

Testimony of

Stephen Hailer

on behalf of the

AMERICAN **BANKERS** ASSOCIATION

before the

Housing and Community Opportunity Subcommittee

Of the

Committee on Financial Services

United States House of Representatives

September 29, 2005



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Mr. Chairman and members of the Committee, my name is Stephen Hailer. I am president and CEO of the North Akron Savings Bank in Akron, Ohio. I am also vice chairman of the American Bankers Association's Housing and Federal Home Loan Bank Committee. ABA, on behalf of the more than two million men and women who work in the nation's banks, brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership – which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks – makes ABA the largest banking trade association in the country.

I am pleased to be here today to present the views of ABA on Title V of H.R. 1295, the Responsible Lending Act. Title V would establish licensing requirements and minimal federal requirements for independent mortgage brokers and, among other things, require background checks and continuing education of independent brokers. Section 503 of H.R. 1295 defines a mortgage broker as “a person who engages for compensation, either directly

or indirectly, in the acceptance of applications for mortgage loans for others, solicitation of mortgage loans on behalf of borrowers, or negotiation of terms or conditions of loans on behalf of borrowers or lenders.” Section 501 would not apply to brokers who perform work for banks or an affiliate of a bank, including those who fund, underwrite, service, or sell mortgage loans.

In particular, I would like to make three points in my testimony:

I. High Ethical Standards Benefit Everyone

Ensuring that consumers are treated fairly and receive high quality services is clearly in the interest of the entire mortgage industry, which depends upon the trust and patronage of homebuyers.

II. Banks are Subject to Rigorous Enforcement

The entire mortgage lending process performed by banks and their representatives is subject to a sophisticated umbrella of federal laws and regulations. The banking industry is subject to rigorous government oversight and examination. No comparable regulatory regime exists for independent mortgage brokers.

III. Extending Protections Already Required of Banks Makes Sense

Section 501 of H.R. 1295, which would create federal standards and licensing requirements for independent mortgage brokers, represents a practical means of extending existing protections for consumers beyond lenders.

ABA believes that practices that deceive, defraud, or otherwise take unfair advantage of consumers are predatory, and have no place in our financial system. Existing laws against these practices should be rigorously enforced. Practices that are routinely criticized – such as guaranteeing the borrower one loan rate and putting a second, higher rate in a mortgage contract are reprehensible – *and are already illegal*. ABA believes all parties to the home-buying process, whether independent or associated with a bank, should act responsibly and be held accountable when they do not do so. Therefore, ABA supports minimal federal requirements for independent mortgage brokers.

I. High Ethical Standards Benefit Everyone

The success or failure of any business depends upon the satisfaction of its customers. Mortgage lending is a vast enterprise, which requires the coordination of several layers of professionals throughout the process of issuing a home loan.

The U.S. mortgage market is more competitive than ever. Consumers have hundreds of lenders to choose from and even more brokers competing for their business. Reputation plays a large role in deciding which brokers succeed over the long-term. The damage caused by deceptive or unscrupulous sales practices extends beyond the consumer who is directly targeted. News and government reports of bad actors can destroy whole businesses and ruin reputations. In contrast, ethical and efficient brokers attract more customers and generate more business for themselves and lenders.

Mortgage brokers are a critical part of the home lending market because they account for a substantial percentage of all mortgage contracts – nearly two-thirds – and, next to real estate brokers, are likely the first person a homebuyer contacts after deciding to purchase a home. Mortgage brokers often serve as guides to the process of buying a home, providing important information to consumers about down payments, loan terms, and the mortgage-closing process. Brokers who work on behalf of banks frequently present buyers with customized packaged services, while independent mortgage brokers will “shop” mortgage prices and rates offered by a host of potential lenders. Regardless of the lender, brokers are responsible for fulfilling an essential job in the home-buying process: they bring buyers and lenders together. Only the highest ethical standards can preserve this vital relationship.

II. Banks are Subject to Rigorous Enforcement

Banks and the activities of mortgage brokers who act on banks’ behalf are heavily regulated and thoroughly examined for compliance with a host of federal laws and regulations. Because banks are subject to, and examined regularly for, compliance with a wide range of laws and regulations, they must hold all their employees and representatives to high standards. Banks are subject to the Truth in Lending Act, Home Mortgage Disclosure Act, the Equal Credit Opportunity Act, RESPA, and the Fair Lending Act, among other laws. Federal law contains numerous disclosure requirements relating to mortgage loans generally, and especially so-called high-cost loans. Additionally, continually updated regulatory guidance is enforced by a panoply of federal agencies.

