THE COMMUNITY MORTGAGE LENDERS OF AMERICA

November 14, 2018

The Honorable Mick Mulvaney
Acting Director
Consumer Financial Protection Bureau
1700 G Street NW
Washington, DC 20552

Dear Acting Director Mulvaney,

The Community Mortgage Lenders of America is writing to urge the Consumer Financial Protection Bureau (CFPB) to make changes to its Loan Originator Compensation (LO Comp) rule necessary to help consumers and reduce regulatory burden. We recognize the CFPB is considering a variety of regulatory actions following the conclusion of its Request for Information process and believe changes to the LO Comp rule should be among the top priorities in its review of the mortgage rules.

The original motivation for the LO Comp rule was to protect consumers from steering. In the current regulatory environment, the harm associated with steering – borrowers agreeing to a loan they do not understand and cannot repay – is less likely than when the LO Comp rule was first adopted due to the rule itself, as well as other regulatory actions adopted following the passage of the Dodd-Frank Act.

The Qualified Mortgage rule made repayment ability the principal consideration in credit decision-making, largely eliminating loan features and lending practices believed to be risky. More recently, the CFPB's TILA-RESPA Integrated Disclosure rule attempted to make mortgage terms and costs easier to understand by heightening disclosure requirements. Together, these regulations reduce the risk of steering by shielding consumers from unsuitable mortgage loan products and ensuring they are aware of the costs of credit.

While these regulatory developments have reduced the risk of steering, the LO Comp rule places strict limits on certain practices that actually would result in lower consumer costs or greater product availability. After more than five years under the rule, a rebalancing is needed.

The LO Comp rule, while well-intentioned, is causing serious problems for the industry and consumers due to its overly strict exclusions on adjusting compensation and the vague definition of what constitutes a "proxy" for a loan's terms or conditions. These impairments are felt when borrowers are unable to obtain lower interest rates or fees from their lender of choice when shopping for a mortgage, or when lenders are unable to hold loan officers accountable for errors in the origination process. Consumers are also harmed when lenders limit their participation in special programs designed to serve first-time and low- to moderate-income borrowers due to the lack of enough income necessary to enable companies to sustain operations. The following changes would address these problems:

(1) Loan originators should be allowed to voluntarily lower their compensation in response to demonstrable competition in order to pass along the savings to the consumer. The Bureau's rule provides that a loan originator's compensation may not be increased or decreased once loan terms have been offered to a consumer. This provision is designed to eliminate financial incentives for a loan officer to steer a consumer to a higher interest rate or a higher-cost loan. However, the rule as implemented also has the effect of prohibiting reductions in compensation that could otherwise be passed along to the consumer in the form of a lower-priced, more affordable loan or the ability to participate in a product or program with lower margins which would benefit the consumer by providing a loan program better suited to their needs. This is especially critical for first-time and low- to moderate-income borrowers. In addition, this result also has the effect of reducing the consumer benefit that comes from shopping across multiple lenders in order to negotiate the best interest rates, program, and other terms.

Currently, in such situations, a lender must decide between lowering the interest rate, fees, or discount points to meet the competition (and thus originating an unprofitable loan with the fixed loan originator compensation) or declining to compete with other loan offers thus eliminating opportunities for borrowers to receive the product which is best for their specific situation. The requirement to pay the loan originator full compensation for a discounted loan creates a strong economic disincentive for lenders to match interest rates. For the consumer, the result is a more expensive loan or the inconvenience and expense of switching lenders in the midst of the process. This anti-competitive feature impedes loan shopping and discourages price competition and is therefore contradictory to the stated aims of the CFPB's Know Before You Owe / RESPA-TILA Integrated Disclosure rulemaking, which seeks to encourage shopping and empower the consumer to negotiate.

To address this unintended outcome, we urge the CFPB to amend the rule to permit lenders to respond to demonstrable price competition with other lenders by allowing the loan originator to voluntarily reduce his or her compensation in order to pass along the savings to the consumer. This change would significantly enhance competition in the marketplace, helping lenders to compete for more loans and benefiting consumers who will receive a lower interest rate or lower-cost loan offer as well as the best product for their specific situation.

(2) Loan originator's compensation should be allowed to be reduced by the lender when the originator makes an error. The LO Comp rule currently prevents companies from holding their employees financially accountable for losses that result from mistakes or intentional noncompliance with company policy when they make an error on a particular loan. As it stands, a loan originator who is responsible for an error may not bear the cost of that mistake. This result runs directly contrary to the central premise of the Dodd-Frank Act amendments to TILA that led to the LO Comp rule — compensation is the most effective way to incentivize loan originator behavior.

The inability to tie compensation to the quality of a loan originator's work on a given loan severely restricts the creditor's ability to manage its employees and disincentivize future errors. Effectively, the creditor is left with two extreme options: fire the loan originator or pay him or her full commission despite the error. This extremely limited choice does not serve the interests of consumers, creditors, or loan originators, or the agencies. Rather, greater accountability on the part of loan originators will incentivize them to reduce errors and consistently comply with regulatory requirements and company policy, leading to a safer and more transparent market for consumers as well as more desirable loans insured by the agencies and purchased by the GSEs.

(3) Lenders should be allowed to alter loan compensation in order to offer loans made under state and local housing finance agency (HFA) programs as well as those programs offered with lower margins due to specific arrangements between the lender and program sources such as portfolio lenders or independent investors. The LO Comp rule is understood to forbid varying compensation for different loan types or products, including these types of loans. HFA programs are particularly important for first-time homebuyers and low- to moderate-income families who are often underserved and face affordability constraints under market interest rates and terms.

These programs provide participants with much-needed lower interest rates or access to down payment assistance, often along with housing counseling and financial education, encouraging responsible homeownership in a well-regulated manner.

However, the assistance provided through many of these programs is not without costs. The vigorous underwriting, tax law-related paperwork, yield restrictions, and other program requirements make HFA and some other loan programs more expensive to produce. These programs also frequently cap lender compensation at levels below what a lender typically receives on a non-HFA/portfolio loan. Covering these expenses is particularly difficult given that many programs include limits on the interest rates, permissible compensation, and other fees that may be charged to borrowers. In the past, lenders would address this challenge by paying loan originators a smaller commission for loans with restrictions. The inability to do so today reduces the ability of companies to offer HFA loans and other specific products, particularly when producing these loans results in a loss. HFAs report that some lenders have left their programs, and others have limited the volume of their participation. The CFPB should address this dilemma through an exemption in the LO Comp rule for these loans.

(4) Finally, the CFPB should explore ways to generally simplify and clarify the LO Comp rule. The rule broadly prohibits compensation based on loan terms or proxies for terms while providing a short list of expressly permissible compensation factors. Clarity should be a primary focus and added to the regulation, including specifying a clear and precise list of impermissible compensation factors rather than the current approach of providing a short list of permissible factors and a vague and complicated “proxy for a term” analysis that serves to discourage everything else.

The current environment encourages different interpretations of an ambiguous test that unfairly disadvantages those companies that adhere closest to the CFPB’s rule. It is understood that some companies are not following the rule as it is currently being interpreted by our members and intended by the CFPB, and thus placing our members at a major disadvantage. The industry and consumers would be better served with clear, specific rules that are easy to follow, and easy to enforce. The Community Mortgage Lenders of America welcomes the opportunity to discuss the issues discussed in this letter.

Respectfully,

The Community Mortgage Lenders of America

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