staff from two to seven according to our survey, with average annual compliance costs increasing from approximately $432,000 to $1.3 million. The problem becomes painfully evident. The cost of auditing vendors runs about $75,000 annually. The cost of preparing for a mock audit for a CFPB exam that may or may not ever come is $50,000. Since 2010, CMLA data show that compliance costs per loan have more than doubled--and this, again, is for lenders doing predominantly QM lending, which has its own built-in consumer protections.

When you consider these high fixed costs, combined with other tightening factors such as GSE buybacks, the economics of originating small-balance loans look especially challenging. The Houston Association of Realtors data on home sales in December 2014 compared to December 2013 show one way the market has been reacting:

- Sales volumes for homes below **$79,999 declined** 19.8 percent, year over year
-
- Sales volumes for homes $80,000 - **$149,999 declined** 8.1 percent, year over year
-
- Sales volumes for homes $150,000 - **$249,999 increased** 19.4 percent year over year
- Sales volumes for homes $250,000 - **$499,999 increased** 26.1 percent year over year
- Sales volumes for homes $500,000 - **$1 million+ increased** 20.4 percent, year over year

National data tell a similar story; according to NAR data, recent sales of homes in the $250,000 – 500,000 range increased 10 percent from a year ago, while homes valued at $100,000 and below declined by 10 percent, according to the NAR. Our CMLA data show a similar pattern. Some of this divergence is due to jobs and debt pressures at the lower end of the income scale, but some of the lending reflects the fixed costs for any loan and the losses that lenders may take on smaller loans. The inescapable economic fact is that lenders can recover their fixed costs in three ways – through higher fees charged to borrowers, higher interest rates or emphasizing the origination of higher balance mortgages. The first two options make it hard for consumers to buy the home of their choice because of greater out-of-pocket cash demands at closing or a higher monthly payment for the life of the loan. The third option disadvantages moderate-income borrowers and first time buyers who are typically buying smaller, lower cost homes. None of those results appears to advance the cause of consumer protection.

Some people argue that there is good reason to overlook mortgage bankers' need for regulatory relief. They say that since mortgage bankers sell all the loans they originate, and therefore have little or nothing at risk if the loans they originate perform poorly, they do not merit the same consideration.

This is patently false.

There has been a steady stream of repurchase demands issued in the aftermath of the financial crisis. Even if the repurchase demand is without merit, the costs to defend frequently outweigh the loss from the loan. This risk is quite personal to mortgage bankers, taking into account the personal guarantees and the fact that our own net worth is usually tied up in our companies. We have very, very little margin of error, and no access to federally insured funds. Our lenders did not build the business plans of their companies around the origination of Liar Loans, Exploding ARMs, NINJA loans and other toxic products then, and we certainly do not do those types of loans now. Our own money is on the line--which means our interests are aligned with that of our borrowers: carefully underwritten loans that will perform well over time.

In sum, we commend this Committee for the work to ensure community banks thrive on behalf of local consumers, who depend on us for maximum choices and to keep costs low. We urge Congress to extend meaningful regulatory relief to all small community lenders, and to find ways to empower more lending while not compromising consumer protections. Let us return to the original framework of Dodd-Frank and make regulation work for everyone.

STATEMENT OF THE CONFERENCE OF STATE BANK SUPERVISORS
On
"REGULATORY BURDENS TO OBTAINING MORTGAGE CREDIT"

Before the
COMMITTEE ON BANKING, HOUSING, & URBAN AFFAIRS
UNITED STATES SENATE
Thursday, April 16, 10:00 am
538 Dirksen Senate Office Building

INTRODUCTION

The Conference of State Bank Supervisors (CSBS) thanks Chairman Shelby, Ranking Member Brown, and distinguished Members of the Committee for the opportunity to submit a statement for the record for the hearing titled, "Regulatory Burdens to Obtaining Mortgage Credit."

CSBS is the nationwide organization of banking regulators from all 50 states, the District of Columbia, Guam, Puerto Rico, and the U.S. Virgin Islands. State banking regulators charter and supervise more than 5,000 insured depository institutions, and many state regulators also supervise a wide variety of non-bank financial services providers, including more than 16,000 mortgage companies and nearly 132,000 individual mortgage loan originators (MLOs).[1] For more than a century, CSBS has given state supervisors a national forum to coordinate supervision of their regulated entities and to develop regulatory policy. CSBS also provides training to state banking and financial regulators and represents its members before Congress and the federal financial regulatory agencies.

Thank you for holding this important hearing to consider issues related to access to mortgage credit.

In this statement, CSBS will comment on S. 372 (H.R. 1480), the SAFE Act Confidentiality and Privilege Enhancement Act and S. 871 (H.R. 1259), the HELP Rural Communities Act.

S. 372, SAFE ACT CONFIDENTIALITY AND PRIVILEGE ENHANCEMENT ACT

About the Nationwide Multi-State Licensing System and Registry (NMLS, or the System)

Almost 10 years ago, in the lead up to the financial crisis, state regulators recognized the need to oversee the mortgage industry more comprehensively and efficiently. State regulators also wanted to effectively and efficiently streamline the licensing process across state lines. For instance, regulators from neighboring states such as Alabama and Mississippi should be able to seamlessly share information and communicate regarding a financial services provider licensed

[1] Source: CSBS-AARMR Nationwide Multi-State Licensing System and Registry (NMLS), as of December 31, 2014.

in both states. Similarly, a financial services provider should enjoy a streamlined licensing process between Alabama and Mississippi, and all other states in which it is licensed to do business. Furthermore, state regulators wanted to ensure that a bad actor could not have his or her license revoked in one state, only to go set up shop in another. To achieve this simple concept, the states collectively developed an electronic system for mortgage licensing, known as NMLS. The System gives regulators the ability to keep track of bad actors and provide responsible mortgage providers with greater efficiency and consistency in the licensing process. After two years of development, state regulators launched NMLS on January 2, 2008.

When Congress sought to pursue mortgage market reform in 2008, you recognized the benefit of state supervision and NMLS and codified the System into federal law through the Secure and Fair Enforcement for Mortgage Licensing Act (SAFE Act). The SAFE Act required all residential mortgage loan originators (MLOs) be either licensed or registered through NMLS. This web-based system, administered by the states through CSBS, allows state-licensed mortgage companies, their branches, and individuals to apply for, amend, update, or renew a license online for all participating state agencies using a single set of uniform applications.

The SAFE Act also established a framework that clarified state and federal roles and a mechanism for state and federal coordination and information sharing. Under this state-federal cooperative structure, state regulators are given primary responsibility for implementing the law's requirements, with a federal agency serving as a backstop and arbiter of the SAFE Act. All 50 states, the District of Columbia, Puerto Rico, and the U.S. territories enacted laws to implement the mandates of the SAFE Act within one year of its passage. The states responded in record time to adopt NMLS, quickly putting in place a uniform and seamless system of mortgage licensing and supervision across the nation. With the success of NMLS, state regulators are increasingly able to share information across state lines and with their federal counterparts, leveraging collective resources and making the examination environment more efficient.

NMLS also serves as a resource for consumers and promotes greater transparency concerning the companies providing financial services to consumers through the NMLS Consumer Access website.[2] NMLS Consumer Access allows consumers to verify whether a mortgage lender is in fact properly licensed.

The simplicity of the concept underpinning NMLS has been essential to its success: via NMLS, a mortgage lender can easily apply for a license in one state or across multiple states using a uniform, electronic license application form. This uniformity cuts bureaucratic red tape and reduces regulatory burden for state-licensed companies with operations in numerous states. NMLS provides similar streamlining benefits for state regulators by providing back-office services. States that license the same entity are able to share pertinent information and collaborate with colleagues across state lines regarding multi-state entities, thereby reducing duplicative efforts and costs and promoting more efficient supervisory processes at state

[2] http://www.nmlsconsumeraccess.org.

regulatory agencies. NMLS complies with the Federal Information Security Management Act's (FISMA) stringent data security standards.

Expansion and Widespread Support of NMLS

NMLS was designed in a forward-thinking manner to provide functionality for all state licensing regimes. NMLS proved to be such a successful and integral regulatory tool in the mortgage licensing arena, state mortgage regulators decided to expand its use to serve as a licensing system for other state-licensed, non-bank financial services providers. Starting in April 2012, state regulators began voluntarily using NMLS on this expanded basis to include licensees such as check cashers, debt collectors, and money transmitters. As of year-end 2014, 34 state agencies were using NMLS to license money services businesses, debt, and consumer finance. In total, 61 state agencies manage 538 state license authorities through NMLS.

The expanded use of NMLS has streamlined the licensing process for both licensees and regulators. It enables licensees to manage their licenses for multiple states, while states are able to track the number of unique companies and individuals, as well as the number of licenses they hold in each state. As a system of record for state regulatory authorities and a central point of access for licensing, NMLS brings greater uniformity and transparency to these non-depository financial services industries while maintaining and strengthening the ability of state regulators to monitor these industries.

Non-bank financial services companies have also supported the efficiencies that NMLS provides. In a June 2012 House Financial Services Committee hearing on money services businesses, industry representatives testified that widespread adoption of NMLS "would eliminate duplication of effort and opportunities for error" and "urge[d] any changes at the federal level to accommodate and encourage its further development."[3] In another House Financial Services Committee hearing that same month, appraisers, money transmitters, and regulators alike testified to their interest in using NMLS as a licensing platform.[4]

Federal regulators have also benefitted from NMLS efficiencies and are examining advantages to expanded use in other non-mortgage industries. In fact, the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) specifically required the Consumer Financial Protection Bureau (CFPB, or the Bureau) to consult state agencies on existing state registration systems when developing and implementing its own registration requirements.[5] The CFPB has turned to state regulators and NMLS on numerous occasions. Last year, the CFPB was able to use information from NMLS in a proposed rule entitled

[3] Timothy P. Daly, Senior Vice President, Global Public Policy, The Western Union Company. Hearing before the Subcommittee on Financial Institutions and Consumer Credit of the Committee on Financial Services, U.S. House of Representatives, 112th Congress, Second Session, Serial No. 112-139, 49-50 (June 21, 2012). Available at http://financialservices.house.gov/uploadedfiles/hhrg-112-ba15-wstate-tdaly-20120621.pdf.

[4] Subcommittee on Insurance, Housing, and Community Opportunity: "Appraisal Oversight: The Regulatory Impact on Consumers and Businesses," Printed Hearing 112-140 (June 28, 2012). Available at http://financialservices.house.gov/calendar/eventsingle.aspx?EventID=300543.

[5] 12 U.S.C. § 5512(c)(7) and 12 U.S.C. § 5514(b)(7).

"Defining Larger Participants of the International Money Transfer Market."[6] Taking advantage of state-federal information sharing agreements, the CFPB used data that had been collected by the states on money transmitters to perform an analysis of money transmitters. This is exactly the kind of efficient and cooperative supervisory data sharing that state regulators originally envisioned and NMLS now enables. In November 2013, the CFPB issued an Advanced Notice of Proposed Rulemaking on debt collection practices, which specifically sought comments on using NMLS if it were ever to require registration of debt collectors.[7] State regulators appreciated that the CFPB identified NMLS as a potential registration database. As the CFPB contemplates registration requirements of various regulated entities, NMLS is an obvious solution that can efficiently meet regulators' needs while avoiding duplication.

Enhanced Privilege and Confidentiality Protections for an Expanding NMLS

Given the desire for expanded use of NMLS among non-depository financial services companies, state regulators, and other stakeholders, the introduction of S. 372 comes as a very welcome development. The SAFE Act currently provides that information shared through NMLS among mortgage industry regulators retains existing state and federal privilege and confidentiality protections. Neither the SAFE Act nor S. 372 creates any additional privilege or confidentiality rights. Under the SAFE Act, information contained in NMLS retains whatever privilege and confidentiality protections the information enjoyed prior to being entered into NMLS, as long as that information is shared through NMLS among mortgage regulators.

We will use the Alabama State Banking Department (the Department) as an example. Since the Department has the authority to license and supervise entities and individuals involved in mortgage lending, it is considered a mortgage industry regulator, and any regulatory information the Department shares with other mortgage industry regulators through NMLS retains all legal protections related to confidentiality and privilege. However, if another state regulator wants to use NMLS to license a certain category of non-depository companies and that state regulator is *not* a mortgage regulator, it is not clear that the SAFE Act's protections for privilege and confidentiality would apply. In that instance, if the Department needed to share licensing or other regulatory information through NMLS with that other state regulator, that regulator might not be bound to comply with and honor the privilege and confidentiality protections that the Department must follow.

This possible gap limits the states' ability to use NMLS as a licensing system for non-mortgage financial services providers. The change proposed by S. 372 addresses this uncertainty and would provide the Department and its regulated entities with certainty that confidential or privileged information shared through NMLS would continue to be protected under state and federal law.

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[6] Bureau of Consumer Financial Protection. "Defining Larger Participants of the International Money Transfer Market (CFPB 2014-0003)." Federal Register. Vol. 79, No. 21, p. 5316.
[7] Bureau of Consumer Financial Protection. "Debt Collection (Regulation F) (CFPB 2013-0033) " Federal Register. Vol. 78, No. 218, p. 67879.

It is important to note that S. 372 does not create any privilege or new licensing or registration requirements through NMLS. The bill simply allows for existing confidentiality or privilege to continue when regulatory information concerning the expanded financial services industries is shared among state and federal regulators through NMLS. It also provides regulated entities with additional assurance that their sensitive information housed in NMLS retains existing legal protections related to privilege and confidentiality.

Authority to Process Criminal Background Checks through NMLS

In the SAFE Act, Congress mandated that MLOs undergo background checks as part of the licensing process. The Federal Bureau of Investigation (FBI) warehouses the most comprehensive and reliable database of criminal record information from both state and federal law enforcement agencies, and facilitates background checks on their behalf. The process is simple: when an individual is required to undergo a background check, he or she submits fingerprints, which are then sent to the FBI. The FBI pulls the individual's criminal history, and then sends it back to the state via NMLS.

To make this process more efficient, the SAFE Act designates CSBS as a "channeler" – an approved company that acts as an intermediary in the fingerprinting and background check process – in the mortgage context. As a channeler, CSBS streamlines an otherwise lengthy process and makes it efficient. A potential MLO scans his or her fingerprints at just one location. The FBI generates that individual's criminal record and passes it to NMLS, which then directs the information to the relevant state licensing agency.

State law often requires background checks on other non-mortgage licensees, and a similar background check arrangement would need to be in place for successful NMLS expansion. Legislation was introduced last Congress (H.R. 5320) to enable the NMLS to process these background checks in the same manner that background checks are processed for mortgage industry applicants. CSBS is working with Members of the Senate and House on re-introduction of this legislation and request the Committee's support. Action on this issue, combined with passage of S. 372, will support and facilitate state regulators' efforts to provide efficient and effective regulation through expanded use of NMLS.

S. 871, THE HELP RURAL COMMUNITIES ACT

As state regulators, our members have a locally-oriented perspective on regulated entities and the communities they serve. S. 871 supports the ability of community banks to provide mortgage credit by creating greater flexibility to meet local needs.

Certain aspects of lending and the regulation of that lending should include an element of flexibility. S. 871, by establishing a locally-focused petition process for identifying rural communities for purposes of the rural balloon loan Qualified Mortgage (Balloon QM), creates such needed flexibility.

State regulators have identified portfolio lending as a key opportunity for policymakers to ensure community banks' ability to contribute positively to the economic well-being of their local markets. This includes responsibly underwritten balloon loans and flexibility for escrow account services, important factors for credit in markets across the country. S. 871 helps ensure that portfolio lending product options are available in rural areas, including balloon loans. Importantly, to ensure the rural designation process includes local input, S. 871 creates a process for local stakeholders to petition the CFPB for an area to be considered rural.

As you know, CSBS supported Congressman Barr's and Senator McConnell's previous bills on this subject, introduced in the 113th Congress. We note that earlier this year, the CFPB, in response to extensive feedback, proposed changes to the rural designation process. CSBS strongly supports those measures.

CSBS has long-standing policy that regulations should not hinder a bank's willingness to engage in portfolio lending. The CFPB's proposal creates greater opportunities for lenders in rural areas to meet the needs of their communities. The proposed changes correctly acknowledge the aligned interest between small creditors that portfolio mortgage loans with consumer protection, and recognizes the strong incentives portfolio lenders have to consider a borrower's ability to repay a loan. S. 871 complements these proposed changes by creating yet another tool to provide for appropriate flexibility in identifying rural areas.

CSBS and our members see a need for policymakers to continue to efforts to ensure we have a right-sized and appropriate regulatory framework that meets the needs of local communities and that recognizes the relationship-lending business model. Portfolio lending aligns the interests of consumers and lenders, warranting a regulatory framework that supports originate-to-hold mortgage lending.

Finally, we appreciate that S. 871, like H.R. 1259, provides an opportunity for state bank supervisors to provide input into the petition review process. State regulators will bring a perspective that reflects not just local knowledge, but a responsibility for economic development and for fostering competitive and robust financial markets.

As the CFPB continues to implement its mortgage rules and Congress evaluates proposed changes, state regulators stand ready to help ensure processes are in place to properly consider the differences between local areas. CSBS applauds Senators McConnell, Heller, Capito, and Paul for sponsoring S. 871 and urges swift passage of the bill.

CONCLUSION

As locally based and locally accountable regulators, state banking regulators continually strive for better ways to regulate the diverse system of financial services businesses that serve our communities and consumers. State regulators' proximity to both businesses and consumers and their diverse regulatory portfolio gives them a unique perspective on local credit needs and the role of flexibility and regulatory efficiency in promoting sound business

practices and responsible lenders, reducing regulatory burden, and strengthening consumer protection. These two bills recognize the essential role state regulators play in non-depository supervision and in ensuring fair access to mortgage credit in all communities of the United States.

Thank you for the opportunity to submit a statement for the record.

Habitat for Humanity®

Habitat. We build.

April 15, 2015

The Honorable Richard Shelby
United States Senate
304 Russell Senate Office Building
Washington, DC 20510

Dear Mr. Chairman:

Thank you for convening today's hearing regarding Regulatory Burdens to Obtaining Mortgage Credit. As a nationwide mortgage lender and advocate for broadening access to mortgage credit, this issue is of critical importance to Habitat affiliates, their partner families, and the communities where they work.

Habitat for Humanity's vision is a world where everyone has a decent place to live. Anchored by the conviction that housing provides a path out of poverty, Habitat has helped more than 5 million people since 1976 through home construction, rehabilitation and repairs, and by increasing access to improved shelter through products and services. Habitat also advocates to improve access to decent and affordable shelter and offers a variety of housing support services that enable families with limited means to make needed improvements on their homes as their time and resources allow. As a nonprofit Christian housing organization, Habitat works in more than 70 countries and has more than 1,400 local affiliates here in the United States.

Many people are familiar with Habitat's construction work but may not know that a no-interest mortgage lending model is at the core of Habitat's work in the United States. Last year, Habitat originated approximately 5,500 mortgage loans in the U.S. While the Dodd-Frank legislation and resulting regulations were crafted primarily with large financial institutions in mind, as mortgage lenders, local Habitat affiliates throughout Alabama (where there are 33) and around the nation are subject to the vast majority of federal mortgage regulations. Achieving compliance with new regulations has been a difficult and costly challenge to our US affiliates, many of which have no paid staff and raise just enough money to build a couple of houses each year.

Habitat for Humanity International and Habitat affiliates around the country are fully committed to providing Habitat partner families with high quality, low-cost loans that are fully compliant with all applicable federal and state regulations, and the Habitat network has undertaken significant efforts to build the systems, staffing, and knowledgebase necessary to achieve this. Habitat has also worked productively with Director Cordray and his team at the Consumer Financial Protection Bureau (CFPB) to identify a few regulations

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that are clearly inapplicable to Habitat in light of its unique model. Unfortunately, a few regulations remain that promise significant increases in costs, reducing the numbers of families Habitat serves without resulting in better quality loans or performance. New regulations governing appraiser independence are a notable example.

Appraisals are critically important both for homeowners to know the value of their purchase and for Habitat affiliates to structure their mortgages properly. Many Habitat affiliates are fortunate to have relationships with generous appraisers who are willing to donate their appraisals for Habitat homes. Under new appraiser independence regulations, however, appraisers must receive reasonable compensation for their work, potentially adding hundreds of dollars in cost to thousands of Habitat homes each year.

While the appraiser independence rule makes sense in a for-profit environment, where there is an incentive for collusion, there is virtually no risk of appraiser-lender collusion with Habitat loans, because Habitat affiliates make no profit on their loans and typically charge no interest and sell their homes for far less than their appraised values. No Habitat partner family carries a mortgage with a payment of more than 30 percent of monthly income. The interests of Habitat affiliates, who nearly always hold their own mortgages, are fully aligned with those of their partner families, on whose success affiliates depend for their own ability to serve more families. Even so, this new regulation will prevent Habitat affiliates from being able to accept donated appraisals, increasing development costs and resulting in fewer families in Habitat homes.

With housing markets in some areas of the country continuing to lag and with fewer first-time buyers able to qualify for mortgages, homeownership opportunities offered by Habitat have never been more important to lower income home buyers and to the economies of the communities in which they live. Without action by Congress, however, Habitat affiliates will be forced to serve fewer families in order to pay appraisers fees they do not wish to collect and that will not improve the quality or performance of Habitat loans in any way.

Sen. Portman has generously offered to lead a bi-partisan effort to address this narrow but potentially costly problem. I look forward to working closely with you, Sen. Portman, Sen. Brown, and any senator with an interest in Habitat's work to protect Habitat's ability to receive these appraisals and apply the savings to extending access to credit to households with few, if any, other opportunities to achieve homeownership.

GOVERNMENT RELATIONS AND ADVOCACY OFFICE: [illegible]

ADMINISTRATIVE HEADQUARTERS: [illegible]

INTERNATIONAL HEADQUARTERS: [illegible]

Habitat for Humanity®

Habitat. We build.

Thank you for your consideration. Please do not hesitate to contact me if I may be of assistance in any way.

Sincerely,

Christopher Ptomey
Director, Government Relations

GOVERNMENT RELATIONS AND ADVOCACY OFFICE: 1424 K Street NW, Suite 600 Washington, DC 20005
ADMINISTRATIVE HEADQUARTERS: 270 Peachtree St. NW, Suite 1300, Atlanta, GA 30303-1263 USA
INTERNATIONAL HEADQUARTERS: office 322 W. Lamar St., Americus, GA 31709, mail 121 Habitat St., Americus, GA 31709-3498 USA
229-924-6935 toll free 800-422-4828 fax 229-928-8811 habitat.org

Senate Banking Committee Hearing
"Regulatory Burdens to Obtaining Mortgage Credit"
Housing Policy Council Written Statement for the Record
April 16, 2015

The Housing Policy Council (HPC) of the Financial Services Roundtable appreciates the opportunity to submit this statement on "Regulatory Burdens to Obtaining Mortgage Credit." The members of HPC are committed to a strong and stable housing finance system. HPC member companies originate, service and insure mortgages. We estimate that HPC members originate approximately 75 percent and service two-thirds of all mortgages in the United States.

The market for mortgage credit has improved significantly since the financial crisis. The members of HPC have contributed to this improvement in a number of ways. Member companies have assisted and continue to assist at-risk homeowners through participation in loss mitigation programs and foreclosure prevention efforts, including those coordinated by the HOPE NOW Alliance. HPC members also have implemented the major new mortgage-related regulations issued by the CFPB that are intended to correct problems in loan origination and servicing that contributed to the financial crisis. Additionally, HPC members continue to work with the GSEs and FHA on changes and updates to standards and practices that will further enhance the availability of mortgage credit.

Yet, despite record low interest rates for mortgage credit, the market has not recovered to pre-crisis and pre-housing bubble levels, especially for first-time homebuyers and low- and moderate-income homebuyers. This is a result of many factors, including the overall state of the economy. Continued job growth and overall growth in the economy remains a key to a full recovery in housing demand and mortgage credit. There are regulatory factors that are impacting the availability of mortgage credit and contributing to the current state of the mortgage market, and they are discussed below.

1. Modifications to Policies of the GSEs and FHA are Needed

HPC members continue to be concerned about the regulatory and legal risks and costs associated with mortgage lending. The risks and associated costs of loan put-backs are one of the main causes of the tightening of mortgage credit. This is especially true for FHA loans and loans sold to the GSEs, as there is continuing uncertainty related to put-back risk associated with these loans. That is the risk that FHA or the GSEs would require an institution to repurchase the loan based on some error in underwriting.

Recent modifications by the GSEs and FHFA in representations and warranties standards have helped to address this put-back risk but more needs to be done. The new standards include a sunset period for repurchase demands, which is an important improvement. Additionally, the GSEs have stated that this year they will finalize an arbitration framework and non-repurchase

remedies. HPC supports the improvements that have been made to date and continues to work closely with FHFA and the GSEs on this effort.

The FHA, on the other hand, has made much less progress in strengthening and clarifying its repurchase policies, and that is causing significant concern in the industry as lenders are exposed to much risk for loans that may not perform for reasons unrelated to loan underwriting. We urge the FHA to finalize its rules on defects, appropriate remedies, and a third-party dispute resolution system.

HPC believes that setting reasonable and workable representations and warranties standards that can be enforced by both lenders and FHA or GSEs would eliminate much of the risk that currently exists and would facilitate more responsible mortgage lending. Until these changes are made, lenders exercise an over-abundance of caution, which is harming consumers who want to purchase a home, especially those who are self-employed or are first-time homebuyers. HPC wants to work with FHA on these modifications to its representations and warranties policies, as these changes will help increase access to mortgage credit.

A recent analysis by Laurie Goodman of the Urban Institute highlighted the issues affecting the availability of mortgage credit. That analysis found that there are three main factors that have led to creditors restricting mortgage credit: "(1) uncertainty over when and why the GSEs or the FHA will put the credit risk of a loan back to its lender for violating their underwriting or servicing rules, (2) heightened litigation and related reputational risk, and (3) the high and variable cost of servicing delinquent loans."[1] Improving these repurchase policies will reduce risks and related costs and thus contribute to more availability of mortgage credit.

As the FHFA, GSEs, and FHA continue to improve these standards, we ask the agencies and entities to coordinate their efforts. To be clear, we do not advocate that these parties should issue identical policies, as FHA has a different mandate than the GSEs; however, coordination can and should be improved.

2. Need for Regulatory Clarity

a. The CFPB Should Issue Clarifications through APA Notice-and-Comment

[1] Laurie Goodman, *Servicing is an Underappreciated Constraint on Credit Access*, Urban Institute (Dec. 16, 2014) (http://www.urban.org/UploadedPDF/2000049-Servicing-Is-an-Underappreciated-Constraint-on-Credit-Access.pdf). See also, Laurie Goodman, Jun Zhu, & Taz George, *The Impact of Tight Credit Standards on 2009-13 Lending*, Urban Institute (Apr. 2, 2015) (http://www.urban.org/UploadedPDF/2000165-The-Impact-of-Tight-Credit-Standards-on-2009-13-Lending.pdf); Laurie Goodman, Jim Parrott, & Jun Zhu, *The Impact of Early Efforts to Clarify Mortgage Repurchases*, Urban Institute (Mar. 12, 2015) (http://www.urban.org/UploadedPDF/2000142-The-Impact-of-Early-Efforts-to-Clarify-Mortgage-Repurchases.pdf).

The Housing Policy Council and its members continue to work diligently to ensure that the mortgage regulations issued by the CFPB as a result of the Dodd-Frank Act are executed correctly.

Many of these regulations, including rules on assessing a consumer's ability to repay and the definition of a Qualified Mortgage as well as several new requirements for mortgage servicers became effective in January 2014. These rules are well-intended, but are having some unintended consequences. They also are raising questions that complicate compliance and create additional caution in new lending. In addition, the industry is working hard to implement the TILA-RESPA Integrated Disclosure rule (TRID) by August 1st and are finding ambiguities and issues in that rule that need to be resolved. The new disclosure regime should be monitored closely and enforced fairly during its initial implementation phase.

Some of these ambiguities and questions could be resolved by a more transparent regulatory process. The CFPB has issued several amendments to the Title XIV mortgage rules, but more clarification is needed. While the CFPB has engaged in webinars regarding TRID and other mortgage rules and made staff available for phone calls, the lenders need more clarity and certainty with regards to these interpretations by the Bureau.

Oral conversations and webinars do not provide the required certainty to resolve ambiguities and do not produce confidence in lenders that they are interpreting the Bureau's directions on underwriting criteria and other regulations accurately. It is possible that many lenders have different conversations with CFPB staff on one issue and find themselves with different interpretations. That easily leads to confusion or unequal treatment of consumers and that is not a result that lenders or the CFPB desire. Furthermore, courts, who in the future may be called upon to determine whether lenders have met the requirements under TILA and RESPA, would not be likely to defer to webinar statements as definitive guidance and this also increases the risks for lenders that rely on unwritten guidance.

The unintended consequences are most evident in the implementation of the Ability-to-Repay/Qualified Mortgage rule and the impending TRID rule. While the industry works towards the August 1st deadline to implement TRID, issues remain that need to be addressed in a rulemaking. Additionally, concerns remain with the Ability-to-Repay/Qualified Mortgage rule's Appendix Q, including burdensome documentation requirements for self-employed borrowers and rental income. For example, requirements to provide third-party prepared year-to-date profit and loss statements and balance sheets for the businesses of self-employed borrowers are an unreasonable burden as these are not produced in the ordinary course of business. Appendix Q does not allow add-backs for amortization, casualty losses, business use of home, and farming subsidies, which understates self-employed income relative to a GSE analysis. Appendix Q also penalizes the contributions of self-employed borrowers to pension and profit sharing plans

relative to IRA and Keogh plan contributions from other wage earners. The documentation standards for rental income are internally inconsistent, with conflicting requirements for current leases for all rental income and prohibitions on the inclusion of seasonal rental property income. These issues needlessly negatively impact credit-worthy consumers, especially those who are small business owners or self-employed.

HPC believes that these ambiguities and unintended consequences should be addressed through Administrative Procedure Act ("APA") notice-and-comment rulemakings. APA rulemaking will better ensure that ambiguities are clarified with certainty that allows the regulated entities to have confidence that they are acting in accordance with the regulations.

We urge the CFPB to provide interpretations and clarifications on the mortgage regulations utilizing the APA notice-and-comment procedure. All parties involved need to have a clear understanding of the regulations, and the elimination of ambiguities is critical to the success of these mortgage rules. This is especially necessary for TRID, which involves many intricacies and impacts many parties, including lenders, software vendors, closing agents, real estate agents, title companies, and consumers. It is imperative that every party involved have the same interpretation of the regulation to avoid customer confusion or an inadvertent violation of the law.

This clarity and certainty will help lenders offer and originate more loans, especially to consumers who may be near the outer edge of the QM safe harbor standards.

Finally, on a more general level, when the CFPB is creating new policy, we urge the agency to use APA notice-and-comment rulemaking. As the Bipartisan Policy Center noted in its report on the CFPB in 2013:

> Although guidance may be easier for a regulator to issue than a rule, since guidance may avoid the full formal notice-and-comment period mandated by the [APA], guidance issued without input from consumers and marketplace participants can be ineffective and often does not provide the clarity needed for covered entities to effectively comply, leading to adverse results for both consumers and covered entities.[2]

Policy-making through enforcement actions does not provide the industry with enough insight and understanding of the CFPB's concerns and objectives. A recent CFPB enforcement action concerning marketing services agreements (MSAs) and the applicability of RESPA is

[2] Bipartisan Policy Center, *The Consumer Financial Protection Bureau: Measuring the Progress of a New Agency* (Sept. 2013) (http://bipartisanpolicy.org/library/consumer-financial-protection-bureau/).

causing some concern in the mortgage industry.[3] The enforcement action contains language about MSAs that conflict with long-standing interpretations of RESPA. Similarly, lenders have recently been surprised by novel interpretations of terms under HMDA. If CFPB is seeking to change these long-standing interpretations that should be done through APA notice-and-comment.

When addressing ambiguities in existing rules or setting new policy, the CFPB should follow APA notice-and-comment procedure; the resulting policies and regulations will be improved due to this transparent process and opportunity for all stakeholders, including the industry and consumers, to provide input. The certainty that will come from these regulations will help increase mortgage availability.

b. Monitoring the Impact of Regulations

We ask that CFPB continue to monitor the impact of the mortgage regulations, and issue clarifications or modifications as needed. Under Dodd-Frank, the CFPB must evaluate the impact of each significant rule or order five years after it is effective.[4] This assessment must address the effectiveness of the rule in meeting the goals of the Consumer Financial Protection Act and the stated goals of the CFPB, and it should "reflect available evidence and any data that the Bureau reasonably may collect."[5] We ask that CFPB adopt a similar practice as the prudential financial regulators follow under EGRPRA, in which they issue several notices for public comment and hold meetings on the existing rules and areas for improvement. HPC stands ready to work with the CFPB to ensure these mortgage rules are implemented properly and achieve the stated goals.

Assessing the impact of the CFPB's regulations is an important oversight role of the Senate Banking Committee, and we appreciate hearings such as this one which highlight the impact of these rules. We ask the Committee to continue this diligent and thoughtful oversight of the CFPB and the mortgage rules.

3. The Volume and Complex Nature of Mortgage Regulations

a. Title XIV Regulations

The mortgage rules issued under Title XIV of Dodd-Frank are incredibly complex and detailed. The complex nature of the rules, coupled with the tight statutory deadlines, has created

[3] *In the Matter of: Lighthouse Title, Inc.*, Administrative Proceeding File No. 2014-CFPB-0015 (Sept. 30, 2014) (http://files.consumerfinance.gov/f/201409_cfpb_consent-order_lighthouse-title.pdf).
[4] 12 U.S.C. § 5512(d).
[5] 12 U.S.C. § 5512(d)(1).

a significant amount of confusion. The nature and scope of the issues that these rules address often have required such complex rules. The Bureau has issued several amendments to the Title XIV rules. For example, regarding the Ability-to-Repay/Qualified Mortgage rule, the CFPB issued three amendments in 2013 to the rule. Three other amendments were issued regarding the Title XIV mortgage servicing rules, also in 2013. All of those rules went into effect in January 2014. The sheer volume of the rules alone has caused many in the industry to tighten underwriting standards, even more so than what the rules actually require.

These regulations, as well as additional requirements under the National Mortgage Settlement, have contributed to a significant increase in the cost of mortgage servicing. The costs of servicing non-performing loans have risen almost twice as fast as those for performing loans. According to Laurie Goodman of the Urban Institute, the average industry costs of servicing performing loans increased more than two and a half times, from $59 in 2008 to $156 in 2013.[6] By contrast, the overall costs of servicing nonperforming loans increased nearly five-fold, from approximately $482 in 2008 to $2,357 in 2013. This negatively impacts the availability of mortgage credit and lenders' appetite for mortgage loans. Lenders are wary of lending outside the Qualified Mortgage space as non-QM loans come with greater risks and costs, both regulatory and legal.

b. TRID

In addition, the impending changes under TRID are massive and are causing genuine concern in the industry. The effectiveness of TRID and its implementation depends on many different parties including loan originators, software vendors, real estate agents, title insurance agents, settlement companies and other service providers. August 1st is rapidly approaching and our members are concerned about whether correct implementation will occur given the scale of changes and the number of parties involved. This concern could very well lead to additional tightening of credit and significant delays in origination and closing.

To help ease these concerns, we ask the CFPB to be mindful of the significant efforts the industry is undertaking to meet the August 1st deadline. We ask the CFPB to recognize good faith efforts to comply as the agency oversees implementation of TRID. This consideration of good-faith efforts should extend to supervisory exams and any future enforcement actions that concern these beginning months under the new TRID regime. This relief from administrative enforcement should be provided in writing to assure lenders and to avoid undue credit tightening and delays in origination and closing.

We also believe the CFPB needs to engage in educational efforts for parts of the mortgage industry it does not supervise, but which are important participants in the home sale

[6] Laurie Goodman on Servicing, *supra* note 1.

and closing process, and are directly affected by TRID including real estate agents. It is imperative that all parties involved in a real estate transaction understand the new rules of the road and their role.

c. Moving Forward

As noted above, the industry is focused on successful implementation of the Title XIV mortgage rules and TRID. In addition to these rules, our members are anticipating CFPB's final rule under HMDA, which will include many new data gathering and significant reporting requirements for lenders.

The CFPB has now completed and implemented all mortgage rules with a statutory deadline under the Dodd-Frank Act. As the CFPB considers additional rulemakings, we ask the CFPB to create an open dialogue with all interested parties and engage in all available tools, including SBREFA and advanced notice of proposed rulemakings under APA. These processes will lead to rules that are more understandable and transparent, and less likely to cause confusion and negatively impact consumers. Additionally, considering fewer issues at a time, rather than the massive regulations the CFPB has issued in the past few years under Dodd-Frank, may be of benefit to all parties involved. We also suggest that CFPB engage with the industry for trial implementations, in which the lenders start complying with new rules without regulatory or legal exposure for a reasonable period of time. Trial implementations will help the CFPB and the industry understand what parts of rules work well and what needs adjusting before full implementation. Additionally, CFPB should recognize the need for "iterative" rulemakings, in which updates and amendments to rules are inevitable as issues and ambiguities are discovered. Similarly, the inevitable ambiguities and conflicts in the rules should be addressed through written guidance.

Adopting these practices will ensure that the rules CFPB issues achieve their stated goals and the goals of the CFPB itself – to ensure "that all consumers have access to markets for consumer financial products and services and that markets for consumer financial products and services are fair, transparent, and competitive."[7]

The Housing Policy Council appreciates the Committee's consideration of our views. Our members want to work constructively with regulators and the Committee to ensure that the mortgage market is stable and safe and allows credit worthy borrowers to obtain a mortgage and enjoy the benefits of homeownership. Thank you.

[7] 12 U.S.C. § 5511(a).

ICBA
INDEPENDENT COMMUNITY
BANKERS of AMERICA®

April 16, 2015

Legislation Needed to Restore Community Bank Mortgage Credit

On behalf of the more than 6,000 community banks represented by ICBA, thank you for convening today's hearing on "Regulatory Burdens to Obtaining Mortgage Credit." New mortgage rules, including rules that have not yet become effective, are restricting community bankers' ability to extend mortgage credit. Both anecdotal and empirical data clearly illustrate the impact. ICBA is pleased to take this opportunity to submit the following statement for the record, which substantiates our concerns and outlines recommended legislative solutions contained in our Plan for Prosperity.

Customer Impact: Compelling Anecdotal Evidence

As the only national trade association that exclusively represents community banks, ICBA hears from hundreds of community bankers from across the country about their real world experience in implementing a multitude of complex new mortgage rules. Cited below are testimonials from bankers across the country. In many cases, creditworthy, long-term customers were turned away because new mortgage rules deny community bankers the flexibility and the discretion to serve them. These testimonials are representative of what ICBA hears from community bankers.

- A community banker from upstate New York, reports the hardest mortgage to make now is to a self-employed small business owner. An entrepreneur's greatest source of capital is usually the equity in their home. However, the self-employed often have difficulty complying with the income documentation requirements under the Consumer Financial Protection Bureau's (CFPB's) ability-to-repay rule, despite having excellent credit. The New York community banker had to decline a $30,000 first mortgage application from a 20-year customer because he couldn't satisfy rigid income documentation requirements. This community banker would have liked to support a local business owner by making a loan he believed to safe and sound.
- Low dollar loans are typical in many parts of the country for purchase or refinance of residential properties. However, the fees on these loans, though low in absolute terms, often exceed the QM fee caps. The bank's cost to make a low dollar loan is the same as its cost to make a higher balance loan. A community banker from Ohio offers this example: a $75,000 loan with an 80 percent loan-to-value ratio and a cash-out feature. The lender might wish to serve this customer by holding the loan in portfolio as a QM loan, but the closing fee for a loan in this dollar range is capped at $3,000, which is less than the lender's cost of underwriting and processing the loan. As a result, a creditworthy borrower would be unable to receive the loan from his local bank because the banker has little flexibility. Ironically, the

lender could transfer the loan to Fannie Mae or Freddie Mac, which would confer automatic QM status, but their fees would exceed $4,000, in addition to the originator's fee. In this example, QM, far from protecting the customer, would cause him to pay significantly more or be denied access to the loan altogether.

- A community banker in Texas recently had to decline a mortgage for a realtor with 30 years of experience in his field because, having relocated, he did not have enough paystubs from his new employer. This happens time and again with teachers, doctors, pharmacists, and other professionals who relocate to new towns. A creditworthy borrower shouldn't have to rent, and possibly be forced into a 12-month lease, because they don't have enough paystubs to qualify for a mortgage. Community bankers need more flexibility to work with relocated customers.
- While CFPB rules provide special accommodations for "rural lenders," banks that serve both rural and non-rural markets, as defined by the Census Bureau, are effective denied "rural lender" status, which requires that they lend "predominantly" in rural areas. As a matter of demographics and arithmetic, such lenders generate most of their mortgage volume and higher loan balances in their suburban, exurban, or urban markets. They fail the CFPB's rigidly-defined "rural lender" test, even under the agency's proposed expansion of the "rural" definition. It doesn't matter that such a bank may be the only lender serving its rural markets. Beginning in 2016, only a "rural lender" can obtain QM status for balloon loans, a staple of rural lending that protects the lender from interest rate risk on loans that are not eligible for transfer to the secondary market. The vast majority of community banks will not assume the heightened legal liability of non-QM lending. In addition, "non-rural" community banks are deterred from mortgage lending because they cannot provide costly escrow services. ICBA believes that this problem is best solved by elimination of the "predominantly" rural limitation and any references to "rural" in the Truth in Lending Act.
- A New Mexico community banker reports limited availability of mortgage credit in his community is keeping would-be homeowners in the rental market and has driven up rental costs significantly. In his community, an average renter now pays $800 to $900 a month, though he or she could purchase a more appealing home for $80,000 with a monthly mortgage payment of $400. This banker believes the disparity between rents and mortgage payments is directly attributable to the overly stringent underwriting required by new mortgage rules.

These are not isolated anecdotes. They are well supported by a number of empirical studies.

Surveys & Data Analysis Confirm Anecdotal Accounts

In ICBA's 2014 Community Bank Lending Survey, which surveyed over 500 community banks nationwide, 73 percent of survey respondents cited the regulatory burden of new rules and requirements as the most significant barrier to making more residential mortgage loans, more than any other factor including lack of borrower demand, competition from bank and non-bank lenders, or lack of qualified borrowers.[1] A significant percentage of survey respondents, 15 percent, are considering an exit or have already exited this line of business. These results are consistent with a survey conducted by the Independent Bankers Association of Texas (IBAT), just before the ability-to-repay rules became effective in 2014, 13 percent of respondents said they would stop making mortgage loans in response to the new regulatory landscape, and 53 percent of respondents said they would limit the types of mortgages they offer.[2]

For many community banks, mortgage lending is a side product rather than a core component of their business. For example, they may offer mortgage credit that strengthens their relationships with small business customers, originating 50 or fewer mortgages a year. It is these banks that are most likely to exit the mortgage business altogether in response to higher regulatory costs. Though they offer relatively few mortgages, their mortgage lending may be important to their local real estate market and critical to their relationship banking model. In the IBAT survey, 30 percent of respondents said that if they stopped or curtailed their mortgage activity, there were no other banks in their area to fill the void.

In a survey conducted by the Conference of State Bank Supervisors (CSBS), before the QM rule became effective, "15 percent of active mortgage lenders noted 80 percent or more of their 1-to-4 family mortgage loans would not meet QM requirements." The most frequently cited reasons for non-compliance were the DTI cap and the bar on balloon payment loans made by "non-rural" lenders.[3] At the same time, according to ICBA's 2014 Community Bank Lending Survey, only 25 percent of respondents are actively providing non-QM loans. These results indicate a significant unmet demand for non-QM loans. QM has effectively shrunk the credit box, stranding borrowers without access to credit. In the ICBA survey a majority of respondents, 57 percent, reported tighter underwriting in residential mortgage lending and 44 percent reported decreases in originations.

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[1] ICBA 2014 Community Bank Lending Survey

[2] "Texas Community Bank Response to CFPB Mortgage Rules." Compiled by the Independent Bankers Association of Texas. 2014.

[3] "Community Banking in the 21sth Century. Opportunities, Challenges and Perspectives." Federal Reserve System & Conference of State Bank Supervisors. September 2014.

Industry Consolidation, Driven By Regulatory Costs, Will Harm Borrowers

This statement has emphasized the direct impact of regulatory burden on borrowers, where new rules prohibit or make infeasible the offering of certain products and services. However, the lender impact of escalating compliance costs will also affect borrowers. Many community banks report compliance costs have grown from approximately five percent of overhead ten years ago to 15 to 20 percent today. This increase in regulatory burden has likely contributed to the decrease of 1,342 community banks in the United States since 2010. The number of banks with assets below $100 million shrunk by 32 percent, while the number of banks with assets between $100 million and $1 billion fell by 11 percent.[4] Banks need more scale to accommodate higher regulatory costs.

Unfortunately for borrowers, consolidation will result in fewer and more commodified product choices and higher costs. The impact will be particularly severe in rural areas that depend on community banks to provide customized financial products. If consolidation continues apace, certain rural areas may be left without access to mortgage credit at all.

Legislative Solutions Are Needed

The good news is that there are readily available legislative solutions to this pending crisis. Working with community bankers from across the nation, ICBA developed its Plan for Prosperity, a platform of legislative recommendations designed to provide meaningful relief for community banks and allow them to thrive by doing what they do best – serving customers and growing their communities. Each provision of the Plan was crafted to preserve and strengthen consumer protections and safety and soundness. I encourage the members of this Committee to review the Plan, which is attached to this statement.

Key provisions of the Plan for Prosperity are designed to keep community banks in the business of mortgage lending and to give them more flexibility in extending credit. Plan provisions include:

- "Qualified mortgage" status under the CFPB's ability-to-repay rules for any mortgage originated and held in portfolio for at least three years by a lender with less than $10 billion in assets.
- An exemption from any escrow requirements any first lien mortgage held in portfolio by a lender with less than $10 billion in assets.

The principal rationale for these provisions, and the reason they can be safely enacted, is they apply only to loans originated and held in portfolio by community banks. As relationship lenders, community bankers are in the business of knowing their borrowers and assessing their ability to repay a loan. What's more, when a community bank holds a loan in portfolio it holds 100 percent of the

[4] Parsons, Richard J. "Bank Think," The American Banker (February 16, 2015).

credit risk and has an overriding incentive to ensure the loan is well underwritten and affordable to the borrower. In a typical community bank portfolio, even a small number of defaults can put a bank at risk. Community bank portfolio lenders ensure they understand the borrower's financial condition and structure the loan accordingly. If the borrower has trouble making payments due to job loss or other unforeseen circumstances, a community bank portfolio lender will work with the borrower to restructure the loan and keep the borrower in their home. Community bank portfolio lenders will protect their collateral by ensuring borrowers remain current on tax and insurance payments. For this reason, the escrow requirement, which must be outsourced at a relatively high cost by community banks with a low volume of mortgages, is an unnecessary burden when a loan is held in portfolio.

ICBA is pleased these important portfolio QM and escrow provisions are included in the **Community Lending Enhancement and Regulatory Relief Act of 2015 (the "CLEAR Act", S. 812)**, introduced by Senators Jerry Moran and Jon Tester. S. 812 also includes a third provision: relief from the SOX 404(b) internal control assessment mandate for community banks with less than $1 billion in assets. ICBA urges the members of this Committee to cosponsor S. 812 and we urge its provisions be included in any regulatory relief measure emerging from this Committee.

Thank you again for convening today's hearing and for the opportunity to submit this statement. ICBA looks forward to working with this Committee to craft legislation to restore the flow of mortgage credit.

ATTACHMENTS

- ICBA Plan for Prosperity. January 2015

ICBA
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Plan for Prosperity

A Pro-Growth Agenda to Reduce the Onerous Regulatory Burden on Community Banks and Empower Local Communities

2015

Plan for Prosperity: An Agenda to Reduce the Onerous Regulatory Burden on Community Banks and Empower Local Communities

America's 6,500 community banks are vital to the prosperity of the U.S. economy, particularly in smaller towns and rural communities. Providing more than half of all small business loans under $1 million, as well as customized mortgage and consumer loans suited to the unique characteristics of their local communities, community banks serve a vital role in ensuring the economic recovery is robust and broad based, reaching communities of all sizes and in every region of the country.

In order to reach their full potential as catalysts for entrepreneurship, economic growth, and job creation, community banks must be able to attract capital in a highly competitive environment. An end to the exponential growth of onerous regulatory mandates is critical to this objective. Regulation is suffocating nearly every aspect of community banking and changing the very nature of the industry away from community investment and community building to paperwork, compliance, and examination. A fundamentally new approach is needed: Regulation must be calibrated to the size, lower-risk profile, and traditional business model of community banks.

ICBA's Plan for Prosperity provides targeted regulatory relief that will allow community banks to thrive by doing what they do best – serving and growing their communities. By reducing unsustainable regulatory burden, the Plan will ensure that scarce capital and labor resources are used productively, not sunk into unnecessary compliance costs, allowing community banks to better focus on lending and investing that will directly improve the quality of life in our communities. Each provision of the Plan was selected with input from community bankers nationwide and crafted to preserve and strengthen consumer protections and safety and soundness.

The Plan is a set of detailed legislative priorities positioned for advancement in Congress. A subset of these priorities is specifically dedicated to strengthening community bank viability by creating new options for capital raising and capital preservation. A number of regulatory relief measures would be tiered, with different thresholds for Consumer Financial Protection Bureau rules (generally $10 billion and under) and safety and soundness regulation (generally $50 billion and under). The recommended thresholds are based on existing levels and statutory provisions, which may vary by provision.

ICBA is committed to advancing and enacting the provisions of the Plan with all due vigilance and the aggressive use of every resource at our disposal. The Plan is a flexible, living document that can be adapted to a rapidly changing regulatory and legislative environment to maximize its influence and likelihood of enactment. Provisions are described below.

ACCESS TO CAPITAL: CREATING NEW OPTIONS FOR THE CREATION AND PRESERVATION OF COMMUNITY BANK CAPITAL

ICBA is proposing a set of options to strengthen community bank viability by enhancing access to capital.

Basel III Amendments: Restoring the Original Intent of the Rule. Basel III was originally intended to apply only to large, internationally active banks. ICBA proposes the following amendments for banks with assets of $50 billion or less.

- *Exemption from the capital conservation buffer.* The new buffer provisions impose dividend restrictions that have a chilling effect on potential investors. This is particularly true for Subchapter S banks whose investors rely on dividends to pay their pro-rata share of the bank's tax. Exempting community banks from the capital conservation buffer would make it easier for them to raise capital.
- *Full capital recognition of allowance for credit losses.* Provide that the allowance for credit losses is included in tier 1 capital up to 1.25 percent of risk weighted assets with the remaining amount reported in tier 2 capital. This change would reverse the punitive treatment of the allowance under Basel III. The allowance should be captured in the regulatory capital framework since it is the first line of defense in protecting against unforeseen future credit losses.
- *Amend risk weighting to promote economic development.* Provide 100 percent risk weighting for acquisition, development, and construction loans. Under Basel III, these loans are classified as high volatility commercial real estate loans and risk weighted at 150 percent. ICBA's proposed change would treat these loans the same as other commercial real estate loans and would be consistent with Basel I.

Additional Capital for Small Bank Holding Companies: Modernizing the Federal Reserve's Policy Statement. Require the Federal Reserve to revise the Small Bank Holding Company Policy Statement – a set of capital guidelines that have the force of law. The Policy Statement, which makes it easier for small bank and thrift holding companies to raise additional capital by issuing debt, would be revised to increase the qualifying asset threshold from $1 billion to $5 billion. Qualifying bank and thrift holding companies must not have significant outstanding debt or be engaged in nonbanking activities that involve significant leverage.

Relief from Securities and Exchange Commission Rules. ICBA recommends the following changes to SEC rules which would allow community banks to commit more resources to their communities without putting investors at risk:

- Provide an exemption from internal control attestation requirements for community banks with assets of less than $1 billion. The current exemption applies to any company with market capitalization of $75 million or less. Because community bank internal control systems are monitored continually by bank examiners, they should not have to sustain the unnecessary annual expense of paying an outside audit firm for attestation work. This provision will substantially lower the regulatory burden and expense for small, publicly traded community banks without creating more risk for investors.

- Due to an oversight in the 2012 JOBS Act, thrift holding companies do not have statutory authority to take advantage of the increased shareholder threshold below which a bank or bank holding company may deregister with the SEC. Congress should correct this oversight by allowing thrift holding companies to use the new 1,200 shareholder deregistration threshold as well as the new 2,000 shareholder registration threshold.
- Regulation D should be reformed so that anyone with a net worth of more than $1 million, including the value of their primary residence, would qualify as an "accredited investor." The number of non-accredited investors that could purchase stock under a private offering should be increased from 35 to 70.

TARGETED REGULATORY RELIEF

Supporting a Robust Housing Market: Mortgage Reform for Community Banks. Provide community banks relief from certain mortgage regulations, especially for loans held in portfolio. When a community bank holds a loan in portfolio, it has a direct stake in the loan's performance and every incentive to ensure it is properly underwritten, affordable and responsibly serviced. Relief would include:

- Providing "qualified mortgage" safe harbor status for loans originated and held in portfolio by banks with less than $10 billion in assets, including balloon mortgages.
- Exempting banks with assets below $10 billion from escrow requirements for loans held in portfolio.
- An exemption from the higher risk mortgage appraisal requirements for loans of $250,000 or less provided they are held in portfolio by the originator for a period of at least three years.
- New information reporting requirements under the Home Mortgage Disclosure Act should not apply to community banks.

Strengthening Accountability in Bank Exams: A Workable Appeals Process. The trend toward oppressive, micromanaged regulatory exams is a concern to community bankers nationwide. An independent body would be created to receive, investigate, and resolve material complaints from banks in a timely and confidential manner. The goal is to hold examiners accountable and to prevent retribution against banks that file complaints.

Reforming Bank Oversight and Examination to Better Target Risk. ICBA makes the following recommendations to allow bank examiners to better target their resources at true sources of systemic risk:

- A two-year exam cycle for well-rated community banks with up to $2 billion in assets would allow examiners to better target their limited resources toward banks that pose systemic risk. It would also provide needed relief to bank management for whom exams are a significant distraction from serving their customers and communities.
- Banks with assets of $50 billion or less should be exempt from stress test requirements.
- Community banks should be allowed to file a short form call report in the first and third quarters of each year. The current, long form call report would be filed in the second and fourth quarters. The quarterly call report now comprises some 80 pages supported by almost 700 pages of instructions. It represents a growing burden on community banks without being an effective supervisory tool.

Redundant Privacy Notices: Eliminate Annual Requirement. Eliminate the requirement that financial institutions mail annual privacy notices even when no change in policy has occurred. Financial institutions would still be required to notify their customers by mail when they change their privacy policies, but when no change in policy has occurred, the annual notice provides no useful information to customers and is a needless expense.

Balanced Consumer Regulation: More Inclusive and Accountable CFPB Governance. The following changes would strength CFPB accountability, improve the quality of the agency's rulemaking, and make more effective use of its examination resources:

- Change the governance structure of the CFPB to a five-member commission rather than a single Director. Commissioners would be confirmed by the Senate to staggered five-year terms with no more than three commissioners affiliated with any one political party. This change will strengthen accountability and bring a diversity of views and professional backgrounds to decision-making at the CFPB.
- The Financial Stability Oversight Council's review of CFPB rules should be strengthened by changing the vote required to veto a rule from an unreasonably high two-thirds vote to a simple majority, excluding the CFPB Director.
- All banks with assets of $50 billion or less should be exempt from examination and enforcement by the CFPB; and CFPB backup (or "ride along") authority for compliance exams performed by a bank's primary regulator should be eliminated.

Eliminate Arbitrary "Disparate Impact" Fair Lending Suits. Amend the Equal Credit Opportunity Act and the Fair Housing Act to bar "disparate impact" causes of action. Lenders that uniformly apply neutral lending standards should not be subject to frivolous and abusive lawsuits based on statistical data alone. Disparate impact forces lenders to consider factors such as race and national origin in individual credit decisions, which are specifically precluded by law.

Ensuring the Viability of Mutual Banks: New Charter Option. The OCC should be allowed to charter mutual national banks to provide flexibility for institutions to choose the charter that best suits their needs and the communities they serve.

Rigorous and Quantitative Justification of New Rules: Cost-Benefit Analysis. Provide that financial regulatory agencies cannot issue notices of proposed rulemakings unless they first determine that quantified costs are less than benefits. The analysis must take into account the impact on the smallest banks which are disproportionately burdened by regulation because they lack the scale and the resources to absorb the associated compliance costs. In addition, the agencies would be required to identify and assess available alternatives including modifications to existing regulations. They would also be required to ensure that proposed regulations are consistent with existing regulations, written in plain English, and easy to interpret.

Cutting the Red Tape in Small Business Lending: Eliminate Burdensome Data Collection. Exclude banks with assets below $10 billion from new small business data collection requirements. This provision, which requires the reporting of information regarding every small business loan application, falls disproportionately upon community banks that lack scale and compliance resources.

Preserve Community Bank Mortgage Servicing. The provisions described below would help preserve the important role of community banks in servicing mortgages and deter further industry consolidation, which is harmful to borrowers:

- Increase the "small servicer" exemption threshold to 20,000 loans (up from 5,000). To put this proposed threshold in perspective, the average number of loans serviced by the five largest servicers subject to the national mortgage settlement is 6.8 million. An exemption threshold of 20,000 would demarcate small servicers from both large and mid-sized servicers.
- For banks with assets of $50 billion or less, reverse the punitive Basel III capital treatment of mortgage servicing rights (MSRs) and allow 100 percent of MSRs to be included as common equity tier 1 capital.

Creating a Voice for Community Banks: Treasury Assistant Secretary for Community Banks. Economic and banking policies have too often been made without the benefit of community bank input. An approach that takes into account the diversity and breadth of the financial services sector would significantly improve policy making. Creating an Assistant Secretary for Community Banks within the U.S. Treasury Department would ensure that the more than 6,500 community banks across the country, including minority banks that lend in underserved markets, are given appropriate and balanced consideration in the policy making process.

Modernize Subchapter S Constraints. Subchapter S of the tax code should be updated to facilitate capital formation for community banks, particularly in light of higher capital requirements under the proposed Basel III capital standards. The limit on Subchapter S shareholders should be increased from 100 to 200; Subchapter S corporations should be allowed to issue preferred shares; and Subchapter S shares, both common and preferred, should be permitted to be held in individual retirement accounts (IRAs). These changes would better allow the nation's 2,200 Subchapter S banks to raise capital and increase the flow of credit.

Five-Year Loss Carryback Supports Lending During Economic Downturns. Banks with $15 billion or less in assets should be allowed to use a five-year net operating loss (NOL) carryback. The five-year NOL carryback is countercyclical and will support community bank capital and lending during economic downturns.

Risk Targeting the Volcker Rule. Exempt banks with assets of $50 billion or less from the Volcker Rule. The Volcker Rule should apply only to the largest, most systemically risky banks. Proposals to apply the rule to community banks carry unintended consequences that threaten to destabilize segments of the community banking industry.

The Independent Community Bankers of America®, the nation's voice for 6,500 community banks of all sizes and charter types, is dedicated exclusively to representing the interests of the community banking industry and its membership through effective advocacy, best-in-class education and high-quality products and services. For more information, visit www.icba.org.

Written Testimony for the Record

By

Mr. Nathan Smith
Chairman, Manufactured Housing Institute

Before the
Committee on Banking, Housing, and Urban Affairs
U.S. Senate

Hearing on
REGULATORY BURDENS TO OBTAINING MORTGAGE CREDIT

April 16, 2015
Washington, DC

2111 Wilson Blvd. Suite 100 Arlington, VA 22201 Tel: 703.558.0400 Fax: 703.558.0401
http://www.manufacturedhousing.org info@mfghome.org

Thank you, Chairman Shelby, Ranking Member Brown, and Members of the Committee for the opportunity to offer written testimony about the regulatory burdens facing consumers seeking mortgage credit for manufactured housing.

The Manufactured Housing Institute (MHI) is the national trade organization representing all segments of the factory-built housing industry. MHI members include home builders, lenders, home retailers, community owners, suppliers and others affiliated with the industry. MHI's membership includes 50 affiliated state organizations.

Manufactured housing is a key source of quality, affordable housing for more than 22 million Americans. Manufactured housing plays an important role in providing reliable, sustainable housing for current and future homeowners looking to meet a variety of housing and lifestyle needs. Manufactured housing is a highly-regulated industry, with three distinct qualities: manufactured homes are safe, they are energy efficient and they are affordable.

Manufactured housing's affordability means it has long been the housing choice for many low- and moderate-income families, including retirees on fixed incomes and first-time homebuyers. Homes are commonly available at lower monthly payments than what it costs to rent. According to the U.S. Census Bureau, in 2013 the average price of a manufactured home was $43,000 (compared to $177,000 for a site-built home). In addition, the average cost per square foot of a manufactured home was $44 compared to almost $94 for a site-built home. Almost three quarters of families living in manufactured homes have annual incomes less than $40,000 (Foremost Market Study, 2012).

Manufactured homes serve many housing needs in a wide range of communities—from rural areas where housing alternatives (rental or purchase) are few and construction labor is scarce and/or costly (nearly two of three manufactured homes are located in rural areas), to higher-cost metropolitan areas as in-fill applications.

The manufactured housing industry has always been fully committed to protecting consumers throughout the home buying process. MHI recognizes the importance of responsible lending and improving the consumer experience.

Manufactured Housing Consumers are Being Harmed by Current Federal Regulations

Current regulations are unfairly penalizing retirees, veterans, rural residents and working families who otherwise would not have access to affordable homeownership. They are being shut out of the market for quality, non-subsidized, affordable housing because the CFPB rules have caused financing to be unavailable for manufactured homes. Existing owners are harmed since their home values are suffering due to the inability of potential buyers to obtain financing, forcing owners to sell to cash buyers at prices that are only a fraction of the home's market value.

High-Cost Mortgage Definition

The recent high cost mortgage regulations have jeopardized access to manufactured housing financing, disrupted the market, and as a result caused eroding home values for existing owners. The rules have penalized home buyers that cannot access traditional mortgage financing needed for single-family home ownership or live in rural areas where affordable rental or site-built housing is scarce or non-existent.

Additionally, many at-risk families have seen the equity they have diligently built up in their manufactured homes wiped out because lenders are not providing the financing needed for resale due to these regulations.

Many community owners have said that their tenants are having to sell their homes well below market value to cash buyers, because potential buyers cannot find financing. For example, after living in a manufactured home community for 20 years, an elderly couple from Butler County, Ohio[1] needed to move to a condo because they could no longer take care of the yard work. While there were interested buyers, they could not find anyone who could find a loan to purchase the home at the appraised value ($25,000). After a year of waiting, they were finally forced to sell the home for $5,000 cash, which was a loss of $20,000.

There are countless examples like the couple from Butler County, Ohio, taking place in manufactured housing communities across the country where existing homeowners are trapped and have no way to move up, move on or move out. The result is a decrease in the family's assets, net worth and financial well-being. Below-market sales do not just hurt the sellers, they hurt every home owner in the community who experiences a significant loss in the equity of their home and in their net worth when a home sells at a fire sale price. These are real homes owned by real families. These are people who are impacted by the regulations implemented from the Dodd-Frank Act.

At issue are the new HOEPA triggers; current limits are too low to reflect the economics of originating and servicing small balance manufactured home loans. Because costs are calculated as a percentage of loan amount, smaller loan sizes (like loans for manufactured homes) automatically violate points and fee caps. This causes smaller-sized manufactured home loans to be categorized as "high-cost" or predatory under HOEPA, even though there is nothing predatory about the features of the loan.

Due to the increased lender liability associated with the "high-cost" mortgage designation, some manufactured housing lenders have stopped making manufactured home loans. Others have stopped originating manufactured home loans under $20,000. There are no manufactured housing lenders making HOEPA loans as a matter of business practice. As a result, there is a lack of credit availability at the lower end of the income spectrum, which is devastating working family balance sheets and harming consumers seeking affordable housing.

Mortgage Originator Definition

Consumers of manufactured housing have been ill-served by what is effectively a "gag order" placed on retailers of manufactured homes because of the mortgage loan originator (LO) definition. The regulations create confusion for consumers, who are unable to make an informed decision regarding where to send their credit application. Many lenders do not offer loan programs for manufactured housing, and those that do may only offer specific types of loan programs (i.e. land/home loans only, FHA Title II only, VA only, etc). The rules are confusing and unclear to the point that – the retailer is essentially left with the choice of: (1) providing the consumer with no information; or (2) taking on the risk of not complying with the rules by providing information that could be useful to the consumer (ex. "This lender only does VA loans" or "This lender does not make loans that are not secured by real property.") As a result, a consumer must spend a great deal of time and energy searching for a lender,

[1] Two-thirds of Butler County adults age 25 and over have no associate, bachelors, or master's degree or higher, http://development.ohio.gov/files/research/C1010.pdf

and could send in multiple applications and receive multiple denials without finding the lender that actually offers the financing that meets their individual circumstances.

In addition to consumer confusion, lenders are at risk of having their loans deemed to violate QM and HOEPA if a retailer's sales compensation is later deemed to be LO comp and included in the points and fees calculation. This could lead to scenarios where lenders are held liable years later for violating HOEPA caps based on the well-intentioned actions of a retailer if the retailer's activities are somehow found to be enough to constitute some level of LO activity. As a result, lenders have stopped making manufactured housing loans because of this potential liability that has been created by the new regulations.

S. 682, the Preserving Access to Manufactured Housing Act

Earlier this year, Senators Donnelly, Toomey, Manchin, and Cotton introduced the *Preserving Access to Manufactured Housing Act* (S. 682) to address regulations that are reducing the ability of consumers to obtain mortgage financing for manufactured homes.

High-Cost Mortgage Definition

S. 682 modifies the definition of "high-cost" loans so that manufactured home loans are not unfairly swept under this designation simply due to their small size. This is needed because many lenders have stopped making manufactured home loans since the loans are now considered "high-cost" under the Home Ownership and Equity Protection Act (HOEPA).

The proposed statutory change would more accurately take into account the price pressures unique to manufactured home lending while still maintaining significant consumer protection from predatory lending practices. The terms typically associated with manufactured home loans—namely fixed interest rates, full amortization, and the absence of alternative features (such as balloon payments, negative amortization, etc.)—allow them to satisfy the requirements of what the Dodd-Frank Act would consider conservative and prudent underwriting standards. In addition, existing regulatory requirements and additional statutory guidelines outlined in the Dodd-Frank Act provide significant consumer protections and disclosures while prohibiting many predatory loan features. These provisions ensure that substantial protections are available to consumers without having to subject a majority of manufactured home loans to the onerous HOEPA "high-cost mortgage" designation.

Mortgage Originator Definition

S. 682 also clarifies that manufactured home retailers and their employees are not considered Loan Originators (LOs) under Consumer Financial Protection Bureau (CFPB) guidelines, provided they receive no compensation for performing LO activities.

Similar to real estate agents, manufactured home retailers and salespersons are compensated from the sale of a home and not from originating loans. The sales compensation paid to retailers and their employees is not tied to LO activities, as defined by CFPB, because: (1) the sales compensation is not paid by lenders; (2) the amount and type of sales compensation is not dependent on whether a home is purchased with cash or financing, lender incentives, or loan terms; and (3) the compensation is clearly for sales services that are not loan origination activities. Just as a real estate agent's sales commission

does not make them an LO under CFPB rules, a similar distinction is needed for those selling manufactured homes.

S. 682 excludes manufactured housing retailers and salespersons from the definition of a loan originator, so long as they are only receiving compensation for the sale of the home. This is the same standard applied to real estate agents selling site-built houses. The legislation would preserve existing requirements that an individual selling manufactured homes be licensed as a mortgage originator if they receive compensation from a lender, mortgage broker or mortgage originator for loan origination activity.

Conclusion

MHI appreciates the opportunity to share its point of view concerning the impact of regulatory burdens on mortgage credit for manufactured housing. We urge the Committee to work expeditiously to pass S. 682, The Preserving Access to Manufactured Housing Act. These are modest modifications, but they are much needed to alleviate the challenges facing working families seeking quality affordable housing and families currently living in manufactured housing. We are eager to work with the Committee to reduce the regulatory burdens harming consumers in rural America seeking to purchase or sell a manufactured home.

April 15, 2015
Sent on behalf of Gary Acosta

Below please find NAHREP's statement which we would like entered into the record and appreciate being shared with Chairman Shelby and Ranking Member Brown in advance of the Thursday hearing at 10AM.

Dear Chairman Shelby and Ranking Member Brown:

We write to you today in advance of tomorrow's hearing entitled "Regulatory Burdens to Obtaining Mortgage Credit" to urge you to focus some of your attention on the 15 percent of Hispanic consumers who are excluded by the outdated credit scoring models required by the GSEs who could have access to mortgage credit if newer, more inclusive scoring models are employed by lenders. We also want to thank you for addressing such an important topic in this hearing and hope to continue to be a part of the dialogue on this and other issues going forward.

By way of background, the National Association of Hispanic Real Estate Professionals (NAHREP) is The Voice for Hispanic Real Estate and proud champions of homeownership for the Hispanic community with over 20,000 members across the country. NAHREP is a purpose-driven organization that is propelled by a passionate combination of entrepreneurial spirit, cultural heritage and the advocacy of its members. Our mission is to advance sustainable Hispanic homeownership. NAHREP accomplishes its mission by – (1) Educating and empowering the real estate professionals who serve Hispanic home buyers & sellers, (2) Advocating for public policy that supports the trade association's mission, and (3) Facilitating relationships among industry stakeholders, real estate practitioners and other housing industry professionals.

As you consider some of the hurdles that consumers face in obtaining a mortgage, there is a particularly vulnerable set of potential mortgage borrowers we urge you to consider – unscored consumers who the traditional models prevent from even being considered for a mortgage. Currently, through their seller-service guidelines, the GSEs "lock-in" models based on outdated data from the 1990s – needlessly excluding millions of creditworthy borrowers from the mortgage market. Newer, more inclusive models can generate a score for 98% of consumers with credit files at the three credit reporting companies, including 30-35 million consumers typically not scored by conventional models.

VantageScore Solutions recently examined the impact that adoption of its most recent model would potentially have were it to be accepted by the GSEs. Based on acceptable industry assumptions, 144,000 new households could access mortgage credit and a 32 percent increase in mortgage lending to minorities based on 2013 can be achieved.

Moreover, according to our 2014 State of Hispanic Homeownership Report, the rate of Hispanic homeownership last year was 45 percent, the lowest rate in 15 years and significantly below the 50 percent rate seen prior to the Great Recession. In overall figures, the number of net homeownership gains declined from an increase of 347,000 in 2012 to a notably smaller increase of just 54,000 in 2014. According to government data, Hispanic mortgage applicants were twice more likely than white applicants to be denied a loan from a GSE in 2014.

We urge you in the strongest terms to look into the effect this has on minority populations and millennials given their use of technology, their lifestyles, and demographic trends across the country, and recognizing that these consumers do not use credit the same way as previous generations.

NAHREP supports strong underwriting guidelines and sustainable homeownership and wants to ensure that the right consumers are qualifying for mortgages – not any consumer. But all consumers, including minority groups, should have the opportunity to be evaluated by a potential lender and should not be excluded by outdated models.

We respectfully ask that you include this letter and its attachments in the record of the hearing. Again, we thank you for tackling this enormously important issue and look forward to continuing our dialogue.

Sincerely,

Gary Acosta

Gary Acosta
Co-founder & CEO

591 Camino de la Reina | Suite 720 | San Diego, CA 92108
Office 858-622-9046 | Mobile 619-723-7376
Email gacosta@nahrep.org | Website www.nahrep.org

3138 10th Street North
Arlington, VA 22201-2149
P: 703.842.2234
F: 703.522.0594
chunt@nafcu.org

Carrie R. Hunt
Senior Vice President of Government Affairs
and General Counsel

National Association of Federal Credit Unions | www.nafcu.org

April 15, 2015

The Honorable Richard Shelby
Chairman
U.S. Senate Committee on Banking,
Housing, and Urban Affairs
534 Dirksen Senate Office Building
Washington, D.C. 20510

The Honorable Sherrod Brown
Ranking Member
U.S. Senate Committee on Banking,
Housing, and Urban Affairs
534 Dirksen Senate Office Building
Washington, D.C. 20510

Re: Regulatory Burdens to Obtaining Mortgage Credit

Dear Chairman Shelby and Ranking Member Brown:

On behalf of the National Association of Federal Credit Unions (NAFCU), the only trade association exclusively representing our nation's federally chartered credit unions, I write today to submit comments in conjunction with tomorrow's full committee hearing: "Regulatory Burdens to Obtaining Mortgage Credit." We thank you for holding this important hearing.

While credit unions did not participate in the widespread proliferation of subprime loans that led to the financial crisis, they are subject to new rules and requirements in mortgage lending that emerged from the crisis. In 2013, the Consumer Financial Protection Bureau (CFPB) implemented eight new mortgage rules, seven of which were finalized in October of 2013 and were effective by January of 2014. A majority of credit unions are small financial institutions which operate with a limited staff. It is a struggle for them to keep abreast with the constantly changing regulations and growing regulatory burden. Congressional and regulator action to provide relief and assistance in the areas outlined in this letter will assist credit unions in providing mortgage credit to their 100 million members.

Qualified Mortgages

NAFCU continues to have serious concerns about the "Qualified Mortgage" (QM) standard. In short, given the unique member-relationship credit unions have, many make good loans that work for their members that don't fit into all of the parameters of the QM box and fall into the "non-qualified mortgage" category. NAFCU would support the changes outlined below to the QM standard to make it more consistent with the quality loans credit unions are already making.

Points and Fees

NAFCU strongly supports bipartisan legislation to alter the definition of "points and fees" under the "ability-to-repay" rule. NAFCU has taken advantage of every opportunity available to educate and discuss with the CFPB on aspects of the ability-to-repay rule that are likely to be problematic for credit unions and their members. While credit unions understand the intention of the rule and importance of hindering unscrupulous mortgage lenders from entering the

marketplace, it is time for Congress to address unfair and unnecessarily restrictive aspects of this CFPB rule.

NAFCU supports exempting from the QM cap on points and fees: (1) affiliated title charges, (2) double counting of loan officer compensation, (3) escrow charges for taxes and insurance, (4) lender-paid compensation to a correspondent bank, credit union or mortgage brokerage firm, and (5) loan level price adjustments which is an upfront fee that the Enterprises charge to offset loan-specific risk factors such as a borrower's credit score and the loan-to-value ratio.

Making important exclusions from the cap on points and fees will go a long way toward ensuring many affiliated loans, particularly those made to low- and moderate-income borrowers, attain QM status and therefore are still made in the future.

Loans Held in Portfolio
NAFCU supports exempting mortgage loans held in portfolio from the QM definition as the lender, via its balance sheet, already assumes risk associated with the borrower's ability-to-repay.

40-year Loan Product
Credit unions offer the 40-year product their members often demand. To ensure that consumers can access a variety of mortgage products, NAFCU supports mortgages of duration of 40 years or less being considered a QM.

Debt-to-Income Ratio
NAFCU supports Congress directing the CFPB to revise aspects of the 'ability-to-repay' rule that dictates a consumer have a total debt-to-income (DTI) ratio that is less than or equal to 43 percent in order for that loan to be considered a QM. This arbitrary threshold will prevent otherwise healthy borrowers from obtaining mortgage loans and will have a particularly serious impact in rural and underserved areas where consumers have a limited number of options. The CFPB should either remove or increase the DTI requirement on QMs.

CFPB's Definition of Rural Area
NAFCU supports S. 1916, the *Helping Expand Lending Practices in Rural Communities Act*, introduced by Leader McConnell. This bill would be helpful to small creditors, including credit unions, as they deal with the CFPB's "rural area" definition particularly as it relates to the ability-to-repay rule.

We are also pleased that the CFPB has taken steps to improve its small creditor exemptions, but aspects of the proposal remain problematic. We believe the CFPB must go farther than its arbitrary definition of small creditor and recognize that all credit unions are small creditors. We would encourage the Bureau to use its authority under Section 1022 of the *Dodd-Frank Act* and exempt all credit unions from the burdensome mortgage rules.

TILA/RESPA

Dodd-Frank directed the CFPB to combine the mortgage disclosures under the *Truth in Lending Act* and *Real Estate Settlement Procedures Act*. Under this mandate, the Bureau, in November of 2013, released the integrated disclosures rule. This 1900-page rule requires a complete overhaul of the systems, disclosures, and processes currently in place for a consumer to obtain a mortgage. For example, the rule mandates the use of two disclosures: the three-page Loan Estimate (which replaces the Good Faith Estimate and initial Truth in Lending Disclosure); and the five-page Closing Disclosure (which replaces the HUD-1 and final Truth in Lending disclosure). There are also a number of stringent timing requirements and other substantive changes lenders must follow. The rule is effective August 1, 2015, but lenders are still feeling pressure to be compliant on time. The sheer magnitude of this rule, read in conjunction with the totality of the other mortgage rules, has created a very burdensome regulatory environment and many credit unions are finding it difficult to continue lending. Credit unions must comply with the current disclosure requirements, which are extensive, and they must prepare their compliance solutions for the upcoming ones effective in August 1, 2015, further exacerbating costs. We are pleased that National Credit Union Administration (NCUA) Chairman Debbie Matz indicated to NAFCU in a March 24, 2015, letter that NCUA examiners would be looking for "reasonable and good faith efforts by credit unions toward substantial compliance with the new rule as of the effective date." We hope that the CFPB will follow suit and provide similar guidance on this issue.

We would also support a legislative change to ensure that a consumer is not precluded from closing a mortgage because of a legal technicality, by protecting the right of a consumer to waive the requirement that certain mortgage disclosures be provided to the consumer 3 business days before closing.

FHFA Proposed Rule

In September of 2014, the Federal Housing Finance Agency (FHFA) released a proposed rule that would establish new asset threshold for both Federal Home Loan Bank (FHLB) applications and ongoing membership. Specifically, FHLB members and applicants would be required to keep 1 percent of assets in home mortgage loans. Also, current FHLB members would be required to hold at least 10 percent of assets in residential mortgage loans on an ongoing basis – a marked change from the current rule, which only requires this 10 percent threshold at the application stage. The proposal would also require FHLBs to evaluate member compliance annually and to terminate membership after two consecutive years of noncompliance.

This proposed rule threatens to severely hamper credit unions' access to the valuable services the FHLBs provide and must be carefully considered for its full impact before moving forward. In 2007, 11.4% of credit unions were members of an FHLB, representing 61.7% of total credit union assets. Today, however, 19% of all credit unions are members of an FHLB, and these credit unions represent 75.8% of the total credit union assets and this number continues to grow. This growth of credit union membership in FHLBs only underscores the need to ensure that the eligibility requirements for membership in FHLBs are set appropriately. Unfortunately, this proposal would disenfranchise over 1 million credit union member-owners from receiving the benefits of FHLB resources as their institution's membership would be terminated under the newly proposed requirements.

While NAFCU appreciates FHFA's intention of fostering FHLB's housing finance missions, we believe the current regulatory requirements effectively ensure that FHLB members demonstrate ongoing commitments to mortgage lending in their communities. For example, when an FHLB member borrows an advance, it must provide eligible collateral to secure the advance. Nearly all eligible types of collateral, which are determined by Congress, are related to housing. In addition, current members must certify their active support of housing for first-time homebuyers to the FHFA every two years through the Community Support Statement. Further, FHFA has failed to provide any data or empirical evidence to support its claims that the FHLB system is at risk because some members may not meet the proposed asset percentage requirements on an ongoing basis. Given the sufficient existing requirements, and the lack of statistical support for the proposed changes, NAFCU does not believe FHFA needs to move forward with the newly proposed "ongoing" membership requirements for depository institutions in this rulemaking.

Further exacerbating this issue for credit unions is the statutory exemption for FDIC-insured banks with under $1.1 billion in assets from the 10% requirement as outlined in the *Federal Home Loan Bank Act*. In addition to seeking changes to the underlying FHFA proposal, NAFCU believes this discrepancy also needs to be addressed to ensure an even playing field between all financial institutions including credit unions on this matter. We would urge the committee to act on this matter and create parity for credit unions.

NCUA's Risk Based Capital Proposal and Mortgage Servicing Assets

NAFCU supports bipartisan legislation that has advanced through the House Financial Services Committee that would require the federal financial regulators, including the National Credit Union Administration (NCUA), to study the appropriate capital requirements for mortgage servicing assets. Relative to NCUA's recently proposed risk-based capital system, this legislation would promote much-needed transparency, require a thorough analysis of the proposal's impact on mortgage servicing assets and generally encourage NCUA to consider the full impact of the costly proposal and how it will affect the ability of credit unions to make mortgage loans to consumers. We would urge the committee to consider similar legislation in the Senate.

Thank you again for holding this hearing and your continued focus on regulatory relief to community based financial institutions including credit unions. We look forward to continuing to work with the Banking Committee as you move forward in addressing many of these issues. If my staff or I can be of assistance to you, or if you have any questions regarding this issue, please feel free to contact myself, or NAFCU's Vice President of Legislative Affairs Brad Thaler at (703) 842-2204.

Sincerely,

Carrie R. Hunt
Senior Vice President of Government Affairs and General Counsel

cc: Members of the Senate Committee on Banking, Housing, and Urban Affairs

Prepared Testimony of

The National Association of Mortgage Brokers

on

"Regulatory Burdens to Obtaining Mortgage Credit"

Before the

Committee on Banking, Housing and Urban Affairs

Unites States Senate

Thursday April 16, 2015

The National Association of Mortgage Brokers appreciates this opportunity to address certain regulatory burdens that are having a significant adverse affect on consumers' ability to obtain mortgage credit.

NAMB is the only national trade association devoted to representing the mortgage broker industry. NAMB speaks on behalf of more than 50,000 mortgage professionals in all 50 states and the District of Columbia. Our members are independent, small business men and women who adhere to a strict code of ethics and best lending practices when assisting consumers through the loan process. We typically maintain business relationships with various lenders to provide consumers with multiple financing options. These partnerships allow our members to offer consumers the most competitive mortgage products available.

We commend the Committee for holding this important hearing to identify, examine and address the underlying burdens that so many consumers are still facing today when seeking to obtain mortgage credit.

I. Summary

NAMB, like our sister trade groups, is very concerned that consumers are being harmed by certain unintended consequences stemming from regulatory requirements in the Dodd-Frank Act. Specifically, the steady rise in regulatory compliance costs, loan originating entities' fear of action by the Consumer Financial Protection Bureau, and a lack of clear and reliable regulatory guidance is adversely affecting the affordability and availability of mortgage credit for consumers and delaying our housing recovery.

The cost of regulatory compliance has surged beyond $7,000 per loan. As a result, mortgage broker companies, small lenders and community banks are increasingly leaving the primary mortgage origination market. With less competition, consumers across the board are facing increased costs. However, we are seeing a particularly disparate impact on low- and moderate-income borrowers.

NAMB believes this erosion of competition in the marketplace stems largely from a simple definitional error in the Dodd-Frank Act, which is greatly increasing the cost to consumers seeking loan amounts under $150,000 and making it virtually impossible for mortgage broker entities to serve those borrowers. Our testimony focuses on the harm this is causing consumers, the technical correction that we believe will solve this problem, and the impact of the broker business model.

II. Dodd Frank Act - Creditor Payments to Broker Firms - Explanation of the Problem

NAMB believes that there is a definitional error in the Dodd-Frank Act affecting the calculation of points and fees for Qualified Mortgages. We are confident that it could not have been the intent of Congress to include payments from creditors to mortgage broker entities in the calculation of points and fees, because such payments are already included in the rate established and offered by the creditor. Nevertheless, under current CFPB regulations, mortgage broker companies are forced to double-count their business and operational costs within the 3% cap on points and fees for Qualified Mortgages while every other originating entity is not.

Mortgage broker companies are generally small businesses. With an increase in labor costs stemming from recent Department of Labor regulations, and with the steady increase in the cost of employee healthcare, small businesses are seeing their operational expenses skyrocket. The CFPB's interpretation of the Dodd-Frank Act as requiring only mortgage broker companies to double-count their business and operational expenses and still remain within the 3% cap for Qualified Mortgages places broker entities at a significant pricing disadvantage as compared with every other market participant.

Recently, the CFPB acknowledged this problem of double-counting in another area. In its final rule on Loan Originator Compensation issued May 29, 2013, the CFPB took corrective action

and excluded from the calculation of points and fees payments from mortgage broker companies to their employee loan officers.

> "Because payments by mortgage brokers to their employees already have been captured in the points and fees calculation, excluding such payments will facilitate compliance with the points and fees regulatory regime by eliminating the need for further investigation into the mortgage brokers' employee compensation practices, and by making sure that all creditors apply the provision consistently. [Emphasis added] It will also effectuate the purposes of TILA by preventing the points and fees calculation from being artificially inflated, thereby helping to keep mortgage loans available and affordable by ensuring that they are subject to the appropriate regulatory framework with respect to qualified mortgages and the high-cost mortgage threshold." CFPB Final Loan originator compensation rule, page 76 May 29, 2013.

This was extremely helpful, and we believe a correct interpretation of the Dodd-Frank Act. However, despite identifying the same problem of double-counting with creditor payments to mortgage broker companies, and despite acknowledging that mortgage broker companies are at a disadvantage vis-a-vis their competitors, the CFPB remains unable, in their estimation, to take similarly necessary corrective action with regard to creditor payments to mortgage broker companies. The reason for this, cited by the CFPB, is because of language in the Dodd-Frank Act attempting to define which mortgage entities' fees should be included in the points and fee calculation for purposes of determining a Qualified Mortgage. In relevant part, Section 1431(c)(A) of the Dodd-Frank Act (current Section 103(bb)(4)(B) of TILA) provides:

> "(B) all compensation paid directly or indirectly by a consumer or creditor to a mortgage originator from any source, including a mortgage originator that is also the creditor in a table-funded transaction;"

Experts within and outside of the CFPB believe this definitional language, which is preventing the CFPB from excluding creditor payments to mortgage broker companies from the calculation of points and fees, is actually a drafting error in the Dodd-Frank Act.

Any amount that is already reflected in the rate of a loan should not be included in the calculation of points and fees. The CFPB utilized it's Congressionally-granted power to exclude from the Qualified Mortgage definition of points and fees any payments from a creditor to the creditor's employees. In its release published in the Federal Register June 12, 2013, (78 FR 35429), the CFPB additionally pointed-out that a similar result should occur for payments from lenders to mortgage broker companies and their loan originator employees since such fees are already reflected in the mortgage rate and are being counted twice.

> "The final rule excludes from points and fees loan originator compensation paid by a consumer to a mortgage broker when that payment has already been counted toward the points and fees thresholds as part of the finance charge under § 1026.32(b)(1)(i). The

> final rule also excludes from points and fees compensation paid by a mortgage broker to an employee of the mortgage broker because that compensation is already included in points and fees as loan originator compensation paid by the consumer or the creditor to the mortgage broker."

This principle is further supported and extended by the CFPB in it's Final Rule on Integrated Mortgage Disclosures that takes affect on August 1, 2015. In that final rule the CFPB declared that the disclosure of mortgage broker compensation is not a beneficial aspect of the transaction and only confuses the consumer as to the consumer's real costs for the transaction. As such, beginning August 1, 2015 mortgage brokers will no longer be required to disclose on the Loan Estimate and Closing Disclosure Forms any compensation they receive from the creditor.

The option for a consumer to select a market rate above par alleviates the need for the consumer to pay a mortgage broker company any fee out of consumer's personal funds. The above par rate enables the creditor to compensate the mortgage broker company directly. This being the case, a payment from a creditor to a mortgage broker company should not be counted in the 3% cap on points and fees for Qualified Mortgages because this payment is already accounted for within the interest rate chosen by the consumer.

In order for a fair and competitive marketplace to be reestablished, payments from a creditor to a mortgage broker company must be excluded from the Qualified Mortgage points and fees calculation.

III. Lack of Competition Hurts Consumers

Empirical studies have shown that mortgage brokers offer better terms, on average, than depository lenders and other creditors.[1] Specifically, these studies show that in areas with a higher concentration of mortgage brokers consumer choice is greater and consumers generally receive lower interest rates from brokers in that area.[2] Conversely, where there are fewer mortgage brokers competing in a given market and thus less competition, consumers typically pay higher interest rates.[3]

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[1] Amany El Anshasy, Gregory Elliehausen & Yoshiaki Shimazaki, *The Pricing of Subprime Mortgages by Mortgage Brokers and Lenders* 12 (July 2005) (unpublished manuscript), *available at* http://www.chicagofed.org/digital_assets/others/events/2005/promises_and_pitfalls/paper_pricing.pdf (finding that "broker-originated mortgages are less costly to the borrower than lender-originated mortgages after holding other loan terms and borrower characteristics constant")

[2] *See* M. Cary Collins & Keith D. Harvey, *Mortgage Brokers and Mortgage Rate Spreads: Their Pricing Influence Depends on Neighborhood Type*, 19 J. HOUSING RES. 153, 168 (2010) ("Our results support our hypothesis that the mortgage broker is a better informed agent and show that in general as mortgage broker density increases, both the likelihood of a rate spread occurring and the size of a rate spread declines, while the loan approval rate increases."

[3] See id at 167-68

As an example of this, a recent examination of closed loans in Duval County Florida found that the average net consumer closing costs for a creditor transaction was $6,222, while the net cost to consumers in broker transactions, after credits were applied, was $3,479. This is a greater than $3000 per loan cost savings for consumers obtaining loans from mortgage brokers. We believe that further examination and analysis of this pricing disparity between creditor and mortgage broker transactions will reveal similar results across the country.

NAMB is deeply concerned that without a correction to the definitional error in the Dodd-Frank Act there will be fewer and fewer mortgage broker companies in many areas, and a significant disparate impact will be felt by low- and moderate-income consumers who have no option but to obtain loans from large national banks. This is an unfortunate reality that is already affecting many consumers across the country and should not be allowed to get any worse. We respectfully urge this Committee and Congress to take corrective action as soon as possible.

IV. Mortgage Company Fixed Compensation

Since 2011, all compensation paid by creditors to mortgage broker companies is fixed, without any possibility for variation from transaction to transaction, as a result of the Loan Originator Compensation Rules issued by the Federal Reserve Board and the CFPB. This is a strong additional layer of consumer protection for borrowers utilizing a mortgage broker company and another reason why creditor compensation to a broker company should not be double-counted in the definition of points and fees.

Under these parameters, not only are loan originators working for mortgage broker companies prohibited from steering consumers toward a particular loan or lender, there is no incentive for them to do so. Making the small, but significant correction to the definition of points and fees in the Dodd-Frank Act that NAMB is encouraging will not put consumers at any risk. Rather, this simple change in definition will work to protect consumers from harm by preserving and enhancing competition, and saving consumers money at the closing table.

V. Policy Recommendations Conclusion

NAMB thanks the Committee for this opportunity to submit testimony for the record. We believe compensation paid from the creditor to a mortgage broker company, which is taken into account when the creditor sets the interest rate, should not be included in the 3% points and fees calculation for Qualified Mortgages. We look forward working with the Committee to correct what we believe is merely a definitional error and resolve this unintended consequence of the Dodd-Frank Act in order to alleviate any further harm to consumers and help preserve and restore competition to the marketplace.

Regulatory Burdens to Obtaining Mortgage Credit
Senate Banking Hearing
April 16, 2015

It is time to examine the impact that the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) has had on the mortgage market. Five years ago, Congress passed to Dodd-Frank Act to protect consumers and prevent another crisis. While the American Financial Services Association (AFSA), the association of consumer finance companies, agrees with that intent, we believe that the law and the regulations implementing it have gone too far. Too many consumers with less-than-perfect credit histories are unable to get loans. Borrowers who are able to qualify for mortgages are facing increased costs.

By enacting a broad definition of a Qualified Mortgage and by setting the threshold for high-priced mortgage loans too low, many consumers do not have access to credit. Because the excessive penalties that apply to violations of the proposed rules on higher-priced mortgages are very significant, the secondary market has shied away from buying higher-priced mortgage loans. As we have already seen, many lenders will not make loans if the secondary market will not buy them. The public HMDA data reflects that the number of high-cost loans has dropped dramatically.

The increased restrictions, penalties and stigmatization have restricted the availability of credit for consumers with less-than-perfect credit histories. As a result of these increased risks, very few of these loans are being made. The few that are made are far costlier, burdening families least able to bear the expense.

Here's an example from an AFSA member in Alabama:

> A customer that was self-employed needed $40,000 to send his twin daughters to a major university in Alabama. The customer owned a thriving restaurant business, but after 2009 he had a couple years where his gross sales went down around 15 - 20%, largely due to a dip in the economy. He also had a couple credit cards that he had to carry a larger than normal balance which had an effect on his credit score. Although the customer had a relationship with several banks for many years (and never had any issues); when he approached these banks for a home equity loan to send his daughters to college, they told him "no." Due to his debt load, reduced gross sales, and slightly lower credit score, they would not help him.
>
> This customer had taken out small, unsecured loans from a traditional installment lender for years. So, he came again to discuss his situation. He owned his home free and clear, and it had an appraised value of over $200,000. He needed $40,000 – $30,000 for college tuition and about $10,000 to put back in his business (which had increased sales over the past 2 years). After the lender took the application, it sent him to the "required counseling services" associated with high-cost loans. The counselors tried to convince the customer that he did not need to mortgage his home at a higher-interest rate. The lender's understanding was that they were to discuss

> the rate and risk of a high-cost loan but not "steer a customer" to NOT seek financing. The gentleman was quick to tell them that the lender had already talked to him about the rate and the other items associated with the loan, but that the banks that always made him loans were now not willing to help him. His need for credit did not go away because of the economy or challenges of running a business, just a source of credit. The lender was able to make this loan for and the customer has made his payments, as agreed.
>
> High-cost lenders (a government term), have to fight to help their customers. The average time from application to funding a real estate loan is almost three weeks or more. Five years ago, this process took under a week. When these customers need money, it is not normally a luxury, it's a need.

Here are other examples from a traditional installment lender's customers in Mississippi:

> Customer A has had accounts with the lender since a least 2005. Even though she has exemplary credit history, she is unable to consolidate and refinance her loan because she baby-sits and cleans houses – sources of income that are unverifiable.
>
> Customer B was unable to get counseling and so she could not get approved for a loan. She attempted to contact multiple approved counseling agencies, but was unable to get help. The branch manager attempted as well, but was unable to speak directly to someone. The customer is now filing for bankruptcy.
>
> Customer C has limited income from her retirement. She has rental income from her nephew, but is unable to prove it. The new laws have kept her from being able to refinance her account and lower her monthly payment due because she is unable to verify all of her income. She has been a real estate customer with the lender since 1996 and has an exemplary credit history. She does not understand why the lender cannot help her, since she pays her bill every month.

We ask Congress to modify these restrictive laws and regulations so that they actually, not just purportedly, help consumers.

Statement for the Record
From John Taylor, President and CEO
To Senate Committee on Banking, Housing, and Urban Affairs
Hearing on Regulatory Burdens to Obtaining Mortgage Credit
April 21, 2015

Chairman Shelby, Ranking Member Brown, and distinguished Members of the Committee:

The National Community Reinvestment Coalition (NCRC) appreciates the opportunity to provide this written statement for the record of the April 16, 2015 hearing on *Regulatory Burdens to Obtaining Mortgage Credit*. In this statement, we will share with the Committee many of the comments we have shared with federal agencies involved in housing finance.

NCRC is a nonprofit, nonpartisan association of more than 600 organizations dedicated to the mission of building and protecting wealth in America's underserved communities. For more than 20 years, we have advocated to ensure vibrant communities for America's working families by actively promoting access to basic banking services and products, homeownership and the development of affordable rental housing, local business growth, and workforce training. Our members include community reinvestment organizations, community development corporations, community development financial institutions, local and state government agencies, faith-based institutions, community organizing and civil rights groups, minority- and women-owned business associations, and social service providers from across the nation.

Quite frankly, NCRC is concerned that several of the proposals before the Committee propose rollbacks to many of the important systemic safeguards and consumer protections enacted by the Dodd-Frank Wall Street Reform and Consumer Protection Act and regulations implemented by the Consumer Financial Protection Bureau (CFPB). The reforms under Dodd-Frank are critical to avoid another financial crisis that ripped apart American communities, resulting in millions of lost jobs and a period of prolonged economic recession.

Access to Mortgage Credit: Key to Economic Opportunity and Building Wealth

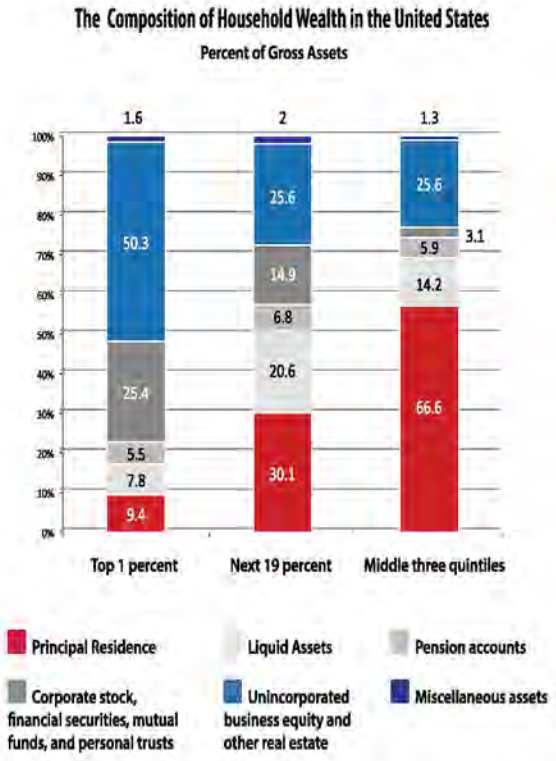
The Great Recession is over, but that doesn't mean the average American is prospering. While the economy is adding jobs every month, many communities still suffer from economic insecurity. The economic situation of most families and communities has been negatively affected by the loss of homeownership and declines in home values and tight credit markets – in both home and small business lending – that continue to plague the nation.

The recession revealed deeper problems in the foundation of the American economy. Inequality is growing and economic mobility has declined. The wealth gap between high income and middle- and lower-income people is at an all time high, and the racial wealth gap has grown. A 2014 Harvard Business School study characterized the struggles of working and middle-class Americans and small businesses as "unsustainable."[1]

The interplay between federal policies affecting home lending, business lending and financial institutions may seem abstract or inconsequential to some. But the growing wealth gap has everything to do with how, where, and to whom financial institutions extend capital and credit, and government law and regulation impacts that significantly.

Stabilizing communities and protecting and repairing the rungs on the ladder of opportunity starts with understanding what drives wealth creation in American communities and how most people build savings and wealth. As evidenced by the chart below, for most Americans, this doesn't happen through the stock market, it happens through buying a home or investing in a business or real estate.

[1] Michael E. Porter and Jan W. Rivkin, "An Economy Doing Half Its Job," Harvard Business School, 2014, available at http://www.hbs.edu/competitiveness/Documents/an-economy-doing-half-its-job.pdf



Source: Wolff (2012)

Ensuring broad access to mortgage credit for the low- and moderate-income and other traditionally underserved communities is especially effective for most Americans because they fulfill another essential need while building wealth. A home also puts a roof over one's head. A business can provide necessary income. In both cases, sustainable ownership has historically had demonstrably positive effects on the community at large, including higher levels of civic participation, job creation and neighborhood stability, and evidence suggests this continues post-financial crisis.[2]

[2] Ibid.

The nationwide foreclosure crisis that led to a financial crisis and the Great Recession demonstrated that protections must be in place to guard against financial fraud and abuse, or else wealth creation will be stripped by unscrupulous actors and not captured by homeowners, small businesses, and communities. As such, the protections created by the Dodd-Frank law and the work of the CFPB, the Fair Housing Act, and the Community Reinvestment Act remain extremely critical.

The following are a number of recommendations that we offer to the Committee to assist in overcoming obstacles to obtaining mortgage credit in underserved communities around the country.

Ensuring that the Secondary Mortgage Market Creates Opportunities for Access to Affordable Credit

The current structure of the housing finance system helps create broader access to conventional financing than would otherwise exist in a fully private market. Prior to the advent of the government-sponsored enterprises (GSEs), the 30-year fixed rate mortgage did not exist. Typical terms were less than 10 years, and often required deposits of 50 percent or more. Such requirements put homeownership out of reach of most Americans.

There are a variety of ways forward in reforming the housing finance system, but any that are undertaken must result in a secondary mortgage market that provides clear access to affordable credit for all creditworthy borrowers. Legislative action may not be wise or feasible at the moment, however unwinding Fannie Mae and Freddie Mac from conservatorship and allowing them to recapitalize would do a great deal to boost the housing market. FHFA and the Treasury Department should begin this process soon to create greater stability and accessibility to the mortgage market.

Affordable Housing Goals & The Enterprises' Affirmative Obligation

A number of the recent moves by the Federal Housing Finance Agency (FHFA) have been encouraging: on mortgages with loan-to-value ratios between 95 and 97 percent; on revising and clarifying the Representation and Warranty Framework; and, importantly, on capitalizing the Housing Trust Fund and the Capital Magnet Fund. However, these actions alone are not enough.

The GSEs are also subject to affordable housing goals that have supported lending to creditworthy working-class borrowers for decades. Fannie Mae and Freddie Mac have made it possible for millions of creditworthy borrowers to become successful homeowners. Unfortunately, under FHFA's supervision, the GSEs' role in facilitating affordable housing has been minimal. The Enterprise Housing Goals are at their lowest levels since numeric benchmarks were first established. Unless the Enterprises renew their historic commitment, long contemplated by Congress, "to lead the industry" by setting a low-income home purchase target that the GSEs will have to "stretch" to meet then, quite simply, the table will be set for many of the nation's low- and moderate-income and underserved communities. The housing market will move further out-of-reach for millions more creditworthy borrowers.

FHFA has proposed three alternatives for the 2015-2017 Enterprise Housing Goals. We believe that the proposed benchmark standard is consistent with statutory mandates and Congressional intent and is the most legally defensible of the three alternatives FHFA has proposed. We also recommend a target goal of 28 percent, based on the GSE's past performance under comparable economic conditions and a similar market environment. These recommendations will better ensure that Fannie Mae and Freddie Mac are fulfilling their statutory obligation to foster a healthy mortgage market for low- and moderate-income families.

Lower Guarantee Fees

We are very concerned that the increases in the guarantee fees by Fannie Mae and Freddie Mac since 2009 are contributing to the affordability challenges facing many borrowers. The guarantee fees currently charged by the Enterprises well exceed what is necessary to support the extraordinary credit quality of the GSEs current book of business. In particular, the strong credit quality ensured by the CFPB's Ability to Repay rule makes high guarantee fees less necessary. FHFA should encourage the Enterprises to lower their guarantee fees to reflect the reality of the GSEs position in conservatorship and to increase affordability of mortgage credit.

Alternative Credit Scoring Models

There are a number of issues around the current FICO credit score that is limiting access for creditworthy borrowers: the GSE's increasing FICO score requirements, the use of old versions of FICO, and the overall limits of FICO modeling. Multiple studies have shown that a disproportionate share of low- and moderate-income individuals are left out of traditional credit scoring models and traditional trade credit lines, yet are fully capable of handling credit and monthly debt obligations responsibly. FHFA is currently reviewing alternative credit scoring models and we urge the agency to expedite that review.

Encourage Housing Counseling

Housing counseling has consistently been proven as a successful tool in helping borrowers achieve and maintain homeownership, lowering the likelihood of delinquency and default. At the moment, housing counseling remains optional for most home purchase programs, including loans backed by the FHA or the GSEs. By requiring housing counseling before receipt of an FHA loan, the FHA could further reduce its already low default rates. Additionally, FHFA could require or encourage the GSEs to make HUD-certified counseling mandatory, at least on low down payment loans, such as the new 97 percent loan-to-value product. Low default rates would make for a safer investment in the secondary market and a stronger and safer housing market overall.

Enforcement and Improvements in the Community Reinvestment Act (CRA)

Since it was passed in 1977, the Community Reinvestment Act (CRA) has helped infuse trillions of dollars in community reinvestment dollars into minority and lower income neighborhoods. The CRA is critical to driving bank investment in underserved areas around the country. It has generated well over $6 trillion in private investment for low- and moderate-income communities.

We need a strong CRA now more than ever. The portion of home purchase loans in low- and moderate-income neighborhoods has stalled at 13 percent.[3] In addition, the Federal Deposit Insurance Corporation's *National Survey of Unbanked and Underbanked* revealed that 7.7 percent of households remain unbanked, and 20 percent of households are underbanked.[4] On a number of fronts, we are concerned about the enforcement of CRA's core provisions and the lack of comprehensive and innovative thinking about many aspects of the Act. CRA examinations should focus more keenly on whether or not banks are achieving results in the communities they serve.

CRA Examination Grade Inflation

Overall, we believe there is grade inflation in CRA bank examinations. For example, from 2012 to 2014, 99 percent of banks examined by the Federal Reserve received a passing grade, with only five receiving a "Needs to Improve" and one receiving a "Substantial Noncompliance". Yet, continued tight lending standards and decreasing loan-to-deposit ratios at the biggest banks indicate that many creditworthy borrowers are being denied access to credit. We think current examination results reflect a need to overhaul examiner training, a limited view of CRA performance context, a lack of meaningful assessment area reform, and insufficient consideration of community input in the examination process.

CRA Performance Context

When conducting evaluations, bank examiners are to consider the "performance context" of the lending institutions. In other words, examiners are advised to consider factors such as the business opportunities available to a lending institution and the size and financial condition of the lending institution. Currently, banks are allowed to write their own performance context, ostensibly with a review from examiners. Performance context should always be written by a community development professional employed by a regulatory agency that has an understanding of the community where the bank operates.

CRA Assessment Area Reform

The geographical locations covered by CRA exams consist of metropolitan areas or counties that contain bank branches. When Congress enacted CRA in 1977, banks received deposits and made loans through branches. While some banks still issue loans predominantly through branches, others make the majority of their loans through brokers and other non-branch channels. Though the CRA regulation stipulates that assessment areas include geographical areas containing bank branches, the regulation also states that assessment areas include other geographical areas in which the bank has originated or purchased a substantial portion of its loans.[5] Despite this regulatory clause, the federal agencies usually adopt a narrow definition of

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[3] 2013 HMDA data, Federal Reserve Report

[4] FDIC, National Survey of Unbanked and Underbanked, available at https://www.fdic.gov/news/news/press/2014/pr14091.html

[5] See Section 345.41 of the FDIC's CRA regulation available via http://www.fdic.gov/regulations/community/community/index.html

assessment areas for banks that issue most of their loans through non-branch channels.

Expanding assessment area coverage would have a positive impact on low- and moderate-income borrowers as well as minorities. Harvard's Joint Housing Center finds that banks issue higher levels of loans to low- and moderate-income borrowers and communities inside their assessment areas than outside assessment areas.[6] It stands to reason that banks will issue more loans to traditionally underserved borrowers and communities in areas where they are examined. Thus, expanding CRA's examination scope will promote housing and economic development in modest income communities and there will be a much clearer picture of how banks are actually performing.

Bank Branches & Alternative Delivery Methods

The disproportionately high number of branch closures in low- and moderate-income communities suggests that many banks need to reevaluate their closure plans to ensure that they are adequately meeting the financial needs of underserved communities. The provision of online and mobile services alone is insufficient. To warrant CRA credit, it must be clear that those services are accessible to low- and moderate-income individuals and geographies, are actually adopted, preferred and that they complement other methods for communities to engage financial institutions. These services are not, and should not be, a replacement for full service branches. Negative marks should be given on the CRA service test for banks that pull out of low-and moderate-income neighborhoods through branch closures, particularly when no viable alternative service delivery method exists.

By adopting practices that engage the community and examine community impact, such as conducting community impact assessments before filing notice of a branch closure and inviting community stakeholders to participate in a discussion of how the bank will otherwise meet its obligation to provide access to credit and capital, banks can demonstrate their commitment to ensuring that the financial needs of all communities are met.

Conclusion

In conclusion, we thank the Committee for providing the National Community Reinvestment Coalition, and the 600 community-based, member organizations that we represent, the opportunity to share out thoughts on the regulatory actions that might most facilitate access to mortgage credit for low- and moderate-income creditworthy borrowers and underserved communities. We reiterate our concern about several of the proposals being considered by the Committee that seek to rollback provisions of Dodd-Frank and restrict the ability of the CFPB to implement rules that are designed to protect consumers. Instead, we urge the Members of the Committee to consider the recommendations we have offered.

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[6] The Joint Center for Housing Studies at Harvard University, *The 25th Anniversary of the Community Reinvestment Act: Access to Capitol in an Evolving Financial Services System*, March 2002.

CUNA
Credit Union National Association

Jim Nussle
President & CEO

601 Pennsylvania Ave., NW
South Building, Suite 600
Washington D.C. 20004-2601

Phone: 202-508-6745
Fax: 202-638-7736
jnussle@cuna.coop

April 15, 2015

The Honorable Richard Shelby
Chairman
Committee on Banking,
Housing, and Urban Affairs
U.S. Senate
Washington, D.C. 20510

The Honorable Sherrod Brown
Ranking Member
Committee on Banking,
Housing, and Urban Affairs
U.S. Senate
Washington, D.C. 20510

Regulatory Burdens to Obtaining Mortgage Credit

Dear Chairman Shelby and Ranking Member Brown:

On behalf of the Credit Union National Association (CUNA), thank you for holding this important hearing entitled "Regulatory Burdens to Obtaining Mortgage Credit" and for allowing us to submit our views on this important topic. CUNA is the largest credit union advocacy organization in the United States, representing nearly 90% of America's 6,300 state and federally chartered credit unions and their 102 million members.

Access to affordable mortgage credit on flexible terms is a key that helps unlock the American Dream for many families. As member owned, not-for-profit financial cooperatives, credit unions seek to meet members' demand for sound financial products like mortgages, but often face significant regulatory barriers as they try to help members achieve homeownership or expand the stock of affordable rental homes. We welcome the opportunity to comment on a few of those barriers and to offer suggestions for relief.

Deem all Portfolio Mortgages QM

Many regulatory barriers arose out of a genuine desire to make the mortgage system safer or more equitable, but all too often, there are unintended consequences to well-intentioned regulations. For example, the Qualified Mortgage (QM) structure and associated ability-to-repay rule were created ostensibly to protect borrowers from mortgages they could not afford. However, QM has significantly curbed access to a variety of flexible mortgage products that can be tailored to suit individual borrowers' specific needs. One way to alleviate this burden would be to allow mortgages that are held in portfolio and serviced by the underwriting financial institution to be deemed QM. Historically, credit unions have predominantly been portfolio lenders. As such, they have very strong incentives to originate quality loans that are properly underwritten to ensure a borrower will be able to repay, simply by virtue of the fact that the loan will be held on the lender's books. When compared to industry averages, credit union charge off rates are incredibly low, which suggests that loans held in portfolio are less likely to become delinquent or go into default. These factors would weigh heavily in favor of allowing greater flexibility from QM requirements for loans held in portfolio and allow credit unions to better assess the credit worthiness of their members.

"Points and Fees" Relief

The Senate should enact legislation that would exclude from the points and fees calculation affiliated title insurance charges and escrowed homeowners' premiums. The QM rule sets the standard for consumer mortgages by providing significant compliance certainty to loans that do not have risky features and meet strict Federal requirements. A key requirement is that points and fees for a QM generally may not exceed 3% of the loan amount. The problem arises from the fact that, under current law and rules, what constitutes a "fee" or a "point" towards the cap varies greatly depending upon who is making the loan and what arrangements are made by consumers to obtain title insurance. If the consumer chooses a title insurance provider that is affiliated with the lender, the title insurance charges count, but if the insurance is purchased from an unaffiliated title agency, the title charges do not count. In addition, escrowed homeowners insurance premiums may count as "points and fees" due to ambiguous drafting in the law.

FHFA 10% Rule & Credit Union Parity for FHLB Membership

We are very concerned about the September 2, 2014, proposal from Federal Housing Finance Agency (FHFA) to revise the agency's rules regarding membership in a Federal Home Loan Bank (FHLB). FHLBs are critical sources of liquidity for many credit unions, and the proposed regulation would make it much more difficult for both new and existing credit unions to maintain access to the FHLB system. CUNA questions the need for the proposal and submitted a comment letter to the agency on January 12, 2015, that asked the agency to withdraw the proposal.[1]

This proposed rule, which is based on an advance notice of proposed rulemaking (ANPR) issued almost four years ago, creates two core requirements for financial institutions. First, the rule would require all financial institutions who are FHLB members to hold one percent of their assets in "home mortgage loans" on an ongoing basis. The proposed regulation suggests that FHFA is considering raising this requirement to as high as five percent in the future. While financial institutions currently must meet the one percent-of-assets threshold to become FHLB members, there is no requirement at this time that the member maintain it to remain a member.

Second, all FHLB-member credit unions—but, because of a statutory limitation in the *Federal Home Loan Bank Act*, only certain banks—would also be required to hold 10% of assets in "residential mortgage loans" on an ongoing basis. By statute, for initial membership, the *Federal Home Loan Bank Act* exempts from the "10 percent" requirement any "community financial institution" or "CFI," as defined as FDIC-insured banks with less than $1 billion in average total assets (adjusted annually for inflation) over the preceding three years. Credit unions, generally insured by NCUA, are not eligible for this exemption. FHFA has proposed to maintain the "CFI" exemption without any variation for the purposes of *maintaining* membership, despite the fact that the agency has flexibility in this regard. FHFA should exercise its discretion and treat credit unions and banks

[1] Letter from Mary Mitchell Dunn, Deputy General Counsel, Credit Union National Association to Alfred Pollard, General Council, Federal Housing Finance Agency. Comments on Proposed Changes to Federal Home Loan Bank Membership Requirements/RIN 2590-AA39. January 12, 2015 (http://www.cuna.org/uploadedFiles/CUNA/Legislative_And_Regulatory_Advocacy/Track_Regulatory_Issues/Pending_Regulatory_Changes/2014/FHLB_MembershipLetter_01122015.pdf)

equally if it moves forward with the proposal. CUNA also calls on Congress to amend the *Federal Home Loan Bank Act* to ensure credit unions are considered "community financial institutions" for the purpose of securing *initial* FHLB membership.

Beyond the issue of parity, we urge Congress to discuss with FHFA the need for this proposal as well as the details. Congress, not the regulator, should define who can be members of the FHLBs. FHFA is under no statutory obligation to impose these membership limits on an ongoing basis. Although we recognize FHFA has an interest in ensuring FHLB members maintain a commitment to housing finance, we believe this is a regulation in search of a problem. We are unaware of any financial institutions who can jump through the substantial regulatory hoops to become FHLB members, who are willing to buy stock in the FHLBs, and who meet the 10% requirement at the time of membership who are not committed to housing. This regulation will create another compliance task for credit unions, who will be forced to maintain a close watch over their balance sheet to ensure they meet an arbitrary requirement on an ongoing basis. FHFA acknowledges that the proposed regulation will put the existing FHLB membership for some credit unions in jeopardy. Loss of FHLB membership will limit access to the low-cost source of funding provided by the FHLBs, restricting credit at a time when our nation's housing recovery remains fragile.

Allowing Privately Insured Credit Unions Membership to FHLB

We support legislation that was introduced by Ranking Member Brown (D-OH) and Senator Portman (R-OH) last Congress to correct a drafting oversight in the *Federal Home Loan Bank Act* which has resulted in a small number of privately insured credit unions being ineligible to join a FHLB.

In 1989, in the wake of the savings and loan crisis, the FHLB System was opened up for the first time to commercial banks and credit unions. Unfortunately, the bill was drafted in such a way to apply only to an "insured credit union" as defined under the *Federal Credit Union Act*. If the legislation had used a broader term in the 12 USC 1752 of the *Federal Credit Union Act* – such as "state credit union" or "state-chartered credit union", terms that are clearly defined, then privately insured credit unions would have the same opportunity for membership as other financial institutions. This is why, for many years, we have suggested that this was likely an oversight in drafting. Unfortunately, it has meant that for over two decades, a small group of credit unions have been denied the right to even apply for membership in the FHLB System.

The House of Representatives has continuously recognized this as a problem. In 2004, 2006, 2014 and as recently as this week, the full House passed corrective legislation. In 2008, as part of the *Housing and Economic Recovery Act of 2008*, Congress made a small change to permit privately-insured, state-chartered credit unions designated as a Community Development Financial Institution (CDFI) to apply for membership to the FHLBs; however, of the 127 privately insured credit unions, only two are CDFI certified.

We understand some policymakers have concerns regarding the existence of the private insurance option; however, this legislation would not expand that option for credit unions

nor would it present an increased risk to the FHLB System, since this legislation only allows privately insured credit unions the option to apply for membership.

If enacted, privately insured credit unions would not be the only non-federally insured institutions eligible for membership in the FHLB System. Currently, insurance companies, which are not federally insured, are members of the System. In fact, in terms of current outstanding advancements, 119 insurance companies are borrowing almost twice as much as 427 federally insured credit unions.[2]

It has never seemed reasonable to our small institutions that some of the largest banks in the world, insurance companies (which are not federally insured) or a foreign bank's U.S. subsidiary can borrow billions of dollars from the FHLB System, but credit unions serving teachers in Ohio and Texas, firefighters in California, postal and county workers in Illinois and farmers in Indiana cannot.

Improving TILA-RESPA's Closing Disclosure Waiting Period

The Consumer Financial Protection Bureau's TILA-RESPA Integrated Disclosure rule requires delivery of the new Closing Disclosure three business days before loan consummation. If the Closing Disclosure is provided to the borrower in person, it is considered received at that time. If the Closing Disclosure is mailed to the borrower or delivered by means other than presenting the form to the member in person, the borrower is considered to have received the disclosure three business days after it is mailed or delivered. In the case where the Closing Disclosure is mailed to the borrower, loan consummation and closing could be delayed for at least six business days from the date the disclosure is mailed.

If loan consummation is scheduled at any time during the three day waiting period, the creditor generally must postpone consummation, unless consummation within the waiting period is necessary to meet a bona fide personal financial emergency of the borrower and the borrower has complied with requirements for waiving the waiting period.

If a credit union makes any of the following significant changes between the three-day waiting period when the Closing Disclosure form is provided and consummation, then the creditor must provide a revised Closing Disclosure to the borrower and must provide an additional three-business-day waiting period after receipt of the new form before consummation can occur:

- Changes to the APR above 1/8 of a percent for most loans (and 1/4 of a percent for loans with irregular payments or periods),
- Changes the loan product, or
- The addition of a prepayment penalty to the loan.

Less significant changes can be disclosed on a revised Closing Disclosure form provided to the member at or before closing - without delaying the closing.

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[2] According to the *Combined Financial Report of the Federal Home Loan Bank System for the Quarter ending on September 30, 2013.*

CUNA believes the bona fide personal financial emergency waiver should be clarified and expanded to provide additional flexibility to consumers and lenders.

In addition, CUNA believes the delivery timing requirement should be reduced from three business days to no longer than two business days or "48 hours" in order to shorten the time period until consummation and closing.

Finally, CUNA believes Congress should push the CFPB to delay the effective date of the TILA-RESPA Integrated Disclosure rule for an additional six months beyond August 1, 2015, to provide additional time for credit unions to implement the requirements of this very complex rule. There is precedent to do so. Prior to the creation of the CFPB, many consumer protection regulations had a compliance date later than the effective date to account for situations where a complicated rule could place diligent financial institutions at risk of non-compliance.

Credit Union Parity for Residential Real Estate Loans

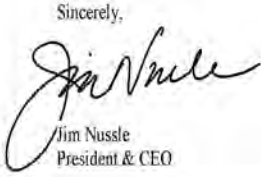
We encourage Congress to address a disparity in the treatment of certain residential loans made by banks and credit unions. When a bank makes a loan for the purchase of a 1-4 unit non-owner occupied residential dwelling, the loan is classified as a residential real estate loan; however, if a credit union were to make the same loan, it would be classified as a business loan and therefore subject to the cap on member business lending under the *Federal Credit Union Act*.

We support legislation to amend the *Federal Credit Union Act* to provide an exclusion from the cap for these loans. Doing so would not only correct this disparity, but it would enable credit unions to provide additional credit to borrowers seeking to purchase residential units, including low-income rental units. It is also worth noting that in its recent risk-based capital proposal, NCUA treated these loans differently than commercial loans. Excluding these loans from the business lending cap would provide consistency with the agency, parity with other depository institutions and provide greater housing accessibility.

Conclusion

These are only a few of the relevant barriers credit unions face in providing members access to affordable mortgage credit, but they are substantial. Credit unions strive to provide accessible and affordable mortgage products for their members. By addressing the issues described above, Congress would undoubtedly allow credit unions to help even more families unlock a piece of the American Dream. Thank you again for the opportunity to comment.

Sincerely,



Jim Nussle
President & CEO