A bank's liability for violations, which continues after consummation of the loan, provides an effective deterrent of unscrupulous behavior and the means to quickly detect outliers. Banks have an ongoing interest in ensuring that the loans made by their employees or contractors are fair, reasonable, and legitimate. In most instances, an ongoing financial interest also exists – the bank will either hold the loan in portfolio or sell it into the secondary market and could be subject to recourse should the loan quality deteriorate. In all instances, banks have a regulatory and reputational interest – their examiners will review their loan practices and hold them accountable for any violations of the many laws to which they are subject.

Independent *mortgage brokers are not subject* to the breadth of consumer protection law and regulations with which banks must comply and, importantly, a regulatory system does not exist to examine them for compliance even with those laws, such as RESPA, which do apply to them. In addition, because of the nature of their jobs, independent brokers may not have the same level of ongoing interest in the quality of the loan they process. Once the loan closes, and they are paid, they have no further financial interest in the loan or obligation to the borrower, although most want to preserve their reputation for long-term relationships.

To help illustrate the extent to which banks are examined for compliance with consumer protection laws, the Federal Deposit Insurance Corporation (FDIC) issues a 49-page examination manual to its examiners evaluating bank compliance with the Truth in Lending Act (TILA). The examination manual lists step-by-step procedures to evaluate bank

compliance with every aspect of TILA, instructing examiners to inspect the dating of loan documents, signatures, annual percentage rates “within the allowed tolerance of 1/8 of 1 percent for regular transactions,” and other mandatory disclosures. Banks are well aware of these requirements and actively train their employees and representatives for full compliance.

TILA requires banks to provide disclosures to applicants and borrowers disclosures about important terms in an easy to read format at different times in the mortgage process. Good faith estimates of these terms must be provided within three days of application. Final disclosures must be provided before the loan is consummated. Special “early” disclosures are required for home equity lines of credit. Failure to provide proper disclosures can mean significant potential liability for the creditor. In addition to damages and statutory damages, this liability may include loss of any security interest and the refund of all interest and other fees paid up to three years.

Banks, savings associations and credit unions are also subject to the Home Mortgage Disclosure Act (HMDA). They must report certain information on home mortgage loans that they originate, purchase or refinance. However, independent brokers are not required to report any information on the mortgage applications that they process, as insured depository institutions must. Not only must depository institutions report under HMDA, but bank examiners regularly inspect the institution’s loan files to determine whether the HMDA reporting was done correctly and also to review the loans for possible fair lending violations, if the institution’s HMDA numbers reveal unexplained disparities in lending, denials, pricing and other reported information.

Independent mortgage brokers, though not as heavily regulated, play a vital role in the mortgage lending industry. Many banks rely on brokers as their retail outlet. It is essential that all brokers be honest, trustworthy, and reliable. While some may seek to bring all participants in the lending process into a strict examination and compliance regime (expanding coverage and enforcement of many existing laws even to those who do not fund loans), we recognize that doing so would be expensive and would require significantly enhanced governmental resources.

III. Extending Protections Already Required of Banks Makes Sense

Title V of H.R. 1295 would address the present regulatory gap in current consumer protection law in a minimally obtrusive manner by requiring that independent brokers comply with minimum licensing requirements under either state or federal law and that a database of licensed brokers be created to allow consumers to gain useful information on any broker they may consider using. Forty-five states already require licensing of independent mortgage brokers. Uniform protections would help to ensure that all consumers are dealing with honest, fair, and trustworthy loan professionals. Licensing and the creation of a publicly available nationwide database would allow consumers to have a degree of confidence that the broker they are dealing with has met minimum standards of education and training, and would let them see if the broker has any criminal record.

We believe the licensing of independent brokers is a rational step toward better consumer protection. Additionally, it would enhance lenders' ability to screen brokers they

may seek to employ, further ensuring that lenders and consumers deal only with legitimate brokers.

Thank you. I would be happy to answer any questions you may have